

IN THE MATTER OF
SHARP ELECTRONICS CORPORATION

SET ASIDE ORDER IN REGARD TO ALLEGED VIOLATION
OF THE FEDERAL TRADE COMMISSION ACTS

Docket C-2574. Consent Order, Oct. 9, 1974—Set Aside Order, Aug. 21, 1989

The Federal Trade Commission has set aside a 1974 consent order with Sharp Electronics Corporation, (84 FTC 743), because respondent satisfactorily demonstrated that changes in the law required such action, thus enabling respondent to maintain favorable relations with its full service dealers, and thereby develop and promote an efficient distribution system to compete more effectively with other electronic calculator manufacturers; as a result, consumers are likely to benefit.

ORDER REOPENING AND SETTING ASIDE ORDER
ISSUED ON OCTOBER 9, 1974

On April 25, 1989, Sharp Electronics Corporation ("Sharp") filed a "Request To Reopen The Proceeding And Set Aside The Order" ("Request"), pursuant to Section 5(b) of the Federal Trade Commission Act, 15 U.S.C. 45(b), and Section 2.51 of the Commission's Rules of Practice and Procedure, 16 CFR 2.51. The Request asks the Commission to reopen the proceeding and set aside the order issued by the Commission on October 9, 1974, in Docket No. C-2574, 84 FTC 743. The order prohibits Sharp from restricting in any manner the territories in which, or the customers to whom, its dealers may sell Sharp electronic calculators. In support of its request, Sharp argues that the order should be set aside to reflect changed conditions of law and fact and "to promote considerations of fairness and the public interest." Request at 6, 9. Sharp's request was placed on the public record for thirty days, pursuant to Section 2.51(c) of the Commission's Rules. No comments were received.

For the reasons discussed below, the Commission has concluded that Sharp has made a satisfactory showing of changed conditions of law that require reopening the proceeding and warrant modifying the order in the manner requested by Sharp. The Commission has therefore determined to reopen the proceeding and set aside the order in its entirety.

I.

The Commission issued its complaint in this matter on October 9, 1974. 84 FTC at 743-45. The complaint alleged that Sharp violated Section 5 of the Federal Trade Commission Act, by, among other things, prohibiting its dealers from selling Sharp electronic calculators outside of their "allotted" territories, and imposing restrictions "as to the persons or classes of persons" to whom Sharp dealers may sell such calculators. 84 FTC at 744. Sharp's distribution practices, as alleged in the complaint, "actually hindered, restricted, restrained and prevented competition . . .," and constituted "unfair acts . . . and methods of competition . . ." within the meaning of Section 5 of the FTC Act. *Id.*

The Commission's order, entered by consent, prohibits Sharp from imposing any territorial restrictions on its dealers, or defining the class of customers to whom they are permitted to sell Sharp electronic calculators. The order also prohibits Sharp from using any mandatory fixed schedules for the division of profit between any selling dealers and a dealer in whose territory the product is serviced that has the effect of restricting the territory in which electronic calculators may be sold. 84 FTC at 746.¹ However, the order explicitly permits Sharp to designate for its dealers geographical areas within which a dealer may agree to devote its best efforts to the sale of electronic calculators, engage in activities specifically rendered lawful by legislation enacted by Congress, require a dealer to undertake obligations of installation and warranty service, and require its dealers to comply with any voluntary profit passover program made available by Sharp. *Id.* at 746-47.

II.

Section 5(b) of the FTC Act, 15 U.S.C. 45(b), provides that the Commission shall reopen an order to consider whether it should be modified if the respondent "makes a satisfactory showing that changed conditions of law or fact" require such modification. A satisfactory showing sufficient to require reopening is made when a request to reopen identifies significant changes in circumstances and shows that the changes eliminate the need for the order, bring the

¹ For a period that expired in 1979, paragraph 5 of the order prohibited Sharp from establishing mandatory fixed schedules for the division of profit between any selling dealer and a dealer in whose territory the product is serviced, regardless of effects. *Id.*

order into conflict with current law, or make continued application of it inequitable or harmful to competition. *Louisiana-Pacific Corp.*, Docket No. C-2956, Letter to John C. Hart (June 5, 1986), at 4. See S. Rep. No. 96-500, 96th Cong., 2d Sess. 9 (1979) (significant changes or changes causing unfair disadvantage); *Phillips Petroleum Co.*, Docket No. C-1088, 78 FTC 1573, 1575 (1971) (no modification for changes reasonably foreseeable at time of consent negotiations); *Pay Less Drug Stores Northwest, Inc.*, Docket No. C-3039, Letter to H. B. Hummelt (Jan 22, 1982) (changed conditions must be unforeseeable, create severe competitive hardship, and eliminate dangers that the order sought to remedy); see also *United States v. Swift & Co.*, 286 U.S. 106, 119 (1932) (modification warranted by "clear showing" of changes that eliminate reasons for order or such that the order causes unanticipated hardship).

The language of Section 5(b) plainly anticipates that the burden is on the petitioner to make the requisite satisfactory showing of changed conditions to obtain reopening of the order. The legislative history also makes clear that the petitioner has the burden of showing, other than by conclusory statements, why changed circumstances require that the order should be modified.² If the Commission determines that the petitioner has made the necessary showing, the Commission must reopen the order to consider whether modification is required and, if so, the nature and extent of the modification. The Commission is not required to reopen the order, however, if the petitioner fails to meet its burden of making the satisfactory showing required by the statute. The petitioner's burden is not a light one given the public interest in the finality of Commission orders. See *Federated Department Stores, Inc. v. Moitie*, 425 U.S. 394 (1981) (strong public interest considerations support repose and finality).

III.

Based on the information provided by Sharp and other available information, the Commission has determined that Sharp has made a satisfactory showing that changes in law require reopening the proceeding and warrant setting aside the order. Having reopened and set aside the order on the basis of change of law, the Commission does

² The Commission may properly decline to reopen an order if a request is "merely conclusory or otherwise fails to set forth specific facts demonstrating in detail the nature of the changed conditions and the reasons why these changed conditions require the requested modification of the order." S. Rep. No. 96-500, 96th Cong., 1st Sess. 9-10 (1979).

not reach the issue whether reopening is also warranted based upon the changes of fact or the public interest considerations asserted by Sharp.

In 1974, when this consent order was issued, all vertical restraints were considered *per se* unlawful, based on *U.S. v. Arnold Schwinn & Co.*, 388 U.S. 365 (1967). Three years after the order was issued, the Supreme Court overruled *Schwinn* in *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36 (1977), stating that territorial restrictions and other nonprice vertical restraints are not inherently anticompetitive, and should be analyzed under the rule of reason.³ The Court said that nonprice vertical restraints had the potential to “promote interbrand competition by allowing the manufacturer to achieve certain efficiencies in the distribution of his products.” 433 U.S. at 54. One such efficiency that the Court expressly recognized was the use of such restraints to permit suppliers “to induce retailers to engage in promotional activities or to provide service and repair facilities necessary to the efficient marketing of their products.” *Id.* at 55. Subsequent cases have reaffirmed that nonprice vertical restraints, in the absence of further agreement on price or price levels to be charged by distributors, are to be analyzed under the rule of reason. See *Business Electronics Corp. v. Sharp Electronics Corp.*, 108 S. Ct. 1515 (1988); *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752, 762-63 (1984).

Sharp has identified *Sylvania* as a change in the law of nonprice vertical restraints from a *per se* to a rule of reason analysis. However, this showing alone, without a further showing that the order’s prohibitions cannot be justified under current law, would be insufficient to require reopening. This is because the challenged vertical restrictions, although not *per se* unlawful, may nonetheless be unreasonable. If so, the order’s prohibitions would be consistent with existing law.

The Commission has previously relied upon *Sylvania* to conclude that only nonprice vertical restraints having “a probable adverse effect on *interbrand* competition” at either the manufacturer or dealer level are unlawful.⁴ The Commission has also stated that “[w]hen the exercise of market power in a properly defined relevant market is unlikely, the Commission considers non-price vertical

³ *Sylvania* did not change the *per se* rule against resale price maintenance.

⁴ *TEAC Corp. of America*, 104 FTC 634, 635 (1984) (emphasis in original), citing *Bellone Electronics Corporation*, 100 FTC 68, 208 (1982).

restraints to be efficiency-enhancing in purpose and effect, and therefore lawful, without further inquiry.”⁵

In its request, Sharp has shown that, under the rule of reason analysis that the Commission applies to nonprice vertical restraints, there is no basis for continuing the order’s prohibitions. Competitive conditions in the electronic calculator industry today make it unlikely that nonprice vertical restraints could be used to create or enhance market power or facilitate collusion. Today, more than twenty major calculator suppliers compete in the United States, none of which appears to have a controlling share of the market.⁶ The structure of the distribution and retailing segments appears to be even more diffuse. There also appear to be no significant impediments to entry into the market for the supply of electronic calculators. Sharp has shown that, since 1974, at least ten new suppliers have entered the calculator market. Similarly, there is no evidence of impediments to entry into the distribution or retailing of electronic calculators. In general, the market today appears to be competitive. The number of available model types has increased substantially, and retail prices⁷ and supplier profit margins have decreased, since the order was issued.⁸ Given existing levels of concentration, the absence of significant entry impediments, and the apparent competition in the sale of electronic calculators, it appears unlikely that Sharp’s use of nonprice vertical territorial or customer restraints would significantly restrict interbrand competition and reduce output. Therefore, Sharp has made a sufficient showing to justify reopening the order.

As to relief on the merits, the Commission is not aware of any facts or of any public interest considerations that weigh against setting aside the order in this matter. The petitioner has demonstrated that

⁵ *TEAC Corp. of America*, 104 FTC 634, 635-36 (1984).

⁶ Assuming the United States electronic calculator industry to be a relevant market, Sharp’s estimated current share is less than twelve percent; its largest competitor is estimated to have no more than fifteen percent of such a market. Maul Affidavit at ¶ 6.

⁷ The prices of Sharp’s calculators ranged from \$500 to \$1,000 in 1972, and from \$150 to \$300 in 1982 when it became involved in the *Business Electronics* litigation. *Business Electronics Corp. v. Sharp Electronics Corp.*, 780 F.2d 1212, 1221 n.2 (5th Cir. 1986), *aff’d*, 108 S. Ct. 1515 (1988).

⁸ These changes in the market were acknowledged in Judge Jones’ concurring opinion in *Business Electronics* as follows:

Only atavistic devotees of the abacus or slide rule could fail to recall the remarkable history of the electronic calculator market during the last fifteen years. The range of available models, variety of functions that can be performed, and myriad optional enhancements have multiplied rapidly while the average prices have plummeted. The number of competing manufacturers has increased. To maintain their market position and profitability, manufacturers like Sharp have obviously been required to react quickly and imaginatively to changes in the marketplace.

relief is appropriate. Elimination of the order's prohibitions will enable Sharp to maintain and promote an efficient distribution system. Sharp's inability to ban transshipping and to require its dealers to observe territorial restrictions could cause Sharp significant competitive injury by, among other things, lessening the efficiency of Sharp's distribution system and discouraging it from making necessary investments to promote sophisticated products and provide application support and training to potential customers.⁹ Setting aside the order will allow Sharp to compete more effectively with other electronic calculator manufacturers, and consumers are likely to benefit.

IV.

Accordingly, *it is ordered*, that this matter be reopened and that the Commission's order in Docket No. C-2574, issued on October 9, 1974, be, and it hereby is, set aside, as of the date of service of this order. Commissioner Strenio did not participate by reason of absence.

⁹ According to Sharp, its competitors are able to prevent free-riders from "disturbing the orderly distribution of their products" by full service dealers through such restraints as prohibiting mail order sales and sales to

IN THE MATTER OF
MOTOR TRANSPORT ASSOCIATION OF CONNECTICUT, INC.
FINAL ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATION OF
SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

Docket 9186. Complaint, Sept. 18, 1984—Final Order, Aug. 25, 1989

This final order dismisses the complaint against the respondent, which represents approximately 585 competing motor carriers and files collective rates for its common carrier members with the state regulatory agency.

Appearances

For the Commission: *Michael E. Antalics, Phoebe D. Morse, Jerry A. Philpott and John H. Seesel.*

For the respondent: *Gerald A. Joseloff, Joseloff, Joseloff & Cramer, Wethersfield, Ct.*

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that Motor Transport Association of Connecticut, Inc., a corporation, hereinafter sometimes referred to as "respondent," has violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges as follows:

For the purposes of this complaint the use of the present tense includes the past tense and the following definitions apply:

"*Carrier*" means a common carrier of property by motor vehicle.

"*Intrastate transportation*" means the pickup or receipt, transportation and delivery of property for compensation wholly within any state of the United States by a carrier authorized by that state to engage therein.

"*Tariff*" means a publication and any supplements thereto stating the rates of a carrier for the intrastate transportation of property, excluding general rules and regulations.

"*Member*" means any carrier or other person that pays dues or belongs to Motor Transport Association of Connecticut, Inc., or to any successor corporation.

"*Rate*" means a charge, payment or fixed price according to a ratio, scale or standard for direct or indirect transportation service.

"*Collective rate*" means any rate or charge established under any contract, agreement, understanding, plan, program, combination or conspiracy between two or more competing carriers, or between any carrier and respondent.

PARAGRAPH 1. Respondent, Motor Transport Association of Connecticut, Inc., is a corporation organized, existing and doing business under and by virtue of the laws of Connecticut, with its office and principal place of business located at 508 Tolland Street, East Hartford, Connecticut. Respondent publishes and issues tariffs containing rates for the intrastate transportation of property on behalf of its member carriers.

PAR. 2. Carriers engaging in intrastate transportation of property within Connecticut do so under certificates of public convenience and necessity granted by the Connecticut Department of Public Utility Control. Such carriers are subject to rate regulation by the Department and are required to charge just and reasonable rates. Carriers in Connecticut are required to charge the rates filed once they have been accepted by the Department.

PAR. 3. The statute which provides for regulation of carriers engaged in the intrastate transportation of property within Connecticut does not compel, command, authorize or otherwise provide for the establishment, operation or continuation of collective rates among carriers or others on their behalf.

PAR. 4. Except to the extent that competition has been restrained as herein alleged, respondent's members are now in competition among themselves and with other carriers.

PAR. 5. Respondent's membership consists of approximately 360 carriers engaging in intrastate transportation of property within Connecticut. Respondent's members are entitled to and do, among other things, vote for and elect the officers and directors of respondent. The control, direction and management of respondent are vested in the Board of Directors, which employs a general manager who acts as chief administrative officer of the corporation with direct charge of and supervision over the affairs of the corporation.

PAR. 6. The acts and practices of respondent set forth in paragraph

eight are in or affecting commerce as "commerce" is defined in the Federal Trade Commission Act, as amended, and respondent is subject to the jurisdiction of the Federal Trade Commission. Respondent's acts and practices:

(A) Affect the flow of substantial sums of money across state lines from businesses and other private parties to respondent's members for rendering intrastate transportation services;

(B) Affect respondent's members' purchase and use of equipment and other goods and services which are shipped across state lines; and

(C) Are supported by the receipt of dues and fees which are sent across state lines.

PAR. 7. Shippers use the intrastate services of respondent's members to transport property from warehouses and distribution centers in Connecticut to customers in Connecticut, which property was originally shipped into Connecticut from other states. For such intrastate deliveries of property from warehouses and distribution centers, carriers charge shippers or shippers' customers the intrastate rates published by respondent. These intrastate shipping charges are factors which influence the prices of such property. The intrastate delivery services of these carriers are an essential and integral part of the interstate business transactions of such shippers. Thus, the activities of these carriers have a substantial and direct effect upon interstate commerce.

PAR. 8. Respondent, its members, officers, directors, and others are engaging in a combination, conspiracy, agreement, concerted action or unfair and unlawful acts, policies and practices, the purpose or effect of which is to unlawfully hinder, restrain, restrict, suppress or eliminate competition among carriers engaged in the intrastate transportation of property within Connecticut.

Pursuant to and in furtherance thereof, respondent, its members and others engage in the following acts, policies and practices, among others:

(A) Initiating, preparing, developing, disseminating, and taking other actions to establish and maintain collective rates for the intrastate transportation of property within Connecticut;

(B) Participating in the collective rates; and

(C) Filing collective rates with the Connecticut Department of Public Utility Control.

PAR. 9. The acts and practices of respondent, its members and others as alleged in paragraph eight have the effect of:

(A) Fixing, stabilizing, raising, maintaining, or otherwise interfering or tampering with the rates charged by carriers for the intrastate transportation of property within Connecticut;

(B) Restricting, restraining, hindering, preventing or frustrating rate competition among carriers for the intrastate transportation of property within Connecticut;

(C) Depriving shippers patronizing carriers for intrastate transportation of property within Connecticut of the benefits of free and open competition in the provision of said services; and

(D) Depriving consumers in Connecticut of the benefits of free and open competition in the intrastate transportation of property.

PAR. 10. The acts, policies and practices of respondent, its members and others, as herein alleged, are all to the prejudice and injury of the public and constitute unfair methods of competition in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act, as amended. The acts and practices of respondent, as herein alleged, are continuing and will continue in the absence of the relief herein requested.

INITIAL DECISION BY

JAMES P. TIMONY, ADMINISTRATIVE LAW JUDGE

JANUARY 9, 1987

I. INTRODUCTION

Respondent Motor Transport Association of Connecticut, Inc., ("MTAC") is a rate bureau¹ engaged in collective ratemaking for its motor carrier members. It submits to the Connecticut regulatory agency joint rate proposals on trucking prices for hauls within Connecticut of four types of commodities: general commodities, household goods, bulk commodities in dump trucks and liquid bulk products in tank trucks.

II. SUMMARY OF PROCEEDINGS

On September 18, 1984, the Commission issued its complaint charging respondent, its members, and others with an unlawful

¹ For a general description of the nature of the industry, see *Southern Motor Carriers Rate Conference, Inc. v. United States*, 105 S.Ct. 1721 (1985); and *Massachusetts Furniture & Piano Movers, Inc.*, 102 FTC 1176, 1209 (1983), *rev'd on other grounds*, 773 F.2d 391 (1st Cir. 1985), (referred to herein as "*Mass. Movers*").

combination involving the developing and filing of collective rates with the state regulatory agency.

Respondent's answer dated October 31, 1984, admitted certain corporate facts but denied all jurisdictional facts and substantive allegations of the complaint. In addition, respondent raised thirteen defenses to the complaint. Respondent moved to amend its Answer to add a fourteenth defense but the motion was denied on May 1, 1985.

Complaint counsel moved to stay this matter pending the disposition of *Mass. Movers*, and the motion was granted on June 17, 1985. This case was assigned to me on October 1, 1986. By order dated October 9, 1986, trial was set for January 5, 1987. Respondent moved to stay proceedings pending the disposition by the Commission of *New England Motor Rate Bureau, Inc.*, Docket No. 9170. The motion was denied on November 18, 1986. The parties thereafter agreed to stipulate the record, filing a stipulation of facts and exhibits. The trial was therefore cancelled and the record closed. Order of November 24, 1986. [3]

III. FINDINGS OF FACT

A. Respondent

1. Motor Transport Association of Connecticut, Inc., is a corporation organized, existing and doing business under the laws of the State of Connecticut. Stipulation filed November 17, 1986, paragraph number 1.²

2. MTAC's members engage in the intrastate transportation of property by motor vehicle in Connecticut. (S. 2)

3. MTAC has approximately 585 competing motor carrier members. Answer ¶¶ 9, 10.

4. Intrastate common carriers of property by motor vehicle in Connecticut operate under certificates of public convenience and necessity granted by the State of Connecticut. (S. 3)

5. MTAC was formed in 1920 and incorporated in 1930. Its purpose was to promote and preserve the advantage of highway transportation; promote economical and efficient service by motor truck; promote safety of operation on the highways; promote and support necessary and beneficial legislation; and engage in any other activities that will benefit the welfare of highway transportation and the public generally. (S. 4)

²The stipulation will be referred to as "S." followed by a number designating the paragraph of the stipulation.

6. MTAC issues tariffs and supplements thereto ("MTAC tariffs") in which it publishes intrastate rates on behalf of some of its motor common carrier members engaged in intrastate transportation of property within the State of Connecticut. (S. 5)

7. Any motor carrier may become an active member of MTAC. (S. 6)

8. MTAC's active members are entitled to, and do, among other things, vote for and elect the directors of MTAC. The control, direction and management of MTAC is vested in its Board of Directors. The President is the chief executive officer of MTAC. (S. 7)

9. At its annual meeting MTAC's membership approves and ratifies the actions of MTAC, its directors and officers, since the last annual membership meeting. (S. 8) [4]

10. Officers and directors of MTAC must be representatives of active members. (S. 9)

11. MTAC's President is John E. Blasko. Prior to becoming President, Mr. Blasko was Executive Vice President and General Manager of MTAC for 16 years. His duties in all three capacities were the same: complete control of MTAC's office, employees, records, and property; managing the day-to-day operations of MTAC; and lobbying for the industry. (S. 10)

B. *FTC Jurisdiction*

12. MTAC does not possess a certificate of public convenience and necessity from the Interstate Commerce Commission. (S. 22) MTAC does not engage in the transportation of goods. (S. 23)

13. MTAC actively promotes the economic benefit of its members. (Findings 25-39)³

C. *Commerce*

14. Seventy-five to 100 of MTAC's active members are located outside the State of Connecticut. The majority of these are motor carriers. (S. 11)

15. MTAC renders its out-of-state members services for which it charges a fee. (S. 12)

16. MTAC's out-of-state members pay substantial amounts of money for dues and for fees for services performed by MTAC. These monies are transmitted across state lines to MTAC's offices in Connecticut. (S. 13)

³ Findings are referred to herein as "F." followed by the number of the finding.

17. MTAC purchases goods and services from people or firms located outside Connecticut. (S. 14)

18. MTAC holds some of its conventions of its membership outside Connecticut and expends funds for that purpose. (S. 15)

19. Carrier members of MTAC transport substantial numbers of shipments that originate and terminate within Connecticut for private shippers or receivers with headquarters and principal places of business located outside Connecticut. The rates charged for these shipments are governed by MTAC tariffs. (S. 16)

20. Some of MTAC's carrier members transmit bills for intrastate transportation services to private shippers or receivers at their headquarters and principal places of business outside Connecticut. (S. 17)

21. The private shippers or receivers for whom property is transported within Connecticut by carrier members of MTAC under rates in MTAC tariffs, which shippers or receivers have their headquarters and principal places of business outside Connecticut, transmit to said carrier members of MTAC substantial sums of money in payment for the intrastate transportation services rendered. (S. 18)

22. MTAC members located in Connecticut transport substantial quantities of general commodities of property from warehouses and distribution centers located within Connecticut to customers located within Connecticut, which property had been transported from origin points outside Connecticut to such warehouses and distribution centers for distribution within Connecticut or distribution in other states. In many cases MTAC members charge shippers or shippers' customers the intrastate rates contained in the MTAC tariffs for the intrastate transportation of these general commodities of property from warehouses and distribution centers. (S. 19)

23. Some MTAC members located in Connecticut purchase substantial amounts of equipment and other goods for use in their transportation business, including their intrastate transportation business, from private businesses with headquarters and principal places of business located outside of Connecticut, and the equipment and other goods are transported into Connecticut. (S. 20)

24. Some MTAC members located in Connecticut transmit substantial sums of money in payment for equipment and other goods purchased for use in their transportation business, including their intrastate transportation business, to private businesses from whom the equipment and other goods were purchased, whose headquarters

and principal places of business are located outside Connecticut. (S. 21)

D. Conduct

25. MTAC files proposed tariffs with the Connecticut Department of Public Utility Control ("DPUC") on behalf of its members. (S. 24) [6]

26. Subsequent to DPUC approval, rates published in a MTAC tariff are charged for intrastate shipments within Connecticut to shippers using the services of MTAC members that participate in that MTAC tariff. (S. 28)

27. MTAC acts on behalf of its members pursuant to written powers of attorney. DPUC requires that a carrier desiring to have an agent issue and file its tariffs execute a document citing such appointment. (S. 29; Joint Exhibit 1)⁴

28. MTAC files four different tariffs: (1) the Local and Joint Tariff of Class and Commodity Rates Applying Between Points in Connecticut ("General Commodities Tariff"), which the New England Motor Rate Bureau, Inc. ("NEMRB"), issues and files in conjunction with MTAC; (2) the Local Commodity Tariff Applying On Transportation of Liquid Commodities in Bulk, in Tank Trucks, Between All Points In Connecticut ("Bulk Liquid Tariff"); (3) the Motor Freight Tariff of Local Commodity Rates Applying On Dump Truck Service Between Points Within Connecticut ("Dump Truck Tariff"); and (4) the Motor Freight Tariff of Local Commodity Rates Applying On Household Goods Between All Points in Connecticut ("Household Goods Tariff"). (S. 30; JX 2, JX 3, JX 4, JX 5)

29. The Bulk Liquid Tariff, Dump Truck Tariff and Household Goods Tariff are issued by MTAC without the involvement of NEMRB. (JX 3a, JX 4a, JX 5a)

30. At all relevant times, two or more members of MTAC have participated in the rates set by each of the MTAC tariffs. (S. 31)

31. In general, each MTAC tariff sets out rules and definitions for computing the rates applicable to any given movement of freight covered by the tariff, contains tables standardizing distance computations, and contains tables of rates applicable to movements and to ancillary services. For example, a rule in the General Commodities Tariff defines what collection and delivery services are included in the basic movement rates and specifies a minimum charge and a per

⁴ The Joint Exhibits attached to and incorporated by reference into the Stipulation filed November 17, 1986 are referred to herein as "JX" followed by the exhibit number.

pound rate for collection or delivery beyond the defined area under various specified conditions. Other rules govern the applicability of waiting time, demurrage, storage and other special charges and set minimum or standard charges for these and other ancillary services. (S. 32)

32. The General Commodities Tariff specifies rates per pound and minimum charges for commodities grouped by "class" and [7] by standardized distance "scale numbers." There are five basic classes, as defined in the Coordinated Freight Classification issued by NEMRB, over which MTAC has no control or authority. There are also several "levels" of class rates, which are multiples of class rates. Thus, for any given quantity of any given product covered by the Coordinated Freight Classification there is a specific rate per pound corresponding to the standardized distance between the pickup and delivery points, unless the specified minimum charge applies. To illustrate, effective February 15, 1980, for movements of any less-than-truckload shipment of 500 to 1,999 pounds of any class 5 product between Hartford and New Haven the rate was \$2.89 per hundred pounds over the line of any participating carrier. At that time 14 of the approximately 174 carriers that participated in that tariff took exception to this rate and, as shown in the tariff itself, applied a higher rate of \$3.61 per hundred pounds to the same shipment. At 500 pounds, minimum charges do not appear to be a factor. (S. 33; JX 2)

33. The Household Goods Tariff specifies three or more different sets of rates to be charged by all participating carriers. First, for ancillary services such as packing and unpacking, a rate is specified for each type of service. Second, for moves of twenty miles or less, each participating carrier elects one of several tables of transportation rates per hour for a truck of a certain size with a driver and with or without helpers, with separate tables for normal business hour rates and overtime hour rates. To illustrate, in the tariff effective February 21, 1983, 28 carriers elected table VI which listed a rate of \$22.55 per hour during normal business hours for a vehicle not exceeding 700 cubic feet and a driver and \$11.50 per hour for each helper. At that time, ten carriers elected table VII and three elected table VIII, which had higher rates for vehicle and driver of \$26.20 and \$31.30 per hour, respectively, and for helper of \$13.40 and \$15.00 per hour, respectively. Eleven carriers elected lower priced tables. Third, for moves of over twenty miles, mileage rates applicable to all participating carriers are

specified. To illustrate, to load and unload one ton of household goods valued at no more than \$.60 per pound and move it 105 miles within Connecticut, the rate in the tariff effective February 21, 1983, was \$17.17 per hundred pounds or \$343.40 over the lines of all participating carriers. (S. 34; JX 3)

34. The Bulk Liquids Tariff specifies rates per gallon for particular classes of bulk liquids transported by participating carriers between named points in Connecticut or per mile between any other points in Connecticut. To illustrate, in the tariff effective March 15, 1983, in which eleven carriers participated as to gasoline, exclusive of dedicated continuous service, the rate for hauling gasoline between Bridgeport and Hartford was \$.0235 per gallon, subject to a minimum of 7500 gallons per truck [8] or a minimum charge of not less than \$70.80 for a smaller truck. Different rates applied to different bulk liquids. (S. 35; JX 4)

35. The Dump Truck Tariff specifies rates per mile or hour, minimum shipments, demurrage charges and other rules for specific materials to be hauled by participating carriers. To illustrate, the regular time rate for hauling six ton or larger loads of commercial crushed stone, commercial sand or commercial gravel between any two points in Connecticut in the tariff effective May 12, 1986, was \$1.35 per ton for the first four miles and \$.17 per ton for each additional mile for 79 of the 105 carriers participating. (S. 36; JX 5)

36. Starting in 1959, pursuant to Connecticut law and in response to a petition by MTAC and others, DPUC has periodically issued minimum rate orders pertaining to rates that may be charged for the carriage of general commodities. Under the minimum rate orders, carriers whose tariffs are below the minimum rates are required to increase their rates unless they successfully petition for an exemption. Over 50 carriers have filed petitions for exemption from a minimum rate order. Competing carriers may protest any exemption. The function of a minimum rate order is to set a floor on rates. (S. 38; JX 6, JX 7)

37. MTAC petitioned DPUC to impose a minimum rate order on general commodities in 1958, seeking "a stabilization of rates and charges for motor common carriers authorized to transport general commodities between points in Connecticut." (JX 6d) It further requested that the Commission prescribe a "single hourly rate schedule for the purpose of obtaining uniformity in rates to be applied by carriers performing intrastate transportation service in Connecticut." (JX 6p)

38. MTAC has petitioned DPUC from time to time on behalf of some of MTAC's general commodity carrier members to increase the minimum rate order that sets a floor on intrastate general commodity rates. (JX 7b, i, j) For example, on August 18, 1983, MTAC petitioned DPUC for an increase in minimum rates of approximately 25%. (S. 39; JX 7a-b)

39. MTAC has intervened in opposition to petitions by individual carriers to seek permission to charge less than the minimum rate order. (JX 16q)

E. Active State Supervision

40. Effective in October 1986, DPUC had appointed Edward Regan, formerly head of the Transportation Division, the head and [9] supervisor of the Tariff Division (JX 12) and reporting to him are two rate analysts who review tariffs filed by MTAC and others, Thomas J. Brookman and Joseph Bystrowski. (S. 46, 55)

41. All common carriers are required to file a tariff with DPUC. When a proposed tariff is received by DPUC, it is reviewed by one of these rate analysts, who stamps it as received, ascertains that powers of attorney for the carriers participating are correct, compares the requested rates to the previous ones, assures that they are above the ones in the minimum rate orders, if applicable, and places the tariff on the public record for 30 days unless it is merely a carrier adopting a bureau tariff, in which case only one day's notice is required. The rate analyst may also refuse to place it on the public record if it does not satisfy these and other requirements set forth herein. Other than DPUC regulations, there are no published standards for review of tariffs. If the increases are less than 5% and there are no errors or corrections, the tariff is approved without a hearing unless there is a protest. If there is a protest, the tariff is suspended and a public hearing may be held. Except for hearings on minimum rate orders and petitions for exemption for the minimum rate orders, there have been few public hearings in the last sixteen years. When a hearing is held, witnesses for the tariff proponent testify as to the need for an increase. Normally, there is little opposition and the hearing takes one day. Frequently, the petitioner refiles in an effort to satisfy the DPUC rate analyst. (S. 46, 56, 60, 69; JX 8g)

42. Between 1980 and 1983, DPUC's accounting division reviewed a tariff filing only if a rate analyst requested such a review. Since 1983, as a result of an internal policy review, the accounting division has taken a larger role. (S. 47)

43. If the tariff becomes effective without a rejection, suspension or hearing, that action results from an opinion of the rate analyst that the proposed rates meet the requirements of the statutes and regulations. (S. 49)

44. If a rate increase is for more than 5%, DPUC requires that it be accompanied by financial information designed to justify the reasonableness of the increase, consisting of the proponent's operating revenues, operating expenses, tonnage and revenue to be generated, a *pro forma* operating statement and net operating income. DPUC generally regards an operating ratio (operating expenses divided by operating revenues) of 93% as reasonable. If a tariff affects more than one carrier, a cross section of carriers affected may be used for purposes of analyzing operating ratios. (S. 50, 62, 68; JX 9, JX 10)

45. Since 1957 DPUC has not initiated a minimum rate order review. It has responded to carrier petitions to initiate or increase minimum rates, all of which have been submitted by NEMRB [10] jointly with MTAC. Since then it has issued about twelve additional minimum rate orders in response to carrier petitions. (S. 51; JX 6, JX 7)

46. The Minimum Rate Order issued in 1959 (JX 6) pertains to General Commodities and does not affect the Bulk Liquid Tariff, Dump Truck Tariff or Household Goods Tariff. (JX 6d, m)

47. DPUC does not review carrier decisions to move from one table to another in the Household Goods Tariff, but it does review any change in the tables themselves. (S. 52)

48. Aside from its role in reviewing proposed rate increases, DPUC does not monitor conditions in the intrastate trucking industry in Connecticut (except for safety, insurance, and issuance of stamps (license fees)). (S. 53)

49. DPUC has permitted tariffs to become effective without suspension or hearing. (S. 64; JX 7a)

50. If a tariff rate, charge or rule is set down for a hearing, a legal notice is issued by the DPUC and published in selected Connecticut newspapers of general circulation. (S. 65)

51. Rate analysts in the DPUC submit written recommendations with respect to applications for changes in tariff on all matters that go to a hearing. A written recommendation is also submitted when a matter is not set down for a hearing. (S. 66; JX 15)

52. Any change in the rates and charges filed with DPUC must be held in abeyance for 30 days to permit DPUC to review the rate filings

and permit public comment, except that a shorter period is permissible when such change is to enable the carrier to meet the rate of a competing carrier. (S. 67)

53. If the tariff submitted to DPUC is below the minimum rate order or orders, the carrier must file a petition for exemption in which event the tariff is suspended. (JX 16) A hearing may be held to justify the proposed rate. (S. 69)

54. When a proposal for a general rate increase is submitted by a rate bureau such as MTAC, it must be accompanied by an elaborate justification statement. (F. 44) This justification statement is thoroughly analyzed by the tariff section as well as the audit section of the Commission and a written recommendation is prepared for submission to the Commission. (S. 70)

55. There are about 400 carriers having intrastate rights in Connecticut. If each were to file individual tariffs, in the opinion of DPUC it would be impossible for DPUC to process them without a tremendous increase in its staff and a substantial increase of its budget. (S. 74) [11]

56. The DPUC has the power to prescribe minimum rates and does prescribe them, either on its own motion or upon petition by an interested party. (S. 57, S. 58; JX 8w)

57. When a tariff is filed it is always checked to determine whether it is the same, below or above the minimum rate orders and whether it should be suspended, rejected, returned for errors or corrections or set down for a hearing. The DPUC has rejected some tariffs filed by independent carriers. (S. 59; JX 13d, e)

58. The tariff is processed initially by the tariff section of the DPUC. It always refers a carrier with new authority to the audit section to consider and analyze the financial information submitted. (S. 60)

59. An application for operating rights must be accompanied by a proposed tariff, and its rates are always checked by the tariff section to determine if they are at least equal to or above the minimum rate order at the time. (S. 61)

60. The DPUC has issued several citations for charging rates different than the rate in the tariff. (S. 63; JX 14)

61. If a tariff submitted is above the minimum rate order and the increase is substantial (over 5%) the tariff is checked, the carrier is notified, and the tariff is suspended pending a conference or hearing. If the carrier makes corrections or adjustments satisfying to the tariff section, it is accepted and no hearing is required. (S. 68)

62. Whenever operating rights are transferred, an informal conference is required between the tariff section of the DPUC and the selling carrier at which conference the rates of the selling carrier are checked for compliance with the statutes and regulations. (S. 71)

63. Whenever a complaint by a shipper or another carrier affecting rates is filed, the matter is investigated. If any violation is found the carrier is required to cease and desist immediately and to make the required corrections or rebates if that is indicated. The shipper is always kept informed. (S. 72; JX 17)

64. If a carrier does not obey an order to cease and desist violations of the statutes or regulations, a citation is issued requiring compliance. Penalties are usually imposed if a violation is found. (S. 73)

65. DPUC, in a formal opinion dated February 9, 1975, approved a petition to increase rates for transportation of general commodities, after a hearing. (JX 7z-4) In an opinion dated December 5, 1977 another rate increase on transportation of [12] general commodities was granted after a hearing. (JX 7v) In an opinion dated March 3, 1979 another petition for rate increase was denied after hearing. (JX 7r) In an opinion dated December 14, 1979, a petition for rate increase was granted after hearing. (JX 7r) The next petition for a rate increase was not filed until August 18, 1983, and it was approved on October 5, 1983, without a hearing, since it involved only the smallest carriers, who continually have cash flow problems, and because many of the carriers had gone bankrupt in the past several years or had relinquished their certificates. (S. 38; JX 7a, c)

F. *Legislative Intent*

66. The DPUC is empowered to prescribe maximum and minimum rates and may prescribe reasonable regulations therefor; rates and charges "shall be just and reasonable and reasonably compensatory, except that a rate may be established to meet the existing rate of a competing rate of a motor common carrier or a common carrier not subject to this chapter." (JX 8g Sec 16-287(a))

67. Motor common carriers of freight may agree to establish joint rates. If the carriers fail to agree, the DPUC shall, after hearing, establish by order such a division. (JX 8g Sec 16-287(b))

68. Discrimination in rates is prohibited, "nor shall any carrier refund or remit in any matter any portion of a rate so specified, nor give any unreasonable preference or advantage to any person—nor subject any person to any unreasonable prejudice or discrimination." (JX 8u Sec 16-288)

69. Rates may be changed only after a thirty day notice to the public; the DPUC may on its own initiative or upon protest hold a hearing on any rate changes and "may allow or disallow or prescribe the rate or rates." This statute further provides that the change in rate may become effective upon the effective date of the rate of the competing motor common carrier. (JX 8v Sec 16-289)

70. Any motor carrier who charges less than the regular rates on file shall be fined not more than \$500.00 for each offense. (JX 8x, y Sec 16-306)

71. The DPUC has been granted wide regulatory authority over the rates, certification, routes, speed, service, financial responsibility, insurance, liability, accounting and record keeping, safety and equipment of motor carriers, and has exercised that authority by rule making. (JX 8w, x Sec 16-304, JX 9a-i) [13]

IV. DISCUSSION

In its Answer to the Complaint, respondent raised thirteen affirmative defenses. All of these defenses were raised by the respondent in a very similar case, *The New England Motor Rate Bureau, Inc.*, Docket No. 9170, and were dismissed by Chief Judge Ernest G. Barnes in his Initial Decision dated December 12, 1986 and Order dated March 7, 1986. Furthermore, except for arguments that respondent is not engaged in price fixing and that the state action doctrine applies, these other defenses have not been briefed and, therefore, need not be decided. *Hospital Corporation of America v. Federal Trade Commission*, — F.2d — (7th Cir. 1986) (decided December 18, 1986), slip opinion at pp. 19-20.

A. Price Fixing

Respondent MTAC is a rate bureau composed of competing common carriers operating in the State of Connecticut. (Answer ¶ 6) The rate bureau, on behalf of 585 competing carriers (Answer ¶¶ 9, 10), submits joint rate proposals to the Connecticut Department of Public Utility Control which has authority over motor carrier rates within the State of Connecticut. (Answer ¶ 6) The members elect the directors of MTAC and the directors control and direct MTAC. (F. 8) Officers and directors are representatives of members of MTAC. (F. 10) MTAC acts on behalf of its members. (F. 27) MTAC has petitioned DPUC on behalf of its members to increase the rates charged for transportation of commodities in the State of Connecticut. (F. 36-38, 65)

MTAC initiates minimum rate orders by petitioning the state. (F. 37) The function of a minimum rate order is to set a floor on rates. (F. 36) Carriers can petition for exemptions from the minimum rate order (F. 53), and competing carriers can protest the exemption. (F. 36) MTAC can also protest. (F. 39)

The general commodities tariff states the rates at which commodities may be transported within Connecticut. (JX 2; F. 32) MTAC publishes three other tariffs: the Bulk Liquid Tariff (JX 4), the Dump Truck Tariff (JX 5), and the Household Goods Tariff (JX 3). (F. 28, 29) These tariffs specify rates at which participating carriers will move these categories of goods. (F. 33, 34, 35) Participating carriers charge only a rate in the tariff. (F. 26) The effect of these tariffs is to fix the price charged for intrastate transportation of each of these categories. (F. 26, 60, 64, 70) At least two members of MTAC have participated in each rate set in each MTAC tariff. (F. 30) MTAC's active members control MTAC. (F. 8, 9, 10) MTAC acts as an agent on behalf of its members. (F. 27) [14]

Respondent's collective rate-making activities violate Section 5 of the Federal Trade Commission Act. The stipulated evidence establishes that the challenged conduct constitutes price-fixing and, in the absence of valid defense, is *per se* illegal. An agreement among competitors to eliminate price competition violates the antitrust laws, notwithstanding any argument that may be advanced to justify it. *Catalano, Inc. v. Target Sales, Inc.*, 446 U.S. 643, 647 (1980) (*per curiam*).

Respondent's conduct is virtually identical to that engaged in by the household goods carriers association in *Mass. Movers* which was found to violate Section 5 of the FTC Act. As in that case, respondent MTAC and its competing carrier members (F. 3), in cooperation with the New England Motor Rate Bureau (NEMRB), prepare tariffs pertaining to the intrastate transportation of commodities, approve them and participate in these collectively set rates. (F. 6, 9, 25-39). These activities, as well as the Bureau's publication and dissemination to its members of tariffs (JX 2-5) and tariff revisions containing collectively-set rates and classifications, constitute price-fixing. *Georgia v. Pennsylvania Railroad*, 324 U.S. 439, 460-61 (1945). In *Mass. Movers*, the Commission found that the Association's development of joint tariffs that were formally adopted and adhered to by its members was "*per se* unlawful under the antitrust laws." 102 FTC at 1225

The fact that individual member carriers are free to file rates

independently from the collectively agreed upon rates is irrelevant. An agreement to fix prices that does not coerce adherence is nevertheless illegal price-fixing. *Arizona v. Maricopa County Medical Society*, 457 U.S. 332, 345 (1982); *United States v. Container Corp.*, 393 U.S. 333, 337 (1969); "The continuation of some price competition is not fatal to the Government's case."

Respondent argues that the record does not establish that the carrier members initiated, prepared, developed and disseminated rates and collectively agreed on the rates, and that MTAC merely copies tariff proposals already filed with DPUC. While the stipulated record does show that MTAC relies on NEMRB for help in developing the general commodities tariff (F. 28, 32, 45), it also establishes that MTAC issues other tariffs without the involvement of NEMRB. (F. 29) Furthermore, there is overwhelming evidence of an unlawful combination of MTAC and its members, as well as NEMRB, with respect to the tariff and rates charged for transportation of general commodities. (F. 8-10, 26, 27, 30, 65), *United States v. Container Corp.*, 393 U.S. at 335. Moreover, respondent's argument is based on deposition testimony which was not offered or received as evidence in this case. Order Setting Briefing Schedule, filed November 24, 1986. The stipulation filed November 17, 1986, and the joint exhibits referred to therein, are the entire factual record of this case. *Ibid.* [15]

B. State Action Defense

1. Law

Parker v. Brown, 317 U.S. 341, 344-45 (1943) held that federal antitrust law was not intended to apply to certain state action. To be exempt, the acts must be clearly authorized and supervised by the sovereign state. *Hoover v. Ronwin*, 466 U.S. 558, 568-69 (1984). To determine whether the respondent's acts are exempt, the facts must be analyzed under the standard of *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 105 (1980).

The Court in *Midcal* set out the controlling two part test: "First, the challenged restraint must be 'one clearly articulated and affirmatively expressed as state policy'; second, the policy must be 'actively supervised' by the State itself." *Ibid.*

The second prong of the *Midcal* test prevents the state from "casting . . . a gauzy cloak of state involvement over what is essentially a private price-fixing arrangement." 445 U.S. at 106. This active supervision requirement ensures that a state's actions will

immunize the anticompetitive conduct of private parties only when the state has demonstrated its commitment to a program through its exercise of regulatory oversight. *Southern Motor Carriers Rate Conf. v. United States*, 105 S.Ct. 1721, 1729 n. 23 (1985).

The parties have joined issue on the second prong of the *Midcal* test of the state action defense. Complaint counsel argues that the state regulatory commission does not actively supervise the proposed collectively formulated rates through hearings to review the reasonableness of proposed tariffs. Hearings by a regulatory commission on proposed rates do, of course, constitute evidence that such applications are not "rubberstamped" or approved *pro forma* without hearing or change, and that the state agency actively supervises the anticompetitive conduct. *Sonitrol of Fresno, Inc. v. AT&T*, 629 F. Supp. 1089, 1094-95 (D.D.C. 1986). The requirement that applicants file extensive and detailed memoranda with the regulatory commission is also evidence that the state commission supervises heavily the rate approval process. *Id.* at 1095. The facts here show that respondent participates in both such hearings and filings, *infra*.

Complaint counsel, however, argues that in order to meet the state action exemption, the state regulatory agency must hold hearings, or at least give public notice and opportunity to comment, and publish a reasoned decision in every ratemaking decision.⁵ The basis for this argument is the policy cited in Areeda & Turner, *Antitrust Law*, Vol. 1 at ¶ 213f (1978) [16]

. . . [I]naction evades statutory approval procedures designed to (1) to accord opponents the opportunity to present facts and arguments against the challenged act, (2) to assure conscious consideration by those particular state officials charged with the power and responsibility for approval, and (3) to allow judicial review of the agency record.

Complaint counsel implies that the procedure described in the Areeda & Turner treatise should be used in reviewing all acts by a state regulatory commission under *Parker v. Brown*, to ensure that adequate state approval is contemplated.⁶ To support this argument, counsel relies on cases where statutes required an administrator to support an act by a written statement of reasons, *Dunlop v. Bachowski*, 421 U.S. 560, 573 (1975), or where hearings by the agency, upon application for rate approval, were cited as evidence of

⁵ Memorandum of Law dated December 5, 1986 at pp. 53-58.

⁶ Memorandum of Law dated December 5, 1986. at n. 58.

state supervision leading to immunity for anticompetitive conduct. *Sonitrol, supra*.

Chief Judge Barnes answered this argument in the Initial Decision in *The New England Motor Rate Bureau, Inc.*, Docket No. 9170, decided December 12, 1986, slip opinion at p. 30:

This Areeda-Turner idea would permit not only judicial review of agency decisions, but would compel the agencies to scrutinize more closely the basis for their decisions. Thus, much can be said for [its] adoption and implementation by the states. However, where the state by statute has granted the regulatory commission clear oversight authority to review rates for reasonableness, to suspend rates found to be unreasonable, and to establish just and reasonable rates when necessary, the existence of this latent oversight authority and the presumption of official regularity should shift the burden to the party challenging the ratemaking process to demonstrate that the regulatory commission in fact has never engaged in any active supervision of the ratemaking process. A mere showing that a state supervisory agency has not followed the Areeda-Turner suggested procedures is not sufficient to establish a lack of active supervision. The agency must be given some discretion as to its method and manner of supervision. Instead of concentrating on an agency's failure to follow [17] theoretical and desirable procedures, the record must concentrate on what the agency actually did.⁷

Furthermore, the Areeda-Turner proposal applies only where the regulatory agency has failed to act, *Areeda & Turner* at ¶ 213f.⁸ When the agency shows some regulatory activity and the issue is "how rigorous the supervision," the Professors suggest an entirely different theory, *id.* at ¶ 213c:

213c. **How rigorous the supervision?** When state agencies act within their authority, should the manner in which they exercise their discretion ordinarily be reviewed by the antitrust court? Should the court scrutinize the rigor with which the state supervises the challenged activity to ensure that supervision is more than *pro forma*? We answer in the negative, with the proviso that an outright attempt by a state to simply evade the antitrust laws should not be countenanced. We recognize that our approach may make such evasion easier, but we see no suitable way around this.

. . . There simply is no way to tell if the state has "looked" hard enough at the data,

⁷ The burden of proof rests on the party asserting the affirmative of an issue in the pleadings. *Koehler v. Marcona Mining Co.*, 391 F. Sup. 1158, 1160 (N.D. Cal. 1973), *aff'd*, 518 F.2d 696 (9th Cir. 1975). The procedure suggested by Judge Barnes therefore involves a shifting of the burden of proceeding rather than a shifting of the burden of persuasion. *A General Discussion of the Theory of Presumptions*, 45 Geo. L.J. 410, 417-21 (1957). *But see Ticor Title Ins. Co.*, Docket 9190, Initial Decision issued on January 6, 1987, slip opinion at p. 94, which apparently adopts a shifting of the burden of persuasion.

⁸ The total absence of activity by a state agency will not be active supervision within the meaning of *Midcal. State of Northern Carolina v. P.I.A. Asheville, Inc.*, 740 F.2d 274, 279 (7th Cir. 1984) (en banc). Where the state does not monitor market conditions or engage in any pointed reexamination of the program, the second prong of the state action immunity test will not be met. *Id.* at 279.

and there certainly are no manageable judicial standards by which a court may weigh the various elements of a "public interest" judgment in order to determine whether the legislature or agency decision was correct. . . . Those are political judgments and ought to be made by the legislature and its delegates. [18]

The facts of this case show that the state has demonstrated its commitment to a program exempt from the antitrust laws through statutory delegation and the exercise of regulatory oversight and active supervision of rates by the DPUC.

2. Facts

The state legislature clearly intended to create a program of regulatory oversight of transportation of commodities by motor carrier. (F. 66-71) And that program has been active. Effective in October, 1986, DPUC appointed Edward Regan, formerly head of the Transportation Division, the head and supervisor of the tariff division, and reporting to him are two rate analysts who review tariffs filed. (F. 40) Since 1983, the DPUC's accounting division has taken a larger role in reviewing tariff filings. (F. 42)

All carriers are required to file their rates with the DPUC. (F. 41) Rate analysts review the tariffs to check, among other matters, if rates are above the minimum rate orders. (F. 41) Tariffs are filed and held in abeyance on the public record for thirty days, unless to meet a competing carrier's tariff in which even a shorter period is permissible. (F. 52) Rate analysts can refuse to file the tariff on the public record if it does not satisfy the tariff regulations and requirements. (F. 41)

If the increases are less than five percent and there are no errors or corrections, there is a presumption that the request is reasonable and the tariff is approved without a hearing unless there is a protest. (F. 41, F. 43, F. 49) If there is a protest, a public hearing may be held. (F. 41) Frequently, rejected tariffs are refiled to satisfy the requirements of a DPUC rate analyst. (F. 41)

If a rate increase is for more than five percent, it must be accompanied by financial information to justify the reasonableness of the increase consisting of proponent's operating revenues, operating expenses, tonnage and revenue to be generated, a *pro forma* operating statement, relationship of proposed rates to class rates, net operating income. A net operating ratio of 93% is considered reasonable. (F. 44; JX 9d).

The DPUC has the power to prescribe minimum rates and does

prescribe them, either on its own motion or upon petition by an interested party. (F. 56) The Commission initiated a minimum rate order in 1959 and about twelve additional minimum rate orders since that time in response to carrier petitions. Several of these orders were based on records developed in adversary hearings and were accompanied by a formal published opinion and explication. (F. 45, F. 65) [19]

When a tariff is filed it is always checked to determine whether it is the same, below or above the minimum rate orders and whether it should be suspended, rejected, returned for errors or corrections or set down for a hearing. The DPUC has rejected some tariffs filed by independent carriers. (F. 57) The tariff is processed initially by the tariff section of the DPUC. It always refers a carrier with new authority to the audit section to consider and analyze the financial information submitted. (F. 58) An application for operating rights must be accompanied by a proposed tariff, and its rates are always checked by the tariff section to determine if they are at least equal to or above the minimum rate order at the time. (F. 59) The DPUC has issued several citations for charging rates different than the rate in the tariff. (F. 60) When a tariff rate change or rule is set down for a hearing, a legal notice is issued to the public by DPUC and published in selected Connecticut newspapers of general circulation. (F. 50)

Rate analysts in DPUC submit written recommendations with respect to applications for tariff changes on all matters that go to hearing. Written recommendations are also submitted at times when a matter is not set down for hearing. (F. 51) If a tariff submitted is above the minimum rate order and the increase is substantial (over 5%) the tariff is checked, the carrier is notified, and the tariff is suspended pending a conference or hearing. If the carrier makes corrections or adjustments satisfying to the tariff section, it is accepted and no hearing is required. (F. 61)

If a tariff submitted is below the minimum rate order, the carrier must file a petition for exemption, in which event, the tariff is suspended. A hearing may be held to justify the proposed rate. (F. 41) When a general rate increase is proposed, it must be accompanied by an elaborate justification statement. This statement is thoroughly analyzed by the tariff and audit sections and a written recommendation is prepared. (F. 54)

Whenever operating rights are transferred, an informal conference is required between the tariff section of the DPUC and the selling carrier at which conference the rates of the selling carrier are checked

for compliance with the statutes and regulations. (F. 62) Whenever a complaint by a shipper or another carrier affecting rates is filed, the matter is investigated. If any violation is found the carrier is required to cease and desist immediately and to make the required corrections or rebates if that is indicated. The shipper is always kept informed. (F. 63) If a carrier does not obey an order to cease and desist violations of the statutes or regulations, a citation is issued requiring compliance. Penalties are usually imposed if a violation is not found. (F. 64) [20]

V. CONCLUSIONS

1. The Federal Trade Commission has jurisdiction over the subject matter of this proceeding and over respondent.

2. The acts and practices charged in the complaint took place in or affected commerce within the meaning of the Federal Trade Commission Act.

3. Respondent and its members, officers, and directors have engaged in a conspiracy to restrain price competition amongst common carriers of property by motor vehicle. This conspiracy is an unfair method of competition and an unfair act and practice in commerce or affecting commerce in violation of Section 5 of the Federal Trade Commission Act.

4. This conspiracy is, however, exempt from Section 5 of the Federal Trade Commission Act by reason of the "state action" defense, *Parker v. Brown*.

Accordingly, the complaint must be dismissed.

OPINION OF THE COMMISSION

BY AZCUENAGA, *Commissioner*:

This case involves allegations that the respondent Motor Transport Association of Connecticut unlawfully combined with its members and others to fix prices in violation of Section 5 of the Federal Trade Commission Act, 15 U.S.C. 45, by collectively developing and filing rates for the intrastate transportation of property in the state of Connecticut. After trial on a stipulated record, the Administrative Law Judge dismissed the complaint, holding that the collective ratemaking was unlawful price fixing but that the conduct is protected from action under Section 5 by the state action doctrine of *Parker v. Brown*, 317 U.S. 341 (1943). For the reasons set forth below, we affirm the dismissal of the complaint.

THE FACTS

The undisputed facts in this case show that the Motor Transport Association of Connecticut, Inc. ("MTAC" or "Association"), is an association of approximately 585 competing motor common carriers engaged in the intrastate transportation of property in Connecticut. I.D.F. 1-3.¹ The active members of the Association elect its directors, who, in turn, control and manage the Association. I.D.F. 8. The active members meet annually and approve and ratify the actions of the Association and its directors and officers since the last annual meeting. I.D.F. 9; Stip. 8. Active membership is available to persons or firms that provide motor vehicle transportation for hire or for their own account and to motor vehicle dealers. I.D.F. 7; Stip. 6. Others are eligible for associate membership.

The member carriers are regulated by the state. The state requires that each carrier hold a state certificate of public convenience and necessity and that each carrier file a schedule of rates and charges for transportation services. Conn. Gen. [2] Stat. §§ 16-283 & 16-287 (1985).² A carrier's certificate is subject to revocation for failure to have a tariff on file, and a carrier may not charge a rate different from that filed without thirty days' notice, except "to meet the rate of a competing carrier" or "for good cause shown." Conn. Gen. Stat. § 16-289. Enforcement action may be taken against carriers for failure to have an effective tariff on file, *e.g.*, J.X. 18c-18e, or for failure to adhere to filed rates. I.D.F. 60; *see* J.X. 18h-18m.

The Association files proposed tariffs with the Connecticut Department of Public Utility Control ("DPUC") on behalf of its members. I.D.F. 25. After an MTAC tariff is approved by the DPUC, the rates contained in the tariff govern the fees of the members of the Association that choose to participate in it. I.D.F. 26. Members of the Association may participate in tariffs filed by MTAC, or they may file a separate tariff or file an exception to the MTAC tariff. Stip. 27 & 31.

¹ We use the following abbreviations in this opinion:

I.D.	Initial Decision
I.D.F.	Initial Decision Finding
R.R.B.	Respondent's Reply Brief
C.A.B.	Complaint Counsel's Appeal Brief
C.R.B.	Complaint Counsel's Reply Brief
Stip.	Stipulation of the Parties (Nov. 17, 1986)
J.X.	Joint Exhibit.

² All citations to Connecticut statutes and regulations are to those identified by the parties as the statutes and regulations pursuant to which MTAC filed tariffs and the DPUC reviewed tariffs during the period covered by the complaint. Stip. 44; J.X. 8, 9 & 10.

At all times relevant to the complaint, at least two members of MTAC have participated in the rates set by each of the MTAC tariffs. I.D.F. 30; Stip. 31.

a. *MTAC Tariffs*

MTAC files four different tariffs or schedules of rates, each of which includes rate schedules, general rules for computing applicable rates and rules for applying rates to transportation and ancillary services. I.D.F. 28 & 31. For example, the MTAC tariff of Local Commodity Rates Applying on Household Goods, effective on February 21, 1983, specifies several different sets of basic rates, the services included in the basic rate, the rates for additional services such as packing, piano moving, waiting time and overtime, and transportation rates on a time basis (for moves of 20 miles or less) and on a mileage basis (for moves of more than 20 miles). J.X. 3; *see* I.D.F. 33.

In addition to the Household Goods Tariff, MTAC files a Local and Joint Tariff of Class and Commodity Rates ("General Commodity Tariff"), J.X. 2, a Local Commodity Tariff Applying on Transportation of Liquid Commodities in Bulk, in Tank Trucks ("Bulk Liquid Tariff"), J.X. 4, and a Motor Freight Tariff of Local Commodity Rates Applying on Dump Truck Service ("Dump Truck Tariff"), J.X. 5. *See* I.D.F. 28-35. [3]

The General Commodity Tariff specifies rates per pound and minimum charges for commodities grouped by "class" for standardized distances. I.D.F. 32. The Bulk Liquids Tariff specifies rates per gallon for particular classes of bulk liquids moved between named points in the state or per mile between other points in the state. I.D.F. 34. The Dump Truck Tariff specifies rates per mile or hour, minimum shipments and other rules for hauling specific materials. I.D.F. 35.

In addition to filing tariffs, MTAC, in conjunction with New England Motor Rate Bureau, has from time to time petitioned the DPUC to issue minimum rate orders. I.D.F. 36, 37, 38 & 45. The function of a minimum rate order is, as the term suggests, to set a floor on rates. Carriers are required to charge no less than the minimum rate order unless they successfully petition the DPUC for an exemption. I.D.F. 36. Between 1957 and 1979, the DPUC issued twelve minimum rate orders. I.D.F. 45; *see, e.g.*, J.X. 6 & 7. MTAC also has intervened in opposition to petitions by carriers seeking exemptions from minimum rate orders. I.D.F. 39.

b. *State Regulation*

The Connecticut Department of Public Utility Control regulates motor common carriers. The DPUC is responsible for, among other things, issuing certificates of public convenience and necessity and reviewing proposed tariffs. Connecticut law provides that motor common carrier rates “shall be just and reasonable and reasonably compensatory” and gives the DPUC authority to “prescribe maximum or minimum or maximum and minimum rates or charges” for motor common carriers. Conn. Gen. Stat. ¶ 16-287(a). The DPUC may prescribe rates on its own motion or on the motion of any interested party, after a hearing. *Id.*

After a proposed tariff is filed with the DPUC, it is reviewed by one of the agency’s rate analysts, who stamps it as received, ascertains that the proposed rates comply with any applicable minimum rate orders and checks the form of the proposed tariff.³ If these and certain other requirements are met, the rate analyst places the proposed tariff on the public record for thirty days.⁴ I.D.F. 41. [4]

Carrier rates are required to be “just and reasonable and reasonably compensatory,” but no standards for review of proposed rates have been published. Stip. 46.⁵ In practice, the DPUC presumes that a proposed rate increase that is within 5% of the previously filed rate is reasonable. If a proposed rate increase falls within this 5% “zone of reasonableness” and no other corrections are necessary (and no protests are filed), the DPUC will approve the tariff without a hearing. I.D.F. 41.

If a proposed rate is an increase of more than 5% over the previous rate, the DPUC requires financial information to justify the increase, such as the carrier’s operating revenues and expenses, tonnage and revenue to be generated, net operating income and a *pro forma* operating statement. I.D.F. 44; Stip. 50, 62. The DPUC generally

³ Regulations of the DPUC address the technical aspects of tariff filing. *See, e.g.*, Conn. Agencies Regs. §§ 16-304-C2, et seq., which specify the size of paper, the arrangement of the title page and other requirements as to form of tariffs.

⁴ Rates filed with the DPUC may be changed only after 30 days’ notice, except to meet a competing rate or for good cause shown. One day’s notice is required when a carrier files to adopt a bureau tariff. Conn. Gen. Stat. § 16-289.

⁵ The DPUC has said that rates should be sufficient to meet “[t]he public need for a sound and stabilized motor common carrier industry” in the state and to “provide revenues which will cover all costs of operations and afford carriers a reasonable degree of profit.” In the Matter of Investigation and Stabilization of Rates of Motor Common Carriers, DPUC Docket No. 9652, April 15, 1959, at 15 (J.X. 6o).

regards an operating ratio (operating expenses divided by operating revenues) of 93% as presumptively reasonable.⁶ I.D.F. 44.

Between 1980 and 1983, DPUC's accounting division reviewed a tariff filing only if requested to do so by a rate analyst. Since 1983, as a result of an internal policy review, the accounting division has taken a larger role in reviewing filings. I.D.F. 42. All tariffs filed by carriers with new authority are referred to the audit section of the DPUC to consider and analyze the financial information submitted. I.D.F. 58. A proposal for a general rate increase submitted by a rate bureau such as MTAC must be accompanied by an elaborate justification statement, which is thoroughly analyzed by both the staff and the audit sections of the DPUC, after which a written recommendation is prepared for the Commission. I.D.F. 54. [5]

State law provides for a thirty day public comment period on proposed tariffs, during which time the DPUC reviews the filing, Stip. 67, and a rate analyst prepares a written recommendation with respect to the proposed tariff. I.D.F. 51; Stip. 66. If the proposed tariff is presumptively reasonable—that is, the proposed increase is less than 5% and at least equal to any applicable minimum rate order—then the tariff usually is permitted to become effective at the end of the thirty-day period without a hearing. I.D.F. 41 & 49. When a tariff becomes effective without a rejection, suspension or hearing, the rate analyst to whom the matter has been assigned has concluded that the proposed rates meet the requirements of the applicable statutes and regulations. I.D.F. 43; Stip. 49.

A proposed tariff can be set for a hearing if a protest is filed by "any interested person," or the DPUC may set the matter for a hearing on its own initiative. Conn. Gen. Stat. § 16-289. If a hearing is held, the DPUC issues a legal notice, and the staff of the DPUC submit a written recommendation. I.D.F. 51; Stip. 66. Except for hearings on minimum rate orders and on petitions for exemptions from minimum rate orders, few public hearings have been held in the last sixteen years. I.D.F. 41; Stip. 46. When a hearing is held, normally there is little opposition to the rate increase, and the hearing takes one day. Frequently, when the DPUC poses questions, the petitioner revises and refiles its tariff in order to satisfy the concerns of the DPUC rate analyst. *Id.*

⁶ The DPUC found that an operating ratio of 93% was reasonable in Docket No. 9652, at 15 (J.X. 6o). The DPUC denied a joint MTAC/New England Motor Rate Bureau minimum rate petition on the ground that the projected operating ratio of 83.7% was "more than just reasonable and adequate to enable the Petitioners to provide properly for the public convenience, necessity and welfare." DPUC Docket 781114, March 12, 1979, at 3 (J.X. 7t).

The DPUC has disapproved a minimum rate petition filed jointly by MTAC and the New England Motor Rate Bureau, I.D.F. 65; *see note 6 supra*, and it has rejected some tariffs filed by independent carriers. I.D.F. 57; Stip. 59. The DPUC investigates complaints filed by shippers or other carriers concerning a carrier's rates, and it can issue an order requiring a carrier to cease the violation and to pay rebates. I.D.F. 63. The DPUC also can issue citations requiring compliance if an order is not obeyed, and the DPUC has issued citations to carriers for charging rates different from those in the filed tariff. I.D.F. 60.

LEGAL ANALYSIS

After establishing that the Commission has jurisdiction over the Association under the Federal Trade Commission Act, two questions of law remain. First, we must determine whether the Association's conduct constitutes unlawful price fixing. If the conduct is unlawful, we then must consider whether it is protected from the Federal Trade Commission Act because it is state action within the meaning of *Parker v. Brown*, 317 U.S. 341 (1943). [6]

I. JURISDICTION

The Motor Transport Association of Connecticut has not raised jurisdiction as an issue on appeal.⁷ We note, nevertheless, that the Commission has jurisdiction over MTAC. Section 5(a)(2) of the Federal Trade Commission Act extends the Commission's jurisdiction to "corporations," which, as defined in Section 4 of the Act, includes any firm "organized to carry on business for its own profit or that of its members." MTAC is a nonprofit corporation, organized and doing business in the state of Connecticut. Stip. 1, Answer ¶ 18. The fact that MTAC is a nonprofit corporation does not defeat the Commission's jurisdiction. The Association is subject to the Commission's jurisdiction if its activities provide an economic benefit to its members and if those activities are a substantial part of the Association's activities, rather than merely incidental to the noncommercial activity. *American Medical Association*, 94 FTC 701, 983-84 (1979), *aff'd*, 638 F.2d 443, 447-48 (2d Cir. 1980), *aff'd per curiam by equally divided Court*, 455 U.S. 676 (1982); *National Commission on Egg*

⁷ The respondent lists its Answer defenses, other than state action, in its Answering Brief, R.R.B. at 2-3, but did not brief them at trial or on appeal. The Administrative Law Judge decided that because the defenses were not briefed, they need not be decided, I.D. at 13, and we agree. *See Hospital Corp. of America v. FTC*, 807 F.2d 1381, 1393 (7th Cir. 1986) (Posner, J.) ("[I]ssues cannot be preserved . . . merely by being raised . . . or by being developed inadequately. . . ." (Citations omitted.)).

Nutrition, 88 FTC 89, 177 (1976), *modified*, 570 F.2d 157 (7th Cir. 1977), *cert. denied*, 439 U.S. 821 (1978). MTAC has provided substantial economic benefits for its members by issuing and filing tariffs with the DPUC on behalf of its members and by petitioning the DPUC to issue minimum rate orders. I.D.F. 13 & 25-29.

Although some of the Association's members are carriers subject to the Interstate Commerce Act and therefore exempt from the Federal Trade Commission Act, 15 U.S.C. 45(a)(2), MTAC does not transport goods and is not a common carrier. I.D.F. 12; Stip. 22, 23. The fact that the Association operates as an agent for common carriers does not bring it within the common carrier exemption. *See Massachusetts Furniture & Piano Movers Association, Inc. v. FTC*, 773 F.2d 391, 394 (1st Cir. 1985) (association that is not a common carrier is not within the common carrier exemption); *Official Airline Guides, Inc. v. FTC*, 630 F.2d 920, 923 (2d Cir. 1980), *cert. denied*, 450 U.S. 917 (1981). [7]

II. PRICE FIXING

The Motor Transport Association of Connecticut also does not dispute on appeal that it has engaged in price-fixing. On behalf of its members, MTAC prepares and files with the state DPUC tariffs containing proposed rates for transportation services, which, after approval by the DPUC, establish the prices for those of its carrier members that elect to participate in a particular tariff. In addition to tariff proposals, MTAC has petitioned the state DPUC to adopt minimum rate orders, setting a floor on prices for some transportation services for all intrastate carriers.

This activity is collective ratemaking, concerted activity to fix or stabilize prices, that "easily fits the classic description of a 'naked price restraint.'" *United States v. Southern Motor Carriers Rate Conference, Inc.*, 467 F. Supp. 471, 486 (N.D. Ga. 1979), *aff'd*, 702 F.2d 532 (5th Cir. 1983), *rev'd on other grounds*, 471 U.S. 48 (1985); *see also Massachusetts Furniture & Piano Movers Association, Inc.*, 102 FTC 1176, 1224-25 (1983), *rev'd on other grounds*, 773 F.2d 391 (1st Cir. 1985). The Association and all of its members need not agree to a single price level in order to fix prices. Rather, it is sufficient to show an agreement having the purpose or effect of inhibiting price competition. Such an agreement is *per se* unlawful. "Price is the 'central nervous system of the economy,' *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 226 N.59 [1940], and an agreement

that 'interfere[s] with the setting of price by free market forces' is illegal on its face." *National Society of Professional Engineers v. United States*, 435 U.S. 679, 692 (1978).

III. STATE ACTION

The primary issue on this appeal is whether the otherwise unlawful conduct of the Association is protected from the Federal Trade Commission Act by the state action doctrine.⁸ The Association claims that because the tariffs that it proposes are subject to approval by the state, the tariffs are the action of the state and not the product of private collective ratemaking that is subject to Section 5 of the Federal Trade Commission Act.

The state action doctrine involves principles of federalism and state sovereignty. These principles were invoked in *Parker v. Brown*, 317 U.S. 341 (1943), in which the Supreme Court held that the Sherman Act was not intended to prohibit the states from [8] imposing restraints on competition. The Court said, "In a dual system of government in which, under the Constitution, the states are sovereign, save only as Congress may constitutionally subtract from their authority, an unexpressed purpose to nullify a state's control over its officers and agents is not lightly to be attributed to Congress." 317 U.S. at 351. On the other hand, the court said, "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." *Id.*⁹

To determine whether the challenged conduct is private action or state action, the Court in *California Retail Liquor Dealers Association v. Midcal Aluminum, Inc.*, 445 U.S. 97 (1980), articulated a rigorous two-part test. Under *Midcal*, a private party's conduct is protected by state action if, first, the challenged restraint is "clearly articulated and affirmatively expressed as state policy" and, second, the policy is actively supervised by the state. *Id.* at 105.¹⁰ The purpose

⁸ The state action doctrine is available in Section 5 cases applying Sherman Act standards. *E.g., Asheville Tobacco Board of Trade, Inc. v. FTC*, 263 F.2d 502 (4th Cir. 1959).

⁹ The state action doctrine reflects the "principle that the federal antitrust laws pre-empt state laws authorizing or compelling private parties to engage in anticompetitive behavior," *324 Liquor Corp. v. Duffy*, 479 U.S. 335, 346 n.3 (1987), but state law is not preempted when the *Midcal* criteria are met. See *Fisher v. City of Berkeley*, 475 U.S. 260, 264-65 (1986); *Community Communications Co., Inc. v. City of Boulder*, 455 U.S. 40, 60 (1982) (Rehnquist, J., dissenting).

¹⁰ The *Midcal* test does not apply when the state acts as sovereign through its legislature, *Parker v. Brown*, 317 U.S. 341 (1943), or through its supreme court, *Bates v. State Bar of Arizona*, 433 U.S. 350 (1977). Municipalities must show that their conduct is pursuant to a clearly articulated state policy but need not demonstrate active supervision by the state. *Town of Hallie v. City of Eau Claire*, 471 U.S. 34 (1985). The Court has not decided whether active supervision applies when the actor is a state agency, *id.* at 46 n.10, but lower courts have held that active supervision does not apply to state agencies. See *Interface Group v.*

(footnote cont'd)

of the *Midcal* standard is to ensure that the state action doctrine protects what is in fact state action, not private action.

Because MTAC is a private entity, both parts of the *Midcal* standard must be met here for the state action doctrine to apply. [9]

a. *Clear Articulation*¹¹

The state regulations here are similar to the regulatory scheme considered in *Southern Motor Carriers Rate Conference, Inc. v. United States*, 471 U.S. 48 (1985), in which the Court applied the first part of the *Midcal* standard to collective ratemaking by intrastate common carrier rate bureaus. Although the statutes of Connecticut, like the statutes of Mississippi at issue in *Southern Motor Carriers*, do not specifically address collective ratemaking, they give the state agency authority to regulate common carriers and to prescribe rates for the intrastate transportation of property. The Court in *Southern Motor Carriers* concluded that the Mississippi legislature, by its delegation of ratemaking power to the state agency, "thus made clear its intent that intrastate rates would be determined by a regulatory agency, rather than by the market." 471 U.S. at 63-64.¹² The legislature, having made clear its intent to displace competition with regulation, left "[t]he details of the inherently anticompetitive rate-setting process . . . to the agency's discretion." *Id.* at 64.

The Court concluded that this was sufficiently clear articulation to satisfy the first part of the *Midcal* test:

As long as the State as sovereign clearly intends to displace competition in a particular field with a regulatory structure, the first prong of the *Midcal* test is satisfied. . . . [T]he State's failure to describe the implementation of its policy in detail will not subject the program to the restraints of the federal antitrust laws.

Id. at 64-65 (footnote omitted). Applying this standard to Connecticut's regulatory scheme, we conclude that the state legislature has clearly articulated its intent to displace [10] competition with

Massachusetts Port Authority, 816 F.2d 9 (1st Cir. 1987); *Cine 42d Street Theater Corp. v. Nederlander Organization, Inc.*, 790 F.2d 1032, 1047 (2d Cir. 1986).

¹¹ Although complaint counsel note that the Commission could decide that Connecticut has not clearly articulated a policy favoring the conduct challenged here, this issue was not argued at trial. See C.A.B. at 10 n.11; C.R.B. at 2-4; note 7 *supra*.

¹² In Connecticut, as in Mississippi, the state agency is not authorized to choose competition but is required to prescribe rates for motor common carriers on the basis of statutorily enumerated factors that "bear no discernible relationship to the prices that would be set by a perfectly efficient and unregulated market." *Southern Motor Carriers*, 471 U.S. at 65 n.25. Connecticut law requires that rates be "just and reasonable and reasonably compensatory." Conn. Gen. Stat. § 16-287(a).

regulation and, therefore, that the first part of the *Midcal* test has been met in this case. See also *Massachusetts Furniture & Piano Movers Association v. FTC*, 773 F.2d 391, 395-97 (1st Cir. 1985).

b. *Active Supervision*

To be protected by the state action doctrine, the Association also must show that the state actively supervises the Association's collective ratemaking. The purpose of the active supervision requirement is to ensure "that a State's actions will immunize the anticompetitive conduct of private parties only when the 'state has demonstrated its commitment to a program through its exercise of regulatory oversight.'" *Southern Motor Carriers*, 471 U.S. at 61 n.23, quoting I P. Areeda & D. Turner, *Antitrust Law* ¶ 213a, at 73 (1978).¹³ Absent evidence of active supervision, "[w]here a private party is engaging in the anticompetitive activity, there is a real danger that he is acting to further his own interests, rather than the governmental interests of the State." *Town of Hallie v. City of Eau Claire*, 471 U.S. 34, 47 (1985).¹⁴

Although the purpose of the active supervision requirement is clear, neither judicial nor Commission precedent precisely establishes how the requirement should apply to the facts of this case. We are guided, however, by the three cases in which the Supreme Court has applied the active supervision requirement. The Court found no active supervision of state liquor price posting regulatory schemes in *Midcal* and *324 Liquor Corp. v. Duffy*, 479 U.S. 335 (1987), when the "State simply authorize[d] price setting and enforce[d] the prices established by private parties":

The State neither establishes prices nor reviews the reasonableness of the price schedules; nor does it regulate the terms of fair trade contracts. The State does not monitor market conditions or engage in any "pointed reexamination" of the program.
[11]

Midcal, 445 U.S. at 105-06; accord, *324 Liquor Corp.*, 479 U.S. at 344-45 ("The State has displaced competition among liquor retailers without substituting an adequate system of regulation.").

The Supreme Court most recently applied the active supervision requirement in *Patrick v. Burget*, — U.S. —, 108 S. Ct. 1658 (1988),

¹³ Accord, *Asheville Tobacco Board of Trade v. FTC*, 263 F.2d 502, 509 (4th Cir. 1959) (no state action when private decisions not "adequately supervised by independent state officials").

¹⁴ The Court also said that "[w]e may presume, absent a showing to the contrary, that the municipality acts in the public interest." 471 U.S. at 45 (footnote omitted).

a case involving a challenge under the Sherman Act to a decision by a group of physicians to revoke the plaintiff's hospital privileges. The Court held that the state did not actively supervise the peer review decisions of the defendants, because there was no showing that any state entity reviewed or even had the authority to review those decisions and to correct them if they were inconsistent with state policy. *Id.* at 1663.

The Court's decisions establish that active supervision exists when "state officials have and exercise the power to review" the challenged private acts and to "disapprove those that fail to accord with state policy." 108 S. Ct. at 1663. Consistent with this standard, the Court has established that no active supervision exists when a state agency lacks the authority to set prices, even though the agency could grant exceptions to the privately established prices. *324 Liquor Corp.*, 479 U.S. at 345 n.7. No active supervision exists in the ability of the state legislature to consider proposals to change the regulatory pricing scheme, because "periodic reexaminations by the state legislature [do not] exert any significant control over retail liquor prices or mark-ups." *Id.*¹⁵ And no active supervision exists when state entities do not have the "power to overturn a decision that fails to accord with state policy." *Patrick v. Burget*, 108 S. Ct. at 1664.

In this case, unlike *Midcal* and *324 Liquor Corp.*, the state agency has the authority to review private common carrier rate proposals to ensure that they are "just and reasonable and reasonably compensatory," to reject rate proposals that do not comply with the applicable standards and to "prescribe maximum or minimum or maximum and minimum rates or charges" for motor common carriers. The state, through the DPUC, has the power that was lacking in *Midcal*, *324 Liquor Corp.* and *Patrick v. Burget* to review private price setting and to disapprove those privately established prices that are not consistent with state policy. The state's system of regulation, on its face, provides for active supervision. [12]

The respondent suggests that the fact that the DPUC has authority to prescribe prices and to review proposed tariffs is alone sufficient to establish active supervision. *See* R.R.B. at 19. In *Midcal*, *324 Liquor Corp.* and *Patrick*, because the states lacked this kind of authority, the Supreme Court did not have occasion to consider whether such state authority would alone be sufficient for active supervision.

¹⁵ Although the state legislature's power to change the regulatory scheme apparently would not constitute active supervision, "pointed re-examination by the policymaker . . . in enforcement proceedings" constituted active supervision in *Bates v. State Bar of Arizona*, 499 U.S. 950, 959 (1977).

Nevertheless, the Court has said that the state must “have *and* exercise power to review particular anticompetitive acts of private parties and disapprove those that fail to accord with state policy.” *Patrick v. Burget*, 108 S. Ct. at 1663 (emphasis added).

An assumption that authority alone establishes the existence of active supervision would effectively eviscerate the active supervision requirement, and the “national policy in favor of competition [could] be thwarted by casting . . . a gauzy cloak of state involvement,” *Midcal*, 445 U.S. at 106, over private price fixing by the mere existence of a regulatory framework that is never put to use. Instead, to determine the state’s “commitment to a program through its exercise of regulatory oversight,” *Southern Motor Carriers*, 471 U.S. at 61 n.23, we must consider whether the state agency exercises the authority delegated to it, whether the state in fact actively supervises the private anticompetitive conduct.

We find that the Connecticut DPUC exercises its delegated authority over intrastate motor common carrier rates. The record shows that the DPUC regularly reviews proposed tariffs and considers the reasonableness of proposed rates in the context of minimum rate orders and other agency guidelines for evaluating proposed tariffs. I.D.F. 41-45.¹⁶ The record discloses specific examples of active oversight by the DPUC, when the agency has suspended a proposed rate, held a hearing and issued a written decision. I.D.F. 65. The record shows that the DPUC has prescribed rates in minimum rate orders, pursuant to the notice and hearing procedures provided by state statute. *See* notes 5 & 6 *supra*. The record also shows that when the DPUC allows a proposed rate to become effective without invoking its hearing procedures, that action results from the decision of the agency that the proposed rate “meet[s] the requirements of the statutes and regulations.” I.D.F. 43.¹⁷ [13]

Complaint counsel argue that the Association’s collective ratemaking is not actively supervised unless the state agency acts affirmatively with respect to proposed rates to ensure that “the *state* has in fact acted to insert its judgment in place of market forces.” C.A.B. at 17 (emphasis in original). In a thoughtful brief, complaint counsel propose that unless the state agency provides public notice of each

¹⁶ The DPUC’s 5% “zone of reasonableness” for proposed rate increases, *see* I.D.F. 41, is a matter within the agency’s discretion. *See Southern Motor Carriers*, 471 U.S. at 62-64.

¹⁷ The alleged inaction in this case is not a failure to review proposed tariffs, *see* I.D.F. 41-43, but rather the DPUC’s failure to invoke notice and hearing procedures with respect to every proposed tariff. *See* C.A.B. at 5-7.

pending rate proposal and opportunity for interested persons to comment and publishes a reasoned explanation of its decision, active supervision cannot be found. C.A.B. at 21.

We conclude that a hearing and a written opinion with respect to every rate proposal are not a necessary precondition for finding active state supervision. We have found no precedent for the proposition that notice and hearing procedures are a prerequisite for active supervision. In the cases cited by complaint counsel, the courts did not say that notice and hearing procedures were essential for active supervision. Instead, they considered whether particular notice and hearing procedures implemented under state law constituted active supervision.

Although we agree with complaint counsel that implementation of notice and hearing procedures would provide tangible evidence of the state's active supervision and its commitment to the regulatory scheme, we decline to impose such requirements through the state action doctrine. To be sure, review of proposed tariffs pursuant to negative option procedures, like those created by the Connecticut statute,¹⁸ may provide less tangible evidence of active supervision than the notice, hearings and published decisions that complaint counsel would require.¹⁹ But the use of negative option procedures need not demonstrate the absence of active supervision, unless administrative silence is deemed equivalent to the abandonment of [14] administrative duty.²⁰ The state can exercise its authority to supervise prices, as Connecticut does, by reviewing proposed rates for compliance with the applicable criteria and allowing rates to become effective after determining that the rates in fact are in compliance.

CONCLUSION

We conclude that the Connecticut DPUC has and exercises ultimate

¹⁸ In Connecticut, proposed tariffs are effective 30 days after filing unless suspended and set for a hearing by the DPUC. Conn. Gen. Stat. § 16-289. The Court in *Southern Motor Carriers* described state regulatory procedures virtually identical to those used by the Connecticut DPUC and concluded that "[t]he State [agencies] thus have and exercise ultimate authority and control over all intrastate rates." 471 U.S. at 50-51 (*dicta*).

¹⁹ "[T]he requirement of active state supervision serves essentially an evidentiary function: it is one way of ensuring that the actor is engaging in the challenged conduct pursuant to state policy." *Town of Hallie v. City of Eau Claire*, 471 U.S. at 46.

²⁰ Professors Areeda and Turner suggest that negative option procedures, like those used in Connecticut, ought not be sufficient for state action, because (1) "inaction" may suggest lack of awareness and (2) such procedures may evade statutory notice and hearing procedures designed to assure a certain level of awareness by responsible state officials. I P. Areeda and D. Turner, *Antitrust Law* ¶ 213f, at 78-79 (1978). These concerns are inapposite here. First, the record shows that the DPUC is aware and reviews the contents of proposed tariffs. *E.g.*, I.D.F. 41, 43, 44, 51-54, 57-59 & 61. Second, the procedures at issue here were themselves created by the state legislature.

authority and control over intrastate motor common carrier rates, that the clear articulation and active supervision requirements of *Midcal* have been satisfied and, therefore, that the Association's conduct is protected from action under Section 5 of the FTC Act.

The complaint is dismissed.

FINAL ORDER

This matter having been heard by the Commission on the appeal of complaint counsel from the initial decision and on briefs and oral arguments in support of and in opposition to the appeal, for the reasons stated in the accompanying Opinion, the Commission affirms the decision of the Administrative Law Judge.

Accordingly, *it is ordered*, That the complaint be and it hereby is dismissed.

Chairman Steiger and Commissioner Machol not participating.

IN THE MATTER OF

TICOR TITLE INSURANCE COMPANY, ET AL.

FINAL ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATION OF
SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

Docket 9190. Complaint, Jan. 7, 1985—Final Order, Sept. 19, 1989

This final order prohibits, among other things, each respondent from discussing, proposing, setting, or filing any rates for title search and examination services through a rating bureau in New Jersey, Pennsylvania, Connecticut, Wisconsin, Arizona and Montana.

Appearances

For the Commission: *Michael E. Antalics, James C. Egan, Jr. and Ann Malester.*

For the respondents: *John C. Christie, Jr., Bell, Boyd & Lloyd, Washington, D.C. David M. Foster, Fulbright & Jaworski, Washington, D.C. Robert E. Cooper, Gibson, Dunn & Crutcher, Los Angeles, Ca. and John F. Graybeal, Adams, McCullough & Beard, Raleigh, N.C.*

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, as amended (15 U.S.C. 41 *et seq.*), and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that the respondents named in the caption hereof have violated the provisions of Section 5 of the Federal Trade Commission Act and that a proceeding by it in respect thereof would be in the public interest, hereby issues this complaint, stating its charges as follows:

DEFINITIONS

PARAGRAPH 1. The following definitions shall apply in this complaint:

- a. *"Title search and examination services"* means all activities which are designed to identify and describe the ownership of a particular parcel of real property as well as any other actual or potential rights to, encumbrances on, or interests in the property.

- b. "*Settlement services*" means those services related to the closing of a real estate transaction, including but not limited to those services performed in connection with or in supervision of the execution, delivery or recording of transfer and lien documents, or the disbursement of funds.

RESPONDENTS

PAR. 2. Respondent Ticor Title Insurance Company is a corporation organized under the laws of the State of California, with its principal place of business at 6300 Wilshire Boulevard, Los Angeles, California.

PAR. 3. Respondent Chicago Title Insurance Company is a corporation organized under the laws of the State of Missouri, with its principal place of business at 111 W. Washington Street, Chicago, Illinois.

PAR. 4. Respondent Safeco Title Insurance Company is a corporation organized under the laws of the State of California, with its principal place of business at 13640 Roscoe Boulevard, Los Angeles, California.

PAR. 5. Respondent First American Title Insurance Company is a corporation organized under the laws of the State of California, with its principal place of business at 114 East 5th Street, Santa Ana, California.

PAR. 6. Respondent Lawyers Title Insurance Corporation is a corporation organized under the laws of the Commonwealth of Virginia, with its principal place of business at 6630 West Broad Street, Richmond, Virginia.

PAR. 7. Respondent Stewart Title Guaranty Company is a corporation organized under the laws of the State of Texas, with its principal offices at Stewart Building, Galveston, Texas.

JURISDICTION

PAR. 8. Respondents maintain, and have maintained, a substantial course of business, including the acts and practices as hereinafter set forth, which are in or affect commerce within the meaning of the Federal Trade Commission Act.

PAR. 9. Title search and examination services do not constitute the "business of insurance" within the meaning of the McCarran-Ferguson Act, 15 U.S.C. 1012(b).

PAR. 10. Settlement services do not constitute the "business of insurance" within the meaning of the McCarran-Ferguson Act, 15 U.S.C. 1012(b).

ANTICOMPETITIVE ACTS AND PRACTICES

PAR. 11. Respondents have agreed on the prices to be charged for title search and examination services or settlement services through rating bureaus in various states. Examples of states in which one or more of the respondents have fixed prices with other respondents or other competitors for all or part of their search and examination services or settlement services are Arizona, Connecticut, Idaho, Louisiana, Montana, New Jersey, New Mexico, New York, Ohio, Oregon, Pennsylvania, Wisconsin and Wyoming.

ANTICOMPETITIVE EFFECTS

PAR. 12. As a result of the aforesaid acts and practices, competition in the sale of title search and examination services or settlement services has been restrained in various states.

PAR. 13. The aforesaid acts and practices therefore constitute unfair methods of competition in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act.

INITIAL DECISION BY

MORTON NEEDELMAN, ADMINISTRATIVE LAW JUDGE

DECEMBER 22, 1986

I. STATEMENT OF THE CASE

The complaint in this proceeding was issued on January 7, 1985. It charges that in violation of Section 5 of the Federal Trade Commission Act, 15 U.S.C. 45, respondent insurers,¹ operating through rating bureaus, have restrained competition in setting rates for title search and examination services and settlement services. The gravamen of the complaint appears in Paragraph 11—

Respondents have agreed on the price to be charged for title search and examination services or settlement services through rating bureaus in various states. Examples of states in which one or more of the Respondents have fixed prices with other Respondents or other competitors for all or part of their search and examination services or settlement services are Arizona, Connecticut, Idaho, Louisiana, Montana, New Jersey, New Mexico, New York, Ohio, Oregon, Pennsylvania, Wisconsin and Wyoming.

¹ The complaint cites six title insurers as respondents. On June 24, 1986, the Secretary withdrew this matter from adjudication with respect to First American Title Insurance Company in order for the Commission to consider a settlement agreement under §3.25(c) of the Commission's rules.

Respondents' answers, which were filed on February 11 and February 13, 1985, admit that from time to time they have been members of rating bureaus in several states, but challenge the Commission's subject matter jurisdiction on the grounds that rating bureau activity relating to title search and examination and settlement constitute part of the business of insurance and is therefore exempt from the Federal Trade Commission Act by reason of the McCarran-Ferguson Act. Respondents' answers also assert that the alleged anticompetitive practices are immune from the federal antitrust laws by reason of the "state action" doctrine. Additional defenses include mootness based upon withdrawal from the rating bureaus, and the claim that respondents' collective rate making activities come within the *Noerr-Pennington* doctrine. [3]

It became apparent at the outset of this proceeding that the complaint allegation respecting settlement or escrow services was an ancillary issue. At most it only pertains to rating bureau activity in five states—Arizona, Ohio, Connecticut, Pennsylvania, and New Jersey—and since respondents' escrow practices in Arizona are already the subject of injunctive relief as a result of the final order in *United States v. Title Insurance Rating Bureau of Ariz., Inc.*, 517 F. Supp. 1053 (D. Ariz.), *aff'd*, 700 F.2d 1247 (9th Cir.), *cert. denied*, 104 S. Ct 3509 (1984), both sides directed their efforts almost exclusively to the search and examination issue. The escrow or settlement question, to the extent that it is still an issue in this case, is treated separately for the most part in the Findings of Fact and Discussion herein.

In the prehearing stage, the parties were allowed discovery including advanced notice of proposed exhibits and the prospective testimony of witnesses. Complaint counsel's case-in-chief was heard during the week of February 18, 1986. The defense case was presented between April 21 and July 28, 1986. Rebuttal evidence was offered by complaint counsel on July 29. The record was closed for receipt of evidence on August 29, 1986. During the hearings, counsel for all parties were given full opportunity to be heard and to cross-examine the witnesses. Both sides filed their main briefs and proposed findings on September 22, 1986; replies were filed on October 14, 1986.

After reviewing all of the evidence, as well as proposed findings and briefs submitted by the parties, and based on the entire record, including a determination of the credibility of witnesses (which took

into account demeanor and the consistency between testimony prepared for litigation and the plain meaning of everyday business records), I make the following findings of fact:² [4]

² Proposed findings not adopted in the form or substance proposed are rejected as either not supported by the entire record or as involving immaterial or irrelevant matters.

The following abbreviations are used throughout in citing to the record:

CX (Complaint counsel's exhibits)

RX (Respondents' exhibits)

Joint Physical Exhibit A (JXA, 311 pages) is a compilation of relevant state title insurance statutes. Section 33-25-302 of the Montana Title Insurance Act (cited at p. 184, Vol. I of respondents' main brief) does not appear in JXA but the entire text is quoted in note 269, *infra*. Testimony is cited by the name of the witness followed by the transcript page as in DiSanto 2738-41. CX 1 and RX 1 are the indices required by §3.46(b) of the Commission's Rules.

Respondents requested *in camera* treatment for certain exhibits, and after an adequate justification was made pursuant to §3.45 of the Rules, it was ordered that these exhibits were to be segregated and placed in an *in camera* file. The *Omnibus In Camera Order* issued on February 10, 1986, which governs all *in camera* exhibits, provides as follows:

It should be clearly understood that nothing contained in this Order in any way limits the public use of this material in decisions written by the Administrative Law Judge, the Commission, or reviewing courts. While I have no intention of making unnecessary disclosures, whether or not to publish in my Initial Decision all or part of the material contained in *in camera* exhibits must be left solely to the discretion of Administrative Law Judge, and I must reserve the right to exercise this discretion without counseling any party or third party.

The *Omnibus In Camera Order* also provides that documents shall be removed from the *in camera* file three years after the date on which the record was closed—that is, on August 29, 1989.

The appearances of the witnesses were as follows:

<u>Name</u>	<u>Called By</u>	<u>Transcript Pages</u>
Lawrence F. Anito, Jr. (Independent Attorney and Attorney-Agent for Respondents Ticor and First American)	Complaint counsel ("c.c.")	248-348
Irwin E. Cooper (Independent Attorney and Attorney-Agent for a non- respondent title insurer) [5]	c.c.	357-430
Albert F. Quadraccia (Agent for a non- respondent title insurer)	c.c.	486-530
Robert A. Fraundorf (Bureau Chief, Licensing, Idaho Department of Insurance)	c.c.	3425-3453
Gerald L. Ippel (President, Respondent Ticor)	Respondents ("resp.")	608-706
Albert D. Malaker (Great Lakes Regional Counsel, Respondent Chicago Title)	resp.	707-836

(footnote cont'd)

Initial Decision

Mark W. Sinkhorn (Ohio State Counsel, Respondent Lawyers Title)	resp.	843-934
Michael J. Fromhold (Senior Associate Title Counsel, Respondent Ticor)	resp.	941-1034
Michael F. Waiwood (Agent for Respondent Ticor)	resp.	1040-1128
Perry J. Armstrong (Agent for Respondent Ticor)	resp.	1134-1182
Thomas F. Ferraro (Vice President, Respondent Chicago Title)	resp.	1185-1245, 2298-2368
Joseph C. Bonita (Vice President, Respondent Ticor) [6]	resp.	1251-1309
Erich E. Everbach (General Counsel, Respondent Ticor)	resp.	1311-1418
Robert B. Holtom (Independent Insurance Consultant and Expert)	resp.	1429-1601
Leonard C. Donohoe (General Counsel, Respondent Chicago Title)	resp.	1610-1685
Donald E. Grabski (Vice President, Respondent Lawyers Title)	resp.	1686-1732
Norman J. Wirtz (Insurance Rate and Forms Analyst, Property and Casualty Section, Wisconsin Office of Commissioner of Insurance)	resp.	1738-1827
Joseph M. Clayton (Deputy Manager, New Jersey Land Title Rating Bureau)	resp.	1828-1879
Neil A. Bethel (A Principal Owner, Tillinghast, Nelson & Warren, an insurance actuarial consulting firm)	resp.	1885-2037
John B. Wilkie (President, Respondent Lawyers Title (Arizona))	resp.	2055-2144
Deloris Williamson (Chief Deputy Director, Property and Casualty Section, Arizona Department of Insurance) [7]	resp.	2167-2216

(footnote cont'd)

II. FINDINGS OF FACT

A. IDENTITY OF RESPONDENTS

1. Respondent insurers are engaged in the business of insuring the ownership of real estate for buyers and those lenders (mortgagees) who rely on real estate as security for their loans. As part of the

Emil L. Barberich (Market Conduct Examiner, Arizona Department of Insurance)	resp.	2222-2297
Irving H. Plotkin (Title Insurance Rate Expert, Arthur D. Little)	resp.	2376-2566 2573-2718
Waldo R. DiSanto (Director, Property and Casualty Division, Connecticut Insurance Department)	resp.	2724-2823
Walter S. Bell (Examiner, Property and Casualty Division, Connecticut Insurance Department)	resp.	2824-2847
Robert L. Statton (Vice President, Respondent SAFECO)	resp.	2853-2874
Robert C. Mitchell (Vice President, Respondent SAFECO (Idaho))	resp.	2875-2952
Norman T. Smith (Executive Director, Ohio Title Insurance Rating Bureau)	resp.	2958-3046
Peg Ising (Assistant Chief, Property-Casualty Division, Ohio Department of Insurance)	resp.	3047-3068
Robert L. Ratchford (Former Director, Ohio Department of Insurance) [8]	resp.	3069-3102
Robert T. Haines (Former General Underwriting Counsel, Respondent Chicago Title)	resp.	3107-3243
Marvin C. Bowling, Jr. (Executive Vice President (Law), Respondent Lawyers Title) [9]	resp.	3265-3420

package of services they offer, respondents provide search and examination and settlement or escrow services.³

2. Respondent Tigor Title Insurance Company ("Tigor") is a corporation organized under California law, with its principal place of business located at 6300 Wilshire Boulevard, Los Angeles, California.⁴ Tigor, which conducts its title insurance business in 49 states and the District of Columbia, maintains approximately 300 branch offices and has over 5,000 employees.⁵ For the year ending December 31, 1983, Tigor reported income of \$219,869,518 from title insurance premiums and \$62,488,172 from other sources.⁶

3. Respondent Chicago Title Insurance Company ("Chicago Title") is a corporation organized under Missouri law, with its principal place of business located at 111 W. Washington Street, Chicago, Illinois.⁷ Chicago Title, which conducts its title insurance business in 49 states and the District of Columbia, maintains approximately 150 branch offices.⁸ For the year ending December 31, 1983, Chicago [10] Title reported income of \$205,525,412 from title insurance premiums and \$51,713,074 from other sources.⁹

4. Respondent SAFECO Title Insurance Company ("SAFECO") is a corporation organized under California law, with its principal place of business located at 13640 Roscoe Boulevard, Los Angeles, California.¹⁰ SAFECO, which conducts its title insurance business in 46 states and the District of Columbia, maintains branch and agency offices throughout the United States.¹¹ For the year ending December 31, 1983, SAFECO reported income of \$163,088,978 from title insurance premiums and \$29,713,045 from other sources.¹²

5. Respondent Lawyers Title Insurance Corporation ("Lawyers Title") is a corporation organized under Virginia law, with its principal place of business located at 6630 West Broad Street, Richmond, Virginia.¹³ Lawyers Title conducts its title insurance business through approximately 2500 branch and agency offices

³ CX 156Z-2, Z-4, CX 247F-G, CX 250H-"T", CX 293D.

⁴ Complaint and Tigor's Answer, ¶2. Prior to 1982, Tigor was known as Pioneer National Title Insurance Company. CX 164A.

⁵ CX 165B.

⁶ CX 148Z-52, CX 258.

⁷ Complaint and Chicago Title's Answer, ¶3.

⁸ CX 167B.

⁹ CX 149Z-28.

¹⁰ Complaint and SAFECO's Answer, ¶4.

¹¹ CX 169.

¹² CX 150Z-22.

¹³ Complaint and Lawyers Title's Answer, ¶6.

located in 49 states and the District of Columbia.¹⁴ For the year ending December 31, 1983, Lawyers Title reported income of \$98,302,394 from title insurance premiums and \$16,395,472 from other sources.¹⁵ [11]

6. Respondent Stewart Title Guaranty Company ("Stewart") is a corporation organized under Texas law, with its executive offices located at Stewart Building, Galveston, Texas.¹⁶ Stewart conducts its title insurance business in 45 states and the District of Columbia through regional, district, and state offices.¹⁷ For the year ending December 31, 1983, Stewart Title reported income of \$97,443,521 from title insurance premiums and \$3,382,457 from other sources.¹⁸

7. In 1982, respondents Tigor, Chicago Title, SAFECO, Lawyers Title, and Stewart, collectively accounted for 57 percent of the \$1.35 billion title insurance industry. Tigor with 16.5 percent of the market, Chicago Title with 12.8 percent, Lawyers Title with 12 percent, and SAFECO with 10.3 percent, are the four largest title insurers. First American Title Insurance Company, a named respondent which has a consent settlement agreement pending before the Commission, is the fifth largest title insurer with 9.7 percent of the market. Stewart, which accounts for 5.4 percent of the market, is the eighth largest title insurer.¹⁹

B. COMMERCE

8. Respondent insurers write policies and provide search and examination and settlement services in all states except Iowa, which has a statutory prohibition against issuing title insurance.²⁰ [12]

9. The search and examination of title and the issuance of title insurance policies are integral parts of interstate real estate transactions in which loans either cross state lines or are guaranteed by agencies of the United States located in Washington, D.C. Typically, these lenders or loan guarantors require that the title to the real estate

¹⁴ CX 173.

¹⁵ CX 152Z-84.

¹⁶ Complaint and Stewart's Answer, ¶7.

¹⁷ CX 174B.

¹⁸ CX 153Z-22.

¹⁹ Market shares are measured in terms of gross operating revenues. CX 166Z-3. See also CX 293E. While Stewart's national market share is relatively small, it is the leading title insurer in Texas and it is strongly positioned in the West and Southwest. CX 293G.

²⁰ CX 171.

securing the loan be searched and examined, and that a title insurance policy be issued.²¹

10. Similarly, the settlement services provided by respondents are part and parcel of interstate real estate transactions.²²

11. Respondents offer their search and examination and settlement services through nationwide networks of regional, divisional, and branch offices, which are subject to and benefit from the financial support, control, direction, policies, and national advertising and marketing campaigns of respondents' home offices.²³

*C. TITLE, THE ABSTRACT OF TITLE, THE
ATTORNEY'S OPINION, TITLE INSURANCE*

Real Estate Title

12. Title is a legal concept covering the bundle of rights possessed by the owner of real property. These rights, which are recognized and protected at law, include possession, use, control, enjoyment, and the power to transfer the property.²⁴ [13]

13. In real estate transactions in which title is to be transferred, buyers are interested in determining whether there are any title defects in the form of liens, encumbrances, easements, covenants, restrictions, or claims that might interfere with the quiet enjoyment of possession. This translates into the buyer's need to know if a seller's title is limited or affected by such pre-existing rights or interests of others as the right of a utility company to maintain a right-of-way across the property, or the marital rights of a prior spouse of the seller, or the ability of an adjoining landowner to invoke a restrictive covenant, or the existence of enforceable mortgages, use restrictions, tax judgments, mechanic's liens, and other liabilities, limitations, charges, or liens.²⁵

14. Similarly, the interest of a mortgagee involved in a real estate transaction centers around his need to know of the existence of any clouds on title that may adversely effect the priority of his own lien.²⁶

15. Historically, there have emerged several ways of assuring

²¹ Haines 3231, Bowling 3316; CX 171, CX 182D, CX 196Z-136 to Z-137, CX 237T-W, CX 247C, CX 253Z-31 to Z-32, CX 303A; RX 431M.

²² CX 155D, CX 196Z-60 to Z-74, CX 238F-G; RX 394Z-58 to Z-74, RX 409L, RX 427Z-135, RX 431Z-116 to Z-118.

²³ CX 247B; RX 413G, "T", RX 442F, RX 444J, L; see also Fromhold 955-56, Bonita 1253.

²⁴ CX 155 "T", CX 253Z-3; RX 409Z-32.

²⁵ CX 87X-Y, CX 253Z-3; RX 431M. By custom, the cost of a title evidence is borne by the buyer. RX 436C.

²⁶ CX 156Z-62 to Z-63, CX 237T-W.

buyers and lenders of the existence of good title (see Findings 16-39).²⁷

The Abstract of Title

16. The earliest evidence of good title (which persists to the present day) was provided by title searchers (sometimes called "abstractors") who originally were in the business of researching public records and providing purchasers or lenders with a summary (called the "abstract of title") of all the documents forming a chain of title.²⁸

17. The purpose of the abstract of title was to arrange in chronological order all pertinent information respecting title that appeared on the public record, the assumption [14] being that the buyer or lender would then either cure the revealed defects or decide not to go forward with the purchase or loan.²⁹

18. If in making a purchase or loan decision, the buyer or lender relied on what turned out to be an incomplete or inaccurate abstract, the abstractor was only liable for negligent failure to exercise the level of vocational skill expected of title searchers in the locality where the search was conducted. In the absence of proof of negligence, the abstractor was not liable for mistakes, errors, or omissions in the search.³⁰

19. The negligence liability of the abstractor only attached to errors and omissions in searching public records. The abstractor had no liability for failure to uncover unrecorded defects in title.³¹

20. Over the years, the abstracting business developed several refinements. First, abstractors began to issue "certificates of title," which certified that title vested as shown in the documents searched; still later, abstractors actually guaranteed title and set aside cash reserves to assure their capability for paying losses.³²

21. Presently, the abstract of title is rarely sold to a buyer or lender who relies on it in lieu of the other, more widely used evidences of good title such as an attorney's opinion or title insurance.³³

22. Typically, the modern commercial abstract company performs its searches and examinations as an agent for an insurance compa-

²⁷ See also CX 253Z-3 to Z-4, Z-9; RX 409Z-32.

²⁸ Bowling 3335; CX 87Z-114 to Z-119, CX 154C-E, CX 155C, CX 156V, Z-29, Z-234, CX 249D, CX 253Z-4 to Z-5, CX 261F-G, CX 310B-C; RX 409C, RX 427Z-132, RX 433.

²⁹ CX 189F, CX 253Z-4 to Z-5.

³⁰ CX 91Z-36, CX 246E, CX 253Z-5 to Z-6.

³¹ CX 253Z-6, CX 261F-G.

³² CX 154C-E, CX 155D, CX 253Z-5; RX 391D-E.

³³ Everbach 1414; CX 261F-G.

ny,³⁴ or it may be retained by an [15] independent attorney, attorney-agent, or insurance company personnel who then examine the abstract before issuing an attorney's opinion or a title insurance policy.³⁵

Attorneys' Opinions

23. Since the abstract of title did not include an evaluation of the legal significance of the recorded documents, there eventually evolved a practice, which continues to this day, of submitting either original title records or abstracts to a qualified independent real estate attorney (sometimes called a "conveyancer") who makes a critical review of the records and then renders for buyers or lenders an attorney's opinion or a certification of title.³⁶

24. These independent real estate attorneys are also retained by title insurers or their agents for the purpose of providing an attorney's opinion prior to the issuance of a title insurance policy.³⁷

25. Like the abstract, the main purpose of the attorney's opinion is to give the buyer or lender a full accounting of any title defects so that an informed decision can be made as to whether to attempt to cure the revealed defects or to just drop the deal. The attorney's opinion merely adds to the abstract an interpretation of the legal significance of documents uncovered in the search.³⁸

26. The attorney's opinion, like the simple abstract, carries with it limited liability for errors or omissions, amounting essentially to malpractice liability grounded [16] on negligence or failure to meet the accepted standard of professional legal competence in the locality where the attorney's opinion was given.³⁹ If the attorney conducted the search himself, he is liable for negligence in both the search and examination. In those instances, however, in which the attorney's opinion is based on an abstract prepared by an abstractor, his liability

³⁴ Bowling 3336; CX 172F; RX 488H.

³⁵ Anito 293-95, Cooper 365-67, 370-72 Ippel 699, 702, Fromhold 954-55, Everbach 1341, Donohoe 1665, Bowling 3379; CX 87M, CX 91Z-35, CX 145A, CX 175B; CX 237Z-2, CX 245B, CX 261F-G. Because the work of the abstractor is directly affected by local real estate laws and customs, the present-day commercial abstract company is usually a small, locally-owned business. CX 261R-S.

³⁶ Everbach 1314; CX 154D, CX 156Y to Z-1, CX 175B, CX 182E-F, CX 189Z-15 to Z-16, CX 196Z-136, CX 253Z-5 to Z-6, CX 262E-F; RX 391E. If the attorney conducts the search himself, he issues a certification of title. CX 156Y to Z-1.

³⁷ CX 172F; RX 488H.

³⁸ Cooper 368-69; CX 189Z-15 to Z-16; RX 489E-F.

³⁹ Anito 281; CX 182D, CX 196Z-136, CX 237P-R, CX 253Z-5; RX 489D.

is limited to due care in the preparation of an opinion based on the information reviewed.⁴⁰

27. Also, as is the case of the abstract, an attorney rendering an attorney's opinion is not liable for either hidden defects not discoverable by a diligent record search or for inaccuracies in the public records.⁴¹

28. The liability of the attorney for his opinion is also limited by his solvency, and ends with the death of the attorney or the tolling of a statute of limitations.⁴²

29. A variation of the attorney's opinion is the so-called "bar fund"; in effect, a title insurance company organized by independent attorneys who then issue policies based upon their own searches and examinations.⁴³ Bar funds, which offer an additional layer of protection beyond the attorney's opinion or the simple abstract by covering losses from hidden defects, were organized as the bar's answer to loss of search and examination business to title insurance companies.⁴⁴ [17]

Title Insurance

30. The origin of title insurance as a form of evidence of good title traces to an 1863 Pennsylvania case, *Watson v. Muirhead*, 57 Pa. 161 (1868), which held that an attorney rendering an attorney's opinion was liable only for negligence. The negligence standard of *Watson* imposed a significant barrier to recovery for errors or omissions made by abstractors or attorneys in conducting a title search and examination.⁴⁵

31. Title insurance (technically, an agreement to indemnify an owner or mortgagee for loss or damage sustained by reason of a defect in title not explicitly excluded or excepted from the policy) was designed to go beyond either the abstract or the attorney's opinion by imposing on insurance companies liability for errors in the conduct of the search and examination irrespective of any negligence in carrying out the process.⁴⁶

32. Title insurance covers errors or mistakes made by those who

⁴⁰ Ippel 659, Everbach 1325-26; CX 196Z-136, CX 253Z-5, CX 261F-G.

⁴¹ Anito 281; CX 182E-F, CX 246E, CX 253Z-6 to Z-7.

⁴² CX 196Z-136, CX 237P-R, CX 246E, CX 253Z-6 to Z-7; RX 489D.

⁴³ Ferraro 2319-23; CX 196Z-153 to Z-155. In Connecticut, however, the bar fund is not regulated by the state insurance department. Ferraro 2319-23.

⁴⁴ Ferraro 2319-23. As it happens, title insurers themselves, like respondent Lawyers Title, have been formed by lawyers who specialized in real estate work. RX 456F.

⁴⁵ Everbach 1326-28; CX 237P, CX 310B-D; RX 391D-H, RX 417Z-32.

⁴⁶ CX 155"T", CX 196Z-136, CX 319B; RX 417Z-31, RX 491A.

perform the search and examination on behalf of the insurer whether or not they are agents, independent contractors, or employees (see Findings 40-57).⁴⁷

33. Title insurance in its present form also exceeds the protection given by abstracts or attorneys' opinions in that it survives even if the person who conducted the search and examination dies.⁴⁸

34. Unlike the abstract or an attorney's opinion, title insurance includes the obligation to defend in the event that an insured is sued.⁴⁹ [18]

35. Like the abstract and the attorney's opinion, however, title insurance policies are basically assurances to the buyer or lender that defects in title discoverable from examining the public record have been brought to the attention of the buyer or lender so that they can cure the defect or decide not to go ahead with the deal.⁵⁰

36. A secondary purpose of title insurance, developed over the years and going beyond the scope of the abstract or attorney's opinion, is to protect the buyer or lender from hidden or so-called "off-record" risks not discoverable from examination of public records such as forgery, missing heirs, previous marriage, impersonation, or confusion in names.⁵¹

37. Title insurance is largely a post-World War II phenomenon whose growth reflects the need for a standardized form of assurance of good title to complement standardized mortgages that are resold in a nationwide secondary mortgage market.⁵²

38. While title insurance is now the predominant form of title evidence, the attorney's opinion is still commonplace especially in the New England and Southeastern states.⁵³ As indicated in Findings 21-22, the abstract of title is now rarely used alone as an evidence of good title, and instead usually serves as the basis for issuing either an attorney's opinion or the report that precedes the issuance of a title insurance policy.⁵⁴ [19]

39. Viewed from a market perspective, the search and examination of title is a service business acquired by respondents and other title

⁴⁷ See also Bowling 3363; CX 182E.

⁴⁸ CX 196Z-136, CX 237P.

⁴⁹ CX 182E, CX 253Z-9; RX 417Z-31.

⁵⁰ See Findings 58-59.

⁵¹ CX 82V-W, CX 87Y to Z-1, Z-25 to Z-26, CX 154E-F, CX 182E-F, CX 237P, CX 261"'"T"-K; RX 391F-H
There are several major areas (which may be viewed as off-record risks) that are excepted from the standard coverage, such as easements and liens not shown on the public record (see Finding 87 and CX 250H

⁵² Ippel 699-700; CX 91Z-37 to Z-38, CX 182D, F, CX 189Z-17, CX 196Z-136 to Z-137.

⁵³ Ippel 699, Everbach 1411-17, Bowling 3367; CX 154D, CX 189F, CX 261F-G; RX 391E, RX 436

⁵⁴ Ippel 701-02, Fromhold 954-55, 1005; CX 87M, CX 156Z-2, CX 175B, CX 237Z-2; see also Finding 8

insurers as a result of their aggressive merchandising of title insurance (at the expense of abstracts and attorneys' opinions) as a superior way of evidencing good title.⁵⁵

*D. ATTORNEY-AGENTS, APPROVED ATTORNEYS, AND EMPLOYEES
OF TITLE INSURERS*

40. As indicated in Findings 22 and 24, a title insurance policy may be based on a search and examination conducted by an independent abstractor or an unaffiliated independent attorney. Most title insurance policies, however, are issued after the search and examination has been made by either attorney-agents, approved attorneys (a variation of the independent attorney), or employees of respondent insurers (see Findings 41-57).

41. It is a common practice in the title insurance industry for searches and examinations to be conducted by attorneys who have been designated as agents of title insurers.⁵⁶ These attorney-agents often are recruited from the ranks of independent attorneys (see Findings 23-28) who formerly rendered attorneys' opinions or issued certificates of title.⁵⁷

42. Agents for title insurers have also been drawn from the body of independent commercial abstractors who own title plants,⁵⁸ and who may continue to offer abstracting services apart from their work as agents for title insurers.⁵⁹ [20]

43. Agents, whether they are attorneys or abstractors, are liable (like the independent attorney rendering an attorney's opinion) to the title insurer for negligence in conducting the search and examination.⁶⁰

44. The relationship between agents (especially attorney-agents) and title insurers is fraught with opportunities for directing the placement of title insurance business. While ostensibly acting as independent legal counsel to a usually uninformed buyer, the attorney-agent is in a position to channel the consumer's title

⁵⁵ Ippel 699-700, Ferraro 1219, 1239-41, Donohoe 1664-65, 1667-68, Bowling 3293; CX 87W to Z-8, CX 154A-H, CX 156Z-2, CX 182D-F, CX 189Z-16, CX 196Z-150 to Z-151, CX 236E, CX 237P-W, CX 246A-L, CX 249D, CX 253Z-3 to Z-11, CX 261H, CX 262E-G, CX 292D-E, CX 311A-J, CX 312E, CX 313B, CX 319A-B; RX 312, RX 391D-H, RX 394Z-31, RX 475-RX 475E, RX 476A, RX 484A, RX 489D-E.

⁵⁶ Ippel 698; CX 182G-H; RX 444N, RX 491A-B.

⁵⁷ Ferraro 1241; CX 182G-H.

⁵⁸ Armstrong 1135, Everbach 1341, Bowling 3376; CX 228A.

⁵⁹ Ippel 698, Armstrong 1135.

⁶⁰ Cooper 388; CX 145C, CX 146D; RX 410J. The willingness of respondent insurers to test agent liability is tempered by the strategic importance of agents in garnering insurance business. Bowling 3300-02, 3311; RX 487N-Q; see also Finding 44.

insurance business to the agent's insurer-principal in exchange for commissions, commonly referred to in the title insurance business as "agent's retention" since the agent collects and transmits the premium less his "retention" to the insurer. The agent's retention, however, includes not only the actual cost of conducting the search and examination, but may also reflect his ability to negotiate for a large part of the total insurance premium (as much as 90 percent) on the basis of his strategic position in the real estate transaction.⁶¹ In point of fact, the growth of a title insurer is largely tied to its ability to solicit and retain attorney-agents who can influence the placement of business.⁶²

45. "Approved attorneys" are independent attorneys who have been formally designated by respondent insurers as qualified to conduct a search and examination prior to the issuance of a title insurance policy.⁶³ [21]

46. An approved attorney, who often will graduate to the attorney-agent status described in Findings 41-44,⁶⁴ may also continue to function as an unaffiliated independent attorney, and in that capacity conduct searches and examinations and issue opinions and certificates for individual buyers or sellers or even other insurance companies which have not designated him as an approved attorney.⁶⁵ Moreover, an attorney may function as an approved attorney for one insurer and an attorney-agent for another.⁶⁶

47. An approved attorney is neither an employee nor an agent of the title insurer which designated him as an approved attorney.⁶⁷

48. The approved attorney may perform the search himself or base his examination upon the abstract of an independent abstractor.⁶⁸

49. The approved attorney's analysis, which is indistinguishable

⁶¹ Anito 279, Sinkhorn 917-18, Armstrong 1165, Ferraro 1241-42, Plotkin 2681-84, 2705-12, DiSanto 2737-40, 2799-2808, Bowling 3301; CX 30Z-85, CX 145E, CX 156Z-7, CX 182G-H, CX 232G, CX 247X-Y, CX 257A, CX 278W-X, CX 301B, CX 306B, CX 307B, CX 323J, CX 324L, CX 333Z-11 to Z-15, CX 334C-D; RX 3E, RX 23K-L, RX 32, RX 114, RX 502Z-55.

⁶² Ferraro 2356-57, Plotkin 2698-99, Bowling 3301; CX 166R, CX 237Z-3, CX 293E.

⁶³ CX 160G-H; RX 410L-M, RX 491A.

⁶⁴ CX 182G-H. Approved attorneys (usually lawyers with a real estate practice) are often selected on the basis of their ability to influence the placement of title insurance business. Bowling 3367. From the approved attorney's standpoint, the relationship is desirable because not only may they graduate to the status of an attorney-agent (and the prospect of large "retentions") but as an approved attorney he can expect to receive substantial fees from conducting searches, examinations, and settlements (DiSanto 2806, Bowling 3368; CX 30Z-85; RX 410L) as well as whatever other advantages accrue from being identified with a national title insurance company in professional directories. Sinkhorn 847.

⁶⁵ Cooper 364-70.

⁶⁶ Cooper 370.

⁶⁷ RX 491A.

⁶⁸ CX 160G-H.

from the attorney's opinion or certification of the ordinary independent attorney (see Findings 23-25), is relied upon by the insurer or the agent of the insurer in issuing initially a binder or commitment, and eventually a title insurance policy (see Finding 80).⁶⁹ [22]

50. The approved attorney, however, unlike the attorney-agent prepares neither the preliminary binder leading up to the issuance of the title policy nor the title policy itself.⁷⁰

51. The approved attorney, like any other independent attorney rendering an attorney's opinion for an insurer or an insurer's attorney-agent, is liable to the insurer for failure to exercise due diligence and reasonable professional skill in the search and examination of public records.⁷¹

52. If the approved attorney's examination of title is not based on his own search but rather upon a commercial abstract, liability is limited to the exercise of reasonable care and due professional skill in rendering an opinion in light of the information contained in the abstract.⁷²

53. The approved attorney receives no financial remuneration from the title insurer. The approved attorney bills his client—the buyer or the lender—for the cost of conducting the search and examination.⁷³

54. Respondent insurers do not set, either jointly or separately, the fee that the approved attorney charges his client. The approved attorney sets his own fees.⁷⁴

55. In addition to approved attorneys and attorney-agents, searches and examinations are conducted by employees of respondent insurers stationed in respondents' branch offices.⁷⁵ [23]

56. The mix of attorney-agents, approved attorneys, and direct employees not only varies according to custom and geography, but also reflects how successful a particular title insurer has been in enlisting the support of well-established attorneys who can influence the placement of their client's insurance business.⁷⁶

⁶⁹ Sinkhorn 928-29, Fromhold 953, 1021, Clayton 1838, Bowling 3371-72; CX 155D, CX 160G-H, CX 182G, CX 237Z-9 to Z-10; RX 3E.

⁷⁰ CX 132F, CX 160G, CX 182G, CX 196Z-11 to Z-12; RX 410L, X to Z-1, RX 491A.

⁷¹ CX 160G, CX 237Z-9 to Z-10, CX 257A.

⁷² CX 160G-H.

⁷³ CX 30Z-85, CX 160G, CX 182G; RX 3E.

⁷⁴ Fromhold 1020-22, Bowling 3363-64; CX 30Z-85.

⁷⁵ CX 87M, CX 175C, CX 237Z-2; RX 488H.

⁷⁶ Ippel 624; CX 237Z-3 to Z-4, CX 262"™"; RX 491A; see also Finding 44. The mix may also reflect the intensity of the competitive struggle between attorneys and insurance companies for the search and examination and settlement business. In some areas, respondent insurers may have been compelled to use their own employees because of organized bar opposition to having independent lawyers work as insurance company agents or approved attorneys. See CX 196Z-150 to Z-151.

57. Essentially all title insurers operate in the same way, and while there may be differences among respondent insurers as to how business is allocated among employees, agents, and approved attorneys, the practices and policies described in these findings are fairly attributable to all respondents.⁷⁷

E. THE SEARCH AND EXAMINATION PROCESS FOR ABSTRACTS OF TITLE, ATTORNEYS' OPINIONS, AND TITLE INSURANCE

58. Irrespective of the form in which the buyer or lender are assured of good title (*i.e.*, through abstracts, attorneys' opinions, or title insurance) and irrespective of the hat worn by the searcher and examiner (abstractor, independent attorney, attorney-agent, approved attorney, or insurer's employee) the condition of the title is determined by the same search and examination process.⁷⁸ The process is the same because in all cases the objective is the same—to uncover significant impediments to ownership.⁷⁹ [24]

59. Neither the use by respondents and their agents of insurance jargon to describe the purpose of their searches and examinations—in their view to determine what risks they are willing to insure⁸⁰—nor the existence of state statutory requirements conditioning the issuance of a title insurance policy upon the conduct of a search,⁸¹ materially changes the nature of the search and examination conducted prior to the issuance of an insurance policy as compared to the process used before an abstract or an attorney's opinion are rendered. In all instances, the objective of the searchers and examiners is to provide a statement of the status or condition of title, and to call the attention of the buyer or lender to defects discoverable from the public records so that these clouds on title are corrected before the purchase is made, or if the risks are too great, to call the deal off.⁸² In the words of respondent Ticor:

⁷⁷ See Bowling 3374-75.

⁷⁸ Anito 280-81, Cooper 370-72, 383, Fromhold 1003-04, Haines 3234-35; CX 155D, CX 172F, CX 182G, CX 237Z-9 to Z-10, CX 244"O"-R, CX 245B, CX 247"U", CX 249D, CX 250G, CX 310"U"; RX 290A, RX 488H. While the searches and examinations conducted by an independent attorney, approved attorney, and attorney-agent are identical and indeed the same person may wear all three hats, the record indicates that the standard abstract is more detailed than the typical product of the independent attorney, approved attorney, or attorney-agent (see Findings 16-17, 81).

⁷⁹ Everbach 1395-96; CX 87M, Z-10 to Z-11, CX 175B-C, CX 182E-F, CX 247F-G, CX 253Z-3 to Z-4, CX 261J-K, CX 262C-D, CX 301B, CX 302B, CX 308B; RX 394Z-47.

⁸⁰ Ippel 627, Malaker 745-47, Fromhold 1033, Waiwood 1079, Everbach 1329, Bowling 3337.

⁸¹ See, *e.g.*, JXA, p. 111.

⁸² Anito 265-67, Cooper 421, Quadraccia 490, Sinkhorn 887-89, Fromhold 970, 1033, Waiwood 1103, Haines 3224-25, 3240-43, Bowling 3335; CX 87H-J, N, Z-10 to Z-11, CX 91Z-35, CX 175C, CX 194, CX 236B, CX 246G, CX 247D-G, CX 249D, CX 252S, CX 253Z-9 to Z-10, CX 261"U"-K, CX 262C-D, CX 293D,

(footnote cont'd)

Basically, title insurance is the company's opinion of the ownership and marketability of title to a particular parcel of real property. This can only be ascertained after a thorough and complete search of all the records affecting title to the parcel insured. This search is much more extensive and requires more time than any other investigation conducted in connection with the issuance of other forms of insurance.

A title company is required, not only by law, but in order to make quick and accurate searches, to keep complete records covering all the lands in a particular county. A title company is a service organization and performs a service for those interested in buying, selling and loaning money on real estate. One may make his own search because all of the records necessary to complete such a search are available at the Court House, the City Hall and the Federal Court House. How this search is made and the accuracy of such a [25] search will depend upon an individual's skill, knowledge and perseverance. It could take days, weeks or months, and after completion, the verdict would be inconclusive because with the passage of time, additional filings have been made which have to be considered and construed. This task would be akin to trying to dig away a hill of sand which slides continuously. Through a system of records, kept on each individual parcel, the title company is able to complete this search on a definite date with certainty. When you purchase a title insurance policy, you are buying the services of experts. The company is willing to back the opinion of these experts with the additional feature of insurance. Hence, the use of the word insurance, when naming the product of title insurance.⁸³

Title Search

60. Whether the ultimate product is an abstract, attorney's opinion, or title policy, the first part of the search and examination process—the search—proceeds on the basic premise that important interests in real property (deeds, mortgages, leases, grants, easements, judgments, tax liens) must be made a matter of public record by recording the document in the county recorder's office where the property is located.⁸⁴

61. By recording evidence of a claim or interest in real property, legal or "constructive" notice is given—that is, all persons, including prospective buyers and lenders, are presumed to know what is in the public records even though they do not have actual knowledge.⁸⁵

62. From these public records, the searcher endeavors to establish a "chain of title," consisting of a chronological account of recorded

CX 294D-E, CX 297, CX 298B, CX 299B, CX 311" T", CX 318B, CX 320Z-157 to Z-159; RX 3D, RX 396C, RX 413D, RX 417Z-34, RX 431M-N, RX 488" T".

⁸³ CX 250G. See also CX 308B ("Title Insurance combines the function of the abstracter, in making the chain of title, and the attorney in his examination of the title, plus coverage to the land owner in the form of insurance.")

⁸⁴ CX 155" T", CX 156Z-32 to Z-33, CX 175B, CX 196Z-16, CX 247E; RX 389Z-245 to Z-253, RX 413C, RX 431N-P.

⁸⁵ CX 156Z-32 to Z-33, CX 247E, CX 253Z-3 to Z-4; RX 413C.

instruments affecting title, beginning with the earliest and concluding with the latest.⁸⁶ [26]

63. The "direct" search method of establishing the chain of title entails an examination of public records for all documents relating to the property in question.⁸⁷ Historically, the presumptive search period is 60 years, but depending upon local custom or the existence of an earlier, reliable title policy, or a marketable title act, the search may be considerably shorter.⁸⁸ In an especially complex transaction, the search may go well beyond 60 years to the issuance of the original patent by the sovereign.⁸⁹

64. Typically, the public records searched include county land records (deeds, easements, and mortgages) municipal records covering sewer, sidewalk, and other assessments, tax collector records, and state and federal court records showing bankruptcies, divorces, judgments, and civil actions indicative of liens or other enforceable interests in the property.⁹⁰

65. Instead of starting with public records, which often are not efficiently organized, a search (especially in large metropolitan areas) may be initiated by use of a privately owned "title plant" or "abstract plant." A title plant contains virtually complete summary information (as well as some reproductions) from the public records affecting real estate title in a limited geographic area, organized and indexed in a way that enables a title search to be performed in a fraction of the time and with greater accuracy than a direct search of the public records.⁹¹ [27]

66. Title plants are owned and operated by abstractors, attorneys, real estate brokers, and title insurers or their agents.⁹²

67. Still another method of conducting a title search is to go back no further than a pre-existing title policy or a pre-existing abstract.⁹³

68. There are no special educational or training requirements for becoming a title searcher, and with training and experience, high

⁸⁶ Sinkhorn 852-53, 856-58, Haines 3158-59; CX 196Z-16; RX 409K, RX 427Z-135, RX 431N-P.

⁸⁷ CX 196Z-16 to Z-18; RX 409Z-26, Z-33.

⁸⁸ Anito 291-93, Quadraccia 510-11, Ippel 704-05, Malaker 723-26, 743-44, 792-93, Sinkhorn 853-55, 923-24, Waiwood 1053-54, Armstrong 1147-48, Ferraro 1198; CX 87Z-32 to Z-33, CX 160M-N, CX 196Z-18, CX 223A, CX 294D.

⁸⁹ Quadraccia 511; CX 160M-N, CX 196Z-18, CX 223A. If a searcher has confidence in the work of a particular abstractor, he may begin the search from the point in time when the abstract ended. CX 196Z-19.

⁹⁰ Anito 254, 262-63, Malaker 722, 728-30; CX 196Z-17 to Z-18, CX 247G.

⁹¹ CX 196Z-19, CX 261L-M; RX 401Z-21 to Z-24, RX 409Z-33, RX 427Z-132, RX 488H.

⁹² CX 196Z-36; RX 290A, RX 335, RX 401Z-21 to Z-24. In some areas of the country, title plants are cooperative efforts operated by several title insurers or their agents. CX 196Z-54 to Z-55.

⁹³ Anito 251-53, 270-72, 287-89, Quadraccia 510, Waiwood 1055-56, 1097-98, 1121-22, Armstrong 1146, Bonita 1267-68, Donohoe 1665; CX 196Z-19, CX 223A; RX 389Z-246.

school graduates soon acquire the expertise necessary to move from routine searches to more complex assignments.⁹⁴

Examination

69. The examination phase of the search and examination process involves a critical analysis or interpretation of the condition of title as revealed in the documents uncovered by the search.⁹⁵

70. Examination may be done by approved attorneys, attorney-agents, independent attorneys, searchers, or anyone else who is experienced in interpreting title documents and is knowledgeable about real estate law.⁹⁶ Some examiners dispense entirely with a separate search and instead simply combine the search and examination in a single process.⁹⁷ [28]

71. Similarly, while search is commonly identified as a separate and distinct process from examination by title insurers, and in large insurance company or agency offices the two processes are often performed by separate staffs, in the smaller offices, and in matters involving complex questions of title, the two processes tend to merge.⁹⁸

F. SEARCH AND EXAMINATION AND RISK ASSUMPTION

72. Respondents' retained insurance expert,⁹⁹ as well as respondents' officers and agents, argued that search and examination undertaken prior to the issuance of a title insurance policy is either "underwriting" or part of what they referred to as the "underwriting process" because it is on the basis of the search and examination that risk (chance of loss) is identified and a decision is made either to accept or reject it.¹⁰⁰ This effort of affixing the lofty "underwriter" label to searchers and examiners proceeds initially from the premise that all providers of information respecting the property to be insured

⁹⁴ Fromhold 973, Armstrong 1179; CX 172F. See also Armstrong 1151 for testimony that searchers simply pull every document that is even remotely relevant "and then leave it to the examiners or at least the head searcher to throw them out or not" and CX 196Z-36 where one respondent describes the work of a searcher as "akin to drudgery."

⁹⁵ Anito 264; CX 155F, CX 156Y, Z-2, CX 160G-H, CX 237M, CX 244S, CX 249D, CX 253Z-5, CX 262"O"; RX 401Z-30 to Z-34, RX 405D.

⁹⁶ CX 262"O".

⁹⁷ CX 87M, CX 253Z-5, CX 262F.

⁹⁸ Anito 297, Ippel 631, 635-36, Malaker 720, Fromhold 978-79, Waiwood 1049-50, Ferraro 1200, Bonita 1260-62, Bowling 3336; CX 196Z-36, CX 237M.

⁹⁹ The opinions of the retained expert, Robert Holtom, were uninformed by any experience whatsoever with title insurance. Holtom 1493, 1594.

¹⁰⁰ Ippel 629, Malaker 730, Fromhold 977, Waiwood 1067-68, Armstrong 1159, Bonita 1285-88, Everbach

must be engaged in "underwriting" (or, if you will, be part of the "underwriting process") although this expansive view of underwriting would of necessity embrace the abstractor, the independent surveyor, the approved attorney, and practically anyone else who gives insurers some information bearing on the subject of the policy, including presumably the insured himself who provides his name and a description of the property, and perhaps even the receptionist who records this information on the face of the policy.¹⁰¹ Going beyond the illogic of this open-ended definition, this endeavor to [29] elevate searchers and examiners to the status of "underwriters" also fails to take into account the fact that the search and examination conducted for title insurance purposes is virtually indistinguishable from the process undertaken for the non-insurance (and concededly non-"underwriting") purposes of rendering abstracts or attorneys' opinions, and that irrespective of the purpose, search and examination is carried out by a corps of searchers, abstractors, conveyancers, attorney-agents, and approved attorneys who move freely from one form of title evidence to another without any perceptible change in what they do.¹⁰² Moreover, to the extent that respondents' expansive concept of underwriting rests on the assumption that searchers and examiners for title insurers have discretion about assuming risk, the record evidence is that in an industry in which standard forms predominate and company manuals have reduced most transactions to a set routine, this discretion is narrowly circumscribed.¹⁰³ This strained effort at rolling search and examination, underwriting, and risk into one ball of wax is also suspect on its face since the basic approach of respondents in conducting their title insurance businesses is not to assume any significant risks uncovered by searchers and examiners.¹⁰⁴ Finally, respondents' strained extension of the underwriter label to searchers and examiners is fundamentally unsound since the title policy, in contrast to casualty insurance, does not insure against the happening of some unforeseen future event, and while the searchers and examiners may bend every effort to eliminate risk by

¹⁰¹ Malaker 717-19, Fromhold 977-78, 1005, 1013-14, Everbach 1393-99, 1402-07, Holtom 1541-43, 1584-86, 1587-89, Haines 3196-97. See, e.g., Fromhold 977, 1108 and RX 413C for the pivotal roles played by the surveyor and abstractor (both independent contractors not connected with insurers) in the search and examination process.

¹⁰² See Findings 16-71. The occasional use of the "underwriter" title in respondents' manuals in no material way changes the way in which search and examination are conducted for a title policy as compared to the search and examination undertaken for any other evidence of title. See RX 401Z-27 to Z-34.

¹⁰³ See Findings 73-96 and CX 172F.

¹⁰⁴ See Findings 73-96, 99.

finding recorded title defects, [30] they are not engaged in the underwriting function of assuming and spreading risk among a large universe of insureds.¹⁰⁵

73. Consistent with respondents' guiding principle of not assuming risk, their primary objective before issuing a title insurance policy is in the conduct of an accurate search of the public title records for the purpose of uncovering possible defects which are to be cured by the insured or excepted from coverage.¹⁰⁶

74. Also consistent with respondents' risk-avoidance approach are their company manuals, underwriting guides, and other directives, which are replete with admonitions that risks are to be excepted from coverage.¹⁰⁷ The testimony of respondents' officers and agents directed at diminishing the importance of these directives by claiming in effect that searchers and examiners have wide latitude in ignoring them,¹⁰⁸ is not credible. The insurer-agent contracts as well as the underwriting manuals, guides, and directives themselves instruct employees and agents that they are to be followed to the point that agents may be liable for damages if they are not followed.¹⁰⁹ It is also significant that while these materials are constantly being updated, no documents were offered by respondents indicating that the admonitions [31] respecting risks have been significantly modified.¹¹⁰ On the contrary, respondents' own witness acknowledged that the manuals, underwriting guides, and directives are meant to be followed, and are written in absolute terms because respondent insurers do not want their agents and employees, whose primary function is to generate

¹⁰⁵ Holtom 1496-98, 1505-06, Wirtz 1790-91; CX 56C-D, CX 82E, CX 87H-J, CX 116B-C, CX 156Z-2 to Z-4, CX 182D-E, CX 237Z-8, CX 250F, CX 253Z-10, CX 260H-"T", CX 262C-D, CX 292G-H, CX 294C-D, CX 310D-F, CX 314B; RX 102Z-95 to Z-98, RX 417Z-32, RX 442; see also Findings 98, 114.

¹⁰⁶ CX 30Z-67, CX 91Z-85, CX 160H, CX 166Y, CX 172F, CX 175C, CX 237Z-8, CX 294C-D; RX 482B.

¹⁰⁷ CX 160H, CX 161Z-342, Z-358, Z-382, CX 184A-G, CX 192, CX 214, CX 215, CX 216, CX 219, CX 220, CX 237Z-8, CX 240, CX 241, CX 253Z-10; RX 444Q.

¹⁰⁸ See, e.g., Waiwood 1072-73, Armstrong 1161-62, Ferraro 1200, Haines 3123-25, 3146-49, Bowling 3331-33.

¹⁰⁹ CX 140B, CX 145B-C, CX 160H, CX 228A, CX 232C, CX 237Z-3 to Z-6, CX 309Z; RX 413L, RX 482A. See also Sinkhorn 903-04, Haines 3225-26, Bowling 3300-05 for testimony by respondent officials that agents are audited to determine whether they have complied with respondents' manuals and underwriting guidelines, and that the terms of the agent-insurer contracts must be observed.

¹¹⁰ Haines 3118-20, 3126. See also Haines 3124, 3139-40 for testimony that until guides are changed they should be taken literally and Statton 2872-73 for the statement that manuals are "a broad set of operating guidelines for specific questions that they [branches and regional offices] may have, to save them the time of calling the home office to find out what they should do." The suggestion advanced by respondents that the underwriting guides are only used by "a real green horn" (see, e.g., Haines 3123) is meaningless. While agents or employees may only consult the guides until they become familiar with the contents, it would be absurd to deny that the experienced agent or employee has not incorporated into his total experience the risk limitation admonitions to which he has been exposed from the start of his career.

business, to be making risk decisions that could result in huge claims.¹¹¹

The Title Report Or Binder

75. That the restrictions in respondents' manuals on risk assumption are followed (in the sense that searchers or examiners typically neither eliminate nor make any decision to insure over enforceable defects) is clearly demonstrated by the process for working up the standard form reports or binders provided to respondent insurers by the American Land Title Association (ALTA), and used whenever title insurance is being acquired, irrespective of how the responsibility for search and examination may have been allocated among agents, approved attorneys, or insurance company employees. These standard title reports (also referred to as commitments or binders) purport to show the condition of title as of the date of the search and examination, and are enforceable contracts constituting an agreement by the insurer to issue a policy subject to certain standard requirements and a standard limitation.¹¹² The standard requirements are the [32] payment of the purchase price for the property, recordation of the deed, and payment of the title insurance premium. The heart of the title report, however, is a standard limitation in the form of a general notice that the policy will not insure against loss from any title defects listed on Schedule B of the title report, or any new title defect arising between the date of the report and satisfaction of the standard requirements.¹¹³

76. As a matter of strict rule, respondent insurers require that their agents and employees indicate all enforceable or even doubtful title defects, liens, and encumbrances on Schedule B of the title report.¹¹⁴

¹¹¹ Fromhold 1000-01, Haines 3117, 3123-25.

¹¹² Anito 265-66, Quadraccia 490, Ippel 662-63, Fromhold 1033, Waiwood 1073-79, 1099-1100, 1103; Armstrong 1165-66, Bonita 1276-77, Everbach 1324, Bowling 3268, 3337-38; CX 155D-E, CX 252S, CX 253Z-9 to Z-10, CX 297, CX 302B, CX 320Z-157 to Z-159, CX 342F; RX 3D, RX 417Z-34 to Z-35, RX 487F. Although respondents apparently prefer the designation "commitment" as a way of distinguishing the preliminary report from the abstractors' or attorney's statement of the condition of title, the search and examination is the same for report, binder, or commitment, and there is no evidence that the contents of these pre-policy documents change depending on what they are called. See RX 400Z-84 to Z-95. By the same token, notwithstanding the similarity between a title report and an attorney's opinion, respondents scrupulously avoid the attorney's opinion designation since its use might bring a charge of unauthorized practice of law. Everbach 1328-29, Bowling 3293-94.

¹¹³ CX 252S; RX 420Z-4 to Z-10. Schedule B of the title report contains two sections: section 1 specifies those acts, such as paying off an existing mortgage, that must be performed before the policy issues; section 2 lists the matters which will constitute exceptions on Schedule B of the final policy. CX 222Z-90.

¹¹⁴ Anito 264-66; CX 156Z-45 to Z-46, CX 161Z-34, Z-342, Z-358, Z-382, CX 179L, CX 184A-G, CX 197C, CX 199A, CX 214, CX 215, CX 216, CX 219, CX 220, CX 222Q, Z-64, Z-99, CX 227Z-40, CX 230A, CX 232C, CX 237"O", CX 240, CX 241, CX 254Z-7, CX 320Z-159, CX 342F-M; RX 420.

Thus the title report issued by the attorney as an agent for an insurer is virtually indistinguishable from the attorney's opinion or certification that is issued by the same attorney when he is not acting as an insurance company agent.¹¹⁵

77. Respondents' officers and agents made extravagant claims in their direct testimony about the alleged underwriting discretion that agents and employees, as searchers and examiners, exercise in writing title reports or final policies. The cross-examination [33] of these same witnesses clearly demonstrated, however, that legally enforceable easements, mortgages, restrictive covenants, liens, assessments, and encroachments must be shown on Schedule B of the title report, and that this so-called discretion is narrowly limited to not showing minor, insignificant, and technical title defects ("glitches," "fly specks" or "nits and bits") such as ancient and patently unenforceable mortgages, easements, liens, or covenants, which if not cleaned up would in effect give an inaccurate picture of the true state of title.¹¹⁶

78. That the discretion given to searchers and examiners is severely limited to title objections which are insignificant is demonstrated by the absence of credible evidence that respondent insurers have incurred any significant losses traceable to the exercise of discretion by searchers and examiners in eliminating minor title defects.¹¹⁷

79. Moreover, in sharp contrast to testimony from company officials and agents about searcher and examiner discretion, the insurer-agent agreements and company directives contain explicit requirements that the agent, without any discretion, must list all material title defects as exceptions on Schedule B of the title report.¹¹⁸

80. Similarly, when a title report is to be issued on the basis of an approved attorney's certification, the approved attorney is required to list all valid mortgages, judgments, liens, and other material title defects in his certification.¹¹⁹ But the [34] approved attorney, like the

¹¹⁵ Anito 279-80. As a matter of form, the minor "glitches" that may be dropped entirely from the title report may be included in the attorney's opinion accompanied by an explanatory discussion. Anito 305-06, 315-16.

¹¹⁶ Ippel 639-40, 649-51, 664-67, Malaker 732-34, 748, 792-800, Sinkhorn 867-74, 887, 906-14, Fromhold 965-71, 1005-10, Waiwood 1060-61, 1064-65, 1079-80, 1084-86, 1101-03, Armstrong 1141-42, 1167-68, 1171-72, Ferraro 1228-29, Bonita 1280-86, 1291, 1295-1300, 1302-03, Everbach 1320, 1354-55, 1393-96, Iaines 3120-21, 3130-31, 3222, 3230-31, 3233-37, 3240-43, Bowling 3286-87, 3294-95, 3339-44. See also X 91Z-38, CX 161Z-36, CX 196Z-16, Z-139, CX 237N-"O", CX 342"T"-M; RX 420-RX 420A.

¹¹⁷ See Anito 342, Sinkhorn 906, 911-12, Fromhold 1007, 1011, Armstrong 1174.

¹¹⁸ Sinkhorn 922-23; CX 138B, CX 182G, CX 230A, CX 231A-B, CX 232C, CX 320Z-157.

¹¹⁹ CX 160G-H, CX 196Z-11 to Z-12, CX 237Z-9 to Z-14; RX 410P.

attorney-agent, does not include in his certification clearly technical and immaterial title defects.¹²⁰

81. Independent abstractors, who may perform searches for title insurers or their agents prior to the issuance of a pre-policy report, typically note all pertinent defects, encumbrances, and liens. They usually have no discretion to omit any outstanding interest, no matter how insignificant it may appear.¹²¹

82. These restrictions on the discretion of agents, approved attorneys, and abstractors reflect not only respondents' own basic philosophy of avoiding risk, but also proceed from respondents' legal obligation to inform the prospective owner of all outstanding defects in title,¹²² and the stringent disclosure requirements imposed by the federal guarantors—Government National Mortgage Association (GNMA) and Federal National Mortgage Association (FNMA)—who dominate the secondary mortgage market.¹²³

83. Once enforceable or even doubtful title exceptions appear on Schedule B of the title report of the agent (or in the certifications of the approved attorney or abstractor) they are subject to strict legal review at the regional, divisional, or corporate level of respondents before being considered for either affirmative coverage or elimination from the final policy.¹²⁴ [35]

84. In practice, a decision is rarely made at any level of respondent insurers by which affirmative coverage is extended over a significant disclosed defect, and the common rule in the title insurance industry is that enforceable title defects appearing on Schedule B of the title report will inevitably appear as specific exceptions on Schedule B of the final policy unless the insured takes corrective steps (for example, payment of mortgage money or posting of bonds to satisfy existing tax or judgment liens) to cure them.¹²⁵

The Title Insurance Policy

85. The formal title policy continues the process begun in the

¹²⁰ Sinkhorn 928, Haines 3235-36, Bowling 3361-63, 3379-80; CX 160H, CX 196Z-11 to Z-12.

¹²¹ Cooper 365-67, 370-72, Everbach 1341; CX 253Z-5.

¹²² Ippel 663, Malaker 756-57, Waiwood 1103, Wilkie 2109-10, Bowling 3339-40; CX 183, CX 184A-G, CX 192, CX 198B, CX 221, CX 222Z-64, CX 251A-B, CX 320Z-157 to Z-158.

¹²³ Malaker 808, Bonita 1300-01, Everbach 1398, Haines 3231, Bowling 3342-44; CX 155F, CX 193A-E, CX 253Z-31 to Z-32, CX 303A-B, CX 320Z-159.

¹²⁴ Bowling 3278-79, 3294-95; CX 145B, CX 146B, CX 218, CX 220, CX 221, CX 222Q, Z-25, CX 223B; RX 387, RX 396H, RX 410D, Z, Z-2, RX 413M.

¹²⁵ Anito 265-67, Cooper 372-73, Sinkhorn 887-88, Waiwood 1067, Armstrong 1172, Bonita 1302, Everbach 1396-97, Haines 3234-35; CX 30Z-67, CX 87K, CX 160H, CX 196Z-144, CX 237Z-8, CX 247F, J, CX 252S, CX 260G, CX 292G-H, CX 294C, CX 297, CX 322Z-117; RX 102Z-96, RX 413D, RX 482B, RX 488"T".

preparation of the title report of identifying risks which are not to be insured. Thus the face page of the standard-form owner's policy (ALTA Form B-1970), which is used throughout the title insurance industry,¹²⁶ begins with the declaration that the policy does not cover the exclusions or the exceptions appearing on Schedule B of the policy. The standard terms are as follows:

SUBJECT TO THE EXCLUSIONS FROM COVERAGE, THE EXCEPTIONS CONTAINED IN SCHEDULE B AND THE PROVISIONS OF THE CONDITIONS AND STIPULATIONS HEREOF, [X, Y, Z] TITLE INSURANCE COMPANY . . . herein called the Company, insures, as of Date of Policy shown in Schedule A, against loss or damage, not exceeding the amount of insurance stated in Schedule A, and costs, attorneys' fees and expenses which the Company may become obligated to pay hereunder, sustained or incurred by the insured by reason of:

1. Title to the estate or interest described in Schedule A being vested otherwise than as stated therein;
2. Any defect in or lien or encumbrance on such title;
3. Lack of a right of access to and from the land; or [36]
4. Unmarketability of such title.¹²⁷

86. The standard exclusions, cited on the face page of the policy, are designed to reduce insurer risk by use of the following language:

The following matters are expressly excluded from the coverage of this policy:

1. Any law, ordinance or governmental regulation (including but not limited to building and zoning ordinances) restricting or regulating or prohibiting the occupancy, use or enjoyment of the land, or regulating the character, dimensions or location of any improvement now or hereafter erected on the land, or prohibiting a separation in ownership or a reduction in the dimensions or area of the land, or the effect of any violation of any such law, ordinance or governmental regulation.
2. Rights of eminent domain or governmental rights of police power unless notice of the exercise of such rights appears in the public records at Date of Policy.
3. Defects, liens, encumbrances, adverse claims, or other matters (a) created, suffered, assumed or agreed to by the insured claimant; (b) now known to the Company and now shown by the public records but known to the insured claimant either at Date of Policy or at the date such claimant acquired an estate or interest insured by this policy and not disclosed in writing by the insured claimant to the Company prior to the date such insured claimant became an insured hereunder; (c)

¹²⁶ Cooper 360, Bonita 1302; CX 171; RX 102Z-125, RX 428Z-136, RX 431Y.

¹²⁷ RX 389Z-387. The face amount of the standard owner's policy is the purchase price. Anito 273; CX 247V. The standard mortgagee's policy, which covers the face amount of the loan, has similar coverage except for the addition of provisions insuring the priority of the mortgagee's lien. The mortgagee's policy also has provisions which are similar to the standard exclusion as well as the standard exceptions appearing in Schedule B of the owner's policy. Ippel 626, Haines 3179-80, Bowling 3272; CX 182J-L, Z-90 to Z-95; RX 389Z-408, RX 405Z-172. Owner's and lender's policies may be combined in one simultaneous policy. CX 182L,

resulting in no loss or damage to the insured claimant; (d) attaching or created subsequent to Date of Policy; or (e) resulting in loss or damage which would not have been sustained if the insured claimant had paid value for the estate or interest insured by this policy.¹²⁸ [37]

87. Schedule B of the standard ALTA policy then lists five general exceptions—

- (1) Rights or claims of parties in possession not shown by the public records.
- (2) Encroachments, overlaps, boundary line disputes, and any matters which would be disclosed by an accurate survey and inspection of the premises.
- (3) Easements or claims of easements not shown by the public records.
- (4) Any lien, or right to a lien, for services, labor, or material heretofore or hereafter furnished, imposed by law and now shown by the public records.
- (5) Taxes or special assessments which are not shown as existing liens by the public records.¹²⁹

88. Some of the five “off-record” general exceptions (on either the final policy or the earlier report) may be removed, without creating significant risk to the insurer, by various off-record procedures such as a survey of the property, or by obtaining an indemnity, waiver, release, or proof of payment of taxes.¹³⁰ The removal also requires the purchase of an extended coverage policy.¹³¹ Moreover, if the off-record inquiry discloses any significant title defect, that defect, too, will inevitably appear in the special exception portion of Schedule B.¹³²

89. What are not eliminated from Schedule B of the policy are the special exceptions representing the enforceable easements, restrictive covenants, use restrictions, and liens which first appeared on Schedule B of the title report (see Finding 76) and which were not subsequently removed by the insured. As a matter of [38] strict rule, respondent insurers require that company agents and employees must show all enforceable title defects on Schedule B of the policy as special exceptions to coverage.¹³³

Risk Assumption By Title Insurers

90. As indicated in Finding 84, significant defects to title uncovered

¹²⁸ RX 389Z-392.

¹²⁹ RX 389Z-397.

¹³⁰ Anito 276, Haines 3202-17; CX 182J, L, CX 222Z-47, Z-54 to Z-61, CX 247J, CX 248N-“O”, CX 295E; RX 480-RX 480A.

¹³¹ CX 247J, CX 298B, CX 302B; RX 15A-B, RX 417Z-36 to Z-37.

¹³² CX 242B, CX 248N, CX 295E; RX 428Z-338.

¹³³ Armstrong 1171-72, Bonita 1302; CX 161Z-342, Z-382, CX 184A-G, CX 214, CX 216, CX 219, CX 220, CX 221, CX 240, CX 241, CX 247J, CX 254Z-7, CX 292Q-R.

during the search and examination process are usually either cured by the insured or excepted from coverage since the basic approach of respondent title insurers is to avoid risks and not to insure suspect titles.

91. Thus, like abstractors and independent attorneys, the most significant risk that title insurers face is whatever peril attaches to conducting a competent search and examination of the public records.¹³⁴

92. The risk to insurers from negligence in the title search and examination process is reduced, however, by the contractual relationship between insurers and abstractors, independent attorneys, approved attorneys, and agents which expressly provides for negligence liability in conducting the search and examination.¹³⁵ In addition, agents are commonly required to carry errors and omissions insurance,¹³⁶ and approved attorneys are usually required to have professional liability coverage.¹³⁷ [39]

93. The risk from hidden title defects—forgery (the main danger), false impersonation, or the execution of documents by minors—which cannot be addressed by the search and examination process, represents a relatively minor portion of the already small number of claims paid by title insurers.¹³⁸

94. In a rare number of instances, if an uncovered title defect is not cured, and if the risk is both calculable and low (and assuming further that indemnities or extra premiums have been received from the insured), respondent insurers may make a decision to give affirmative coverage by insuring “over” a known title defect appearing in Schedule B of the title report or the policy.¹³⁹ Considering the severely restrictive conditions under which affirmative coverage is given, it naturally follows that losses due to such coverage are rare.¹⁴⁰

95. For the most part, agents and branch employees of respondent title insurers are prohibited from giving affirmative coverage for a

¹³⁴ Anito 277-78, Quadraccia 505, Sinkhorn 919, Haines 3166-68; CX 156Z-4, CX 172J, CX 181G-H, CX 222Z-11, CX 300A, CX 309Y, RX 397, RX 442A-B.

¹³⁵ CX 138C, CX 140B, CX 145C, CX 146D, CX 160G, CX 228C, CX 230B, CX 231C, CX 261“T”-K; RX 410J. See also CX 186A-B, CX 187A-B, CX 309P, and RX 390A for references to the common law negligence liability of abstractors and agents for errors and omissions in preparing abstracts and reports for title insurers.

¹³⁶ Ferraro 1237; CX 138C, CX 145B, CX 146D, CX 180Z-62, CX 231B, CX 232E.

¹³⁷ CX 230C; RX 410L, RX 413J-K, RX 444N.

¹³⁸ CX 30Z-67 to Z-69, CX 196Z-121 to Z-122; see also Finding 99.

¹³⁹ CX 87K, CX 155C, CX 181H, CX 182M, CX 196Z-139 to Z-140, CX 294D, CX 297, CX 322Z-117; RX 413T, RX 443M, RX 444Y. Even when a title insurer insures “over” a known defect, the common practice is still to list the defect on Schedule B, and then issue affirmative coverage as a way of limiting the insurer’s liability for unmarketability of title. Armstrong 1173, Everbach 1344-45, Bowling 3273, 3299, 3344-45.

¹⁴⁰ Sinkhorn 919, 920. Armstrong 1174.

known risk without the prior approval of respondents' supervisory regional, divisional, or home office underwriting staffs.¹⁴¹ There is no evidence that any title insurer has incurred any loss by reason of [40] an agent's decision to insure over a known title defect without obtaining such prior approval.¹⁴²

96. Significant title defects are insured over (in those rare instances when it is done) on the basis of case-by-case legal analysis by respondents' underwriting staffs located in divisional or regional offices, and in the case of substantial risks by "risk committees" located in the home offices.¹⁴³

97. Another factor taken into account by a title insurer in deciding whether to give affirmative coverage is competitive pressure from other title insurers.¹⁴⁴

98. There is no evidence that in those rare instances when uncovered risks are insured over, this somehow involves a pooling of the risk experience of a group of insurers, or even represents an actuarial assessment of risk by an individual insurer.¹⁴⁵

Claim Payments

99. That all risks assumed by respondent title insurers—whether from a negligent search and examination, or from hidden defects, or from insuring over uncovered defects—are minuscule is shown by the history of claim payments. Only about five to ten percent of a title insurer's gross premium income is used to pay actual losses while over 90 percent is absorbed by operating expenses, mainly the cost of searching and examining title.¹⁴⁶ In contrast, the average loss ratio for homeowner's [41] multiple peril insurance is approximately 65

¹⁴¹ Malaker 777, Fromhold 946-47, 949-50, 1010, Bonita 1302-03, CX 145B, CX 146B, CX 160H, CX 161Z-43, Z-136 to Z-138, Z-153 to Z-154, CX 179L, CX 182M, CX 202L, CX 218, CX 220, CX 222S, Z-11 to Z-12, Z-18, Z-25, Z-65, Z-217 to Z-218, CX 223B, CX 230A, CX 237Z-8 to Z-9, CX 322Z-117, CX 342N-"O", Q; RX 387, RX 410Z to Z-4, RX 413M, T, RX 444Y. The exceptions to this general rule relate to a limited set of circumstances tightly controlled by the insurance companies such as matters with an established expiration date, claims that can be satisfied by the payment of a sum of money, legally unenforceable restrictive covenants, and minor discrepancies in set-back lines. CX 161Z-137 to Z-138, CX 222Z-65, Z-214 to Z-219, CX 237Z-8 to Z-9.

¹⁴² See Fromhold 1011.

¹⁴³ Bowling 3266-67, 3278-79, 3281, 3295-96 CX 160H, CX 182M, CX 218, CX 237Z-8 to Z-9, CX 322Z-117; RX 464E-F, RX 482B-C.

¹⁴⁴ Waiwood 1058, 1080, 1086, 1125, Armstrong 1159-60, Bonita 1294-95, Bowling 3277-79; CX 189Z-17, CX 237Z-6 to Z-7; RX 482B-C, RX 483C, RX 484-484B.

¹⁴⁵ See Holtom 1505-06 and Finding 114.

¹⁴⁶ CX 30Z-67 to Z-68, CX 91Z-84 to Z-85, CX 116D, CX 156Z-3 to Z-4, CX 166Y-X, CX 262R; RX 92Y, RX 102Z-95 to Z-98, RX 364C. See also Anito 277-78, Armstrong 1181, Bethel 1952-53.

percent, and the ratio for other lines of casualty insurance is still higher.¹⁴⁷

100. The one-time premium, which is based on the purchase price of the property or the amount of the mortgage, further distinguishes title from true risk insurance.¹⁴⁸ Thus in contrast to title insurance, casualty insurance involves variable annual premiums that assumes a yearly review followed by a decision as to whether or not coverage is to be renewed or amended depending on risk assessment.¹⁴⁹

101. The difference between title insurance and casualty insurance is also shown by the restrictions in most states preventing title insurers from engaging in any form of casualty insurance for the very reason that these states did not want title insurers to assume risks.¹⁵⁰

G. TITLE INSURANCE RATES

102. Respondents and state insurance departments recognize that there is a sharp distinction between the two things that title insurance companies do—that is, first, provide a service by informing buyers and lenders of the existence of title defects, and second, indemnify buyers and lenders for the small volume of claims that are paid either because of insuring over risks, or hidden risks, or errors in the search.¹⁵¹

103. In the context of rate making, this two-faceted nature of their operations is reflected in the fact that respondents' rate manuals often separate out a small charge for indemnification (what is euphemistically called the "risk" rate for whatever risks are [42] assumed) from a large charge for conducting a search and examination.¹⁵² The "risk" rate is not challenged in this proceeding (except for Ohio, see Findings 158-61), which essentially involves those few states which have required title insurers to file risk as well as search and examination rates, and have allowed both rates to be set by rating bureaus.

104. Prior to October 1983, Connecticut had both an "Approved Attorney Plan" as well as the much larger "All-Inclusive Rate Plan" that included fees for search and examination performed by agents or

¹⁴⁷ Bethel 1994-95; CX 91Z-84, CX 116D.

¹⁴⁸ CX 156Z-3, CX 260H. The one-time premium is the only charge for title insurance so long as the named insured retains an interest in the property. CX 182E.

¹⁴⁹ CX 253Z-10, CX 260H.

¹⁵⁰ CX 260D; RX 102Z-99.

¹⁵¹ Wirtz 1808-09, Haines 3224-25, Fraundorf 3442-43; JXA, p. 89; CX 56B-D, CX 91Z-35, Z-38 to Z-39, CX 130G, CX 131B, CX 133F, CX 156Z-3 to Z-4, CX 208A-C, CX 261" T"-K, CX 293D; RX 167C-D.

¹⁵² Everbach 1377; CX 110B, E, CX 130A to Z-2, CX 132F, CX 155C, CX 222Z-75, CX 237Y to Z-1, CX 273C, CX 311G; RX 3E.

employees.¹⁵³ The Approved Attorney Rate (in the special jargon of the title insurance industry) only covered the risk portion of the premium, the assumption being that approved attorneys would charge an additional and unregulated fee for search and examination.¹⁵⁴ Since October 1983, however, Connecticut has only had a risk rate. The change was intended to reflect the prevalence of the approved attorney system in Connecticut and the redundancy of an all-inclusive rate.¹⁵⁵

105. Pennsylvania, too, has an "approved attorney" rate representing the risk portion only of the total premium (the assumption again being that the approved attorney will bill the consumer separately for an unregulated search and examination fee) as well as an inclusive rate, embracing risk as well as charges for search and examination. The inclusive rate applies when the services are performed by insurance company employees or agents.¹⁵⁶ [43]

106. Until September 1983, New Jersey had separate rate schedules for risk and search and examination.¹⁵⁷ The risk rate, as in Connecticut and Pennsylvania, was designated as the "Approved Attorney Rates" and covered "title insurance underwriting only."¹⁵⁸ Since September, 1983, New Jersey has only published an inclusive rate that simply combines the risk rate with the search and examination charge.¹⁵⁹

107. Montana has an inclusive rate, combining a discrete small charge for risk (designated as the "title insurance premium" and constituting 20% of the rate) and a much larger charge (representing 80% of the total filed rate) for search and examination.¹⁶⁰

108. Idaho has an inclusive rate which combines a risk charge and a fee for performing the search and examination service. The rates are described as "the total title insurance fees charged the applicant including both the risk portion and the service or work portion...."¹⁶¹

109. Arizona has an inclusive rate. It combines the "portion of the

¹⁵³ CX 25B, CX 29B-C, CX 30Z-84 to Z-86, CX 35A-D; RX 101A, RX 102"O"-P.

¹⁵⁴ DiSanto 2753-55. While putatively unregulated, in practice approved attorneys' charges for search and examination reflect the difference between the inclusive rate and the Approved Attorney Rate. DiSanto 2754.

¹⁵⁵ DiSanto 2749-50; CX 32A-X; RX 103A-B.

¹⁵⁶ CX 130A-CX 136D, CX 145E; RX 35J.

¹⁵⁷ CX 276A-CX 283Z-15; RX 3 to RX 3Z-54.

¹⁵⁸ RX 3E, "T".

¹⁵⁹ CX 284A-CX 285W; RX 30-RX 30C.

¹⁶⁰ CX 41K.

¹⁶¹ CX 56Q.

fee...for the assumption by the title insurer of risk" as well as search and examination fees.¹⁶²

110. Ohio has a "risk" rate, which applies only to risk assumption or underwriting expense, and does "not include costs involved in the production of title evidence."¹⁶³

111. Prior to 1984, Wisconsin had a so-called "original" rate, which was simply the addition of two discrete components—a small "risk fee" and a much larger search [44] and examination charge.¹⁶⁴ While the "original" rate has been published since 1984 without the two components, it clearly represents the simple addition of a risk fee and a search and examination charge.¹⁶⁵

Title Insurance Rating Bureaus

112. Title insurance rating bureaus are private organizations organized by respondents and other title insurers doing business in a particular state for the purpose of establishing uniform rates for their members.¹⁶⁶ Uniform rates are established by rating bureaus notwithstanding differences in efficiencies among the members, especially differences in the cost of conducting search and examination.¹⁶⁷

113. Where a title insurance rating bureau establishes either an inclusive rate or a separate rate schedule for search and examination, the rate making function of the bureau is usually supported by profitability studies furnished by retained experts. These studies dwell mainly on the cost of carrying out the search and examination, including the fixed costs of title plants, which must be maintained irrespective of fluctuations in the real estate market.¹⁶⁸

114. There is no evidence that title insurance rates are set collectively through rating bureaus as a way of obtaining intra-industry cooperation in the pooling of risk information. As a matter of fact, there is no evidence that any title insurer, whether [45] operating through a rating bureau or otherwise, sets rates by referring to

¹⁶² JXA, p. 89; CX 9A to Z-52.

¹⁶³ RX 290. See also RX 289 for statement by the Ohio Department of Insurance that Ohio rates do not include a "work charge."

¹⁶⁴ CX 114K, CX 124J.

¹⁶⁵ Wirtz 1794, 1808-09; CX 127J.

¹⁶⁶ DiSanto 2727; CX 171, p. 58, CX 222Z-76.

¹⁶⁷ RX 325.

¹⁶⁸ Plotkin 2457-66; CX 30A to 30Z-98, CX 56A to 56Z-15, CX 208A-C; RX 39 to 39Z-16, RX 91 to 91Z-80, RX 102 to RX 102Z-126, RX 167-RX 167X, RX 364 to RX 364Z-7. Fluctuations in the real estate market are responsible for the cyclical nature of title insurer earnings. Bethel 1969-70; CX 91Z-92 to Z-93; RX 3U-V, RX 102J-K.

actuarially determined loss experience.¹⁶⁹ As the New Jersey Title Insurance Rating Bureau put it:

...it is not possible to set up an actuarial standard for risk assumption based on loss experience. Risks in the title insurance industry are of too low an incidence and too random a character to justify this type of rate determination.¹⁷⁰

115. There is also no evidence that title insurance rating bureaus are necessary in order for respondents to operate as profitable and reliable insurers.¹⁷¹ Nor is there any evidence that rating bureaus are necessary in order for the states to regulate title insurers effectively.¹⁷²

*H. STATE AUTHORIZATION AND ACTIVE SUPERVISION OF TITLE
INSURANCE RATING BUREAUS*

Authorization

116. Complaint counsel concede that the joint rate making activity by rating bureaus in six of the eight states remaining in this proceeding was authorized by state law. The issue of state authorization only arises with respect to rating bureau activity in Pennsylvania and New Jersey, and pertains only to fees charged by attorney-agents (see Findings 117-123).

Pennsylvania

117. Complaint counsel's case with respect to the authorization issue in Pennsylvania rests solely on Section 701(5) of the Pennsylvania Insurance Company Law, which broadly provides that fees for title insurance are subject to regulation but contains the following proviso: **[46]**

"Fee" for title insurance means and includes the premium, the examination and settlement or closing fees, and every other charge, whether denominated premium or otherwise, made by a title insurance company, agent of a title insurance company or an approved attorney of a title insurance company, or any of them, to an insured or to an applicant for insurance, for any policy or contract for the issuance of, or an application for any class or kind of, title insurance; but the term "fee" shall not include any charges paid by an insured or by an applicant for insurance, for any policy or contract, to an attorney at law acting as an independent contractor and retained by

¹⁶⁹ See Wirtz 1790-91; CX 56B-D, CX 82E, CX 91G, CX 156Z-3 to Z-4; RX 39B, RX 102Z-15, RX 167C-D, RX 241-241A.

¹⁷⁰ RX 3Z-4.

¹⁷¹ See Everbach 1410-11, Wilkie 2130-31, Bowling 3357-58.

¹⁷² See Wirtz 1769.

such attorney at law, whether or not he is acting as an agent of or an approved attorney of a title insurance company, or any charges made for special services not constituting title insurance, even though performed in connection with a title insurance policy or contract.¹⁷³

118. There is no dispute that when a Pennsylvania attorney-agent, in connection with the issuance of a title policy, receives a premium from a client, a part of that premium is retained by the attorney-agent as his fee for conducting the search and examination.¹⁷⁴ The record also shows that the total premium including the portion retained by the attorney-agent was fixed by the Pennsylvania Title Insurance Rating Bureau when it set an inclusive rate.¹⁷⁵ Complaint counsel argue, however, that since Section 701 excludes "any charges paid by an insured...to an attorney at law acting as an independent contractor and retained by such attorney at law" the Pennsylvania Rating Bureau had no statutory authority to set an inclusive rate embracing the search and examination charges of an attorney-agent.

119. The Pennsylvania Insurance Department has filed a brief (Amicus Curiae Brief of The Commonwealth of Pennsylvania Insurance Department, March 3, 1986) in which it argues for an interpretation of Section 701 that would make inclusive insurance [47] rates applicable to attorney-agents. In support of this position, Pennsylvania essentially makes three points. First, the interpretation urged by complaint counsel is contrary to the actual practice of the Pennsylvania Insurance Department.¹⁷⁶ Second, complaint counsel's interpretation would leave an unintended void in state regulation based upon the totally irrelevant factor of professional affiliation, and thus is contrary to the Pennsylvania practice of narrowly interpreting legislation that might create such a void.¹⁷⁷ And finally, the intention of the state legislature was not to give a blanket exception but only to exclude from Section 701 those aspects of an attorney-agent's law practice that are unrelated to title insurance such as the issuance of an attorney's opinion (see Finding 46 for evidence that an attorney may function as an independent attorney issuing attorney's opinions as well as an attorney-agent or approved attorney) under the rationale

¹⁷³ JXA, p. 45.

¹⁷⁴ CX 138E, CX 140C, CX 143A-C, CX 145A-E, CX 146A-F.

¹⁷⁵ RX 38F.

¹⁷⁶ Amicus Brief, p. 13.

¹⁷⁷ Amicus Brief, pp. 15-16.

that attorneys, *qua* attorneys, may only be regulated by the judicial branch of the Pennsylvania government.¹⁷⁸

120. Complaint counsel concede that Pennsylvania actively supervises all aspects of title insurance, and the record shows that the state has a long history of aggressive regulation of title insurance.¹⁷⁹ Moreover, no evidence was presented that anyone in Pennsylvania—insurance regulators, consumers, bar, the real estate industry—have endorsed complaint counsel's reading of the statute.

121. Effective February 28, 1986, the Pennsylvania Title Insurance Rating Bureau surrendered its license to the insurance department.¹⁸⁰
[48]

New Jersey

122. Complaint counsel argue that in New Jersey, as in Pennsylvania, there is no statutory authorization for the fixing by the New Jersey Land Title Insurance Rating Bureau of an inclusive rate applicable to searches and examinations carried out by attorney-agents. The relevant statute, *N.J. Stat. Ann.* 17:46B-1(f), which constitutes complaint counsel's entire case on this point, reads in pertinent part—

"Fee" for title insurance means and includes the premium for the assumption of the insurance risk, charges for abstracting or searching, examination, determining insurability, and every other charge, whether denominated premium or otherwise, made by any of them, but the term "fee" shall not include any charges paid to and retained by an attorney at law whether or not he is acting as an agent of a title insurance company or an approved attorney.¹⁸¹

123. As in Pennsylvania, the history of title insurance rate regulation in New Jersey suggests that the state intended that inclusive rates should apply to attorney-agents,¹⁸² and while the New Jersey statute is as ambiguous as Pennsylvania's, complaint counsel offered no testimony, documentary evidence, or legislative history supportive of its interpretation. The only light shed on the statute in

¹⁷⁸ Amicus Brief, pp. 10-13.

¹⁷⁹ See, e.g., RX 35 to RX 35Z, RX 37 to RX 37"O", RX 43.

¹⁸⁰ Amicus Brief, p. 1, n. 1.

¹⁸¹ JXA, p. 3.

¹⁸² During the course of the insurance department's review of rating bureau submissions, no question was ever raised about inclusion of attorney-agents in the inclusive fee schedule. Clayton 1833-35, 1845-47, 1852, 1860. Moreover, despite New Jersey's long history of vigorous opposition to title insurer rate increases and practices from a coalition of real estate attorneys, bankers, builders, and notwithstanding the presence in New Jersey of an insurance ombudsman or public advocate, no one has ever suggested that attorney-agents should be excluded from rate regulation by reason of the interpretation of the statute advanced by complaint counsel. See Clayton 1850-51, 1860-63; CX 276A-R.

this record is that the proviso probably represented a legislative concession to the organized bar's insistence that the state insurance department not infringe on any non-insurance aspect of an attorney's practice.¹⁸³ [49]

Active State Supervision

124. New Jersey and Pennsylvania aside,¹⁸⁴ the state action issue in the six states remaining in this proceeding—Connecticut, Wisconsin, Arizona, Ohio, Idaho, and Montana—turns on whether the joint rate making with respect to title insurance in general, and search and examination in particular, is actively supervised by these states. This determination, which must be made on a state-by-state basis, requires an examination of each state's basic regulatory scheme for title insurance, and how that regulatory scheme responded to readily identifiable areas of concern in the rate making process (see Findings 125-179).¹⁸⁵

Connecticut

125. The Connecticut title insurance rating bureau (the Connecticut Board of Title Underwriters, hereinafter the "Connecticut Rating Bureau") was authorized to [50] establish joint rates for its members after receiving a license from the state's insurance commissioner in 1965.¹⁸⁶

126. The Connecticut Rating Bureau was subject to a wide array of latent powers possessed by the insurance commissioner including the authority to conduct audits, revoke the bureau's license, hold hearings

¹⁸³ See Clayton 1832-33, 1837-42.

¹⁸⁴ On the question of state supervision in New Jersey and Pennsylvania, complaint counsel have entered into the following stipulation:

For purposes of this litigation, complaint counsel will not contest the issue of the level of state supervision under the state action doctrine in New Jersey and Pennsylvania. Complaint counsel has not conducted a detailed factual analysis of the level of state supervision in these states but, solely for purposes of expediting this litigation, agree with respondents to stipulate that there has been active state supervision in New Jersey and Pennsylvania sufficient to satisfy the second prong of the state action doctrine as set forth in *California Retail Liquor Dealers Ass'n v. Midcal Aluminum*, 445 U.S. 97, 102 (1980). RX 43-RX 43 A (Stipulation dated 11-25-85).

¹⁸⁵ The fact that state regulators participate in the proceedings of the National Association of Insurance Commissions (NAIC), including the drafting of a Model Title Insurance Act, tells us nothing about how actively these state regulators actually supervise in their own states. In short, while enactment of the NAIC Model Title Insurance Act may be indicative of a state's determination to supervise certain insurer practices (see note 269, *infra*), there is no convincing evidence that NAIC proceedings are a surrogate for supervision, nor is there any proof that NAIC mandated statistical reports are used or are useful for supervising insurers. See, e.g., Wilkie 2123-24, DiSanto 2795-96, Bowling 3358, Fraundorf 3445.

¹⁸⁶ DiSanto 2727-28; JXA, pp. 142-45; RX 102C.

respecting rates, and rescind previously filed rates.¹⁸⁷ In practice however, the insurance department neither audited the bureau nor did it hold any hearings respecting a bureau rate filing.¹⁸⁸

127. Since 1982 Connecticut has used a “file and use” approach, under which insurers, including insurers operating through rating bureaus, must file rates and wait 30 days before using them. If not disapproved by the insurance commissioner during the 30 days, the rates are “deemed” approved under a “deemer” provision. Prior to 1982, Connecticut allowed rates to be used as soon as they were filed.¹⁸⁹

128. The basic policy of Connecticut is that there should be minimum state involvement in regulation of title insurance rates, the assumption being that rates should be set by the competitive market.¹⁹⁰

129. Notwithstanding its policy of encouraging competition, Connecticut authorized joint title insurance rate making by the Connecticut Rating Bureau on the further assumption that the bureau’s non-competitive rate making process would be [51] scrutinized under the state’s general statutory standard of review, *i.e.*, that the rates should not be excessive, inadequate, or unfairly discriminatory.¹⁹¹

130. The Connecticut Rating Bureau filed only two major rate increases with the Connecticut Insurance Department—in 1966 and on December 3, 1981.¹⁹² With the passage of time, the facts relating to the 1966 filing are elusive,¹⁹³ but it is apparent that the main concern of the insurance department centered on whether the 1966 rate should be for “risk” only or should also include search and examination. On April 3, 1966, the department wrote to the bureau—

We feel that the filing should include insurance rates only and not the fees for the

¹⁸⁷ JXA, pp. 145-58.

¹⁸⁸ Ferraro 2341, DiSanto 2777-78, 2793. Connecticut law does not require that insurance rate filings be subject to public notice, comment, and hearings, or that a written decision, appealable to the state courts, be issued with respect to each rate filing. State insurance regulators are opposed to any such strict procedural requirements on the grounds of cost, and the inevitable delay that such procedures would entail. DiSanto 2769-70, Bell 2841-42.

¹⁸⁹ DiSanto 2813-18; JXA, p. 156.

¹⁹⁰ JXA, pp. 159-60.

¹⁹¹ DiSanto 2818; JXA, pp. 141, 156. See also CX 293C.

¹⁹² Amendments and endorsements, including rate increases and rate reductions, were filed throughout the period 1966 to 1983. CX 26A-CX 28C, CX 33A-CX 34G; RX 148, RX 152-RX 152A, RX 153-RX 153A, RX 154-RX 154B, RX 155F, RX 160-RX 164E. Apparently some were carefully reviewed while others were approved with minimal review; there was no showing, however, in the record that even this minimal review was inadequate considering the subject matter of these minor ancillary filings. See Ferraro 2324-25, DiSanto 2757-69, 2772, 2779-80, 2786-87, Bell 2835-39, 2844-45.

¹⁹³ See DiSanto 2729; CX 25A-H; RX 104-RX 111C.

st of examination of title. We need justification for such rates as well as the breakdown of the premium dollar. How will statistics be kept for this line of insurance? Will reserves be at least equal to those required under the New York law? What states have approved similar filings and what rates became effective?¹⁹⁴

After an exchange of correspondence on the point, the insurance department approved the bureau's rate, effective August 15, 1966,¹⁹⁵ although there is no evidence that the department's request for justification relating to this rate was ever answered satisfactorily.¹⁹⁶ As approved, the 1966 schedule contained both a risk rate (*i.e.*, the so-called [52] "Approved Attorney Plan") and an all-inclusive rate setting the charges for risk as well as search and examination.¹⁹⁷

131. The only other major rate filing of the Connecticut Rating Bureau was made on December 3, 1981. It contained a 20 percent increase in both the approved attorney (risk) rate, as well as the inclusive rate covering risk charges and search and examination fees.¹⁹⁸

132. In support of the 1981 rate increase, the Connecticut Rating Bureau submitted a profitability analysis by Arthur D. Little showing that on the basis of statistical reports received from the members the proposed increase would produce a projected 2.78 percent return on capital.¹⁹⁹ While Dr. Plotkin of Arthur D. Little defended the use of profitability data in connection with the rate submissions of the Connecticut Rating Bureau and other bureaus, he acknowledged that these reports were not intended for the purpose of ascertaining the reasonableness or propriety of insurer expenses.²⁰⁰ He further conceded that a test of state supervision is whether the state examines the extent to which unreasonable insurer expenses are contributing to the burden borne by the insurance buying public.²⁰¹ In Plotkin's view, one expense in particular—excessive commissions paid to agents (*i.e.*, "agents' retention," see Finding 44)—tends to drive up the cost of

¹⁹⁴ RX 104.

¹⁹⁵ RX 105-RX 111C.

¹⁹⁶ See Ferraro 2334-35; RX 105-RX 111C.

¹⁹⁷ CX 25A-H.

¹⁹⁸ DiSanto 2736, Bell 2826; CX 30A to Z-98. On September 30, 1983, the Connecticut Rating Bureau filed an amended manual eliminating the inclusive rate entirely, and in addition making minor adjustments in rates (see Finding 104 and DiSanto 2748-49, Bell 2834; CX 32A-X).

¹⁹⁹ CX 30A to Z-98; RX 102 to Z-126.

²⁰⁰ Plotkin 2650-51, 2704-09.

²⁰¹ Plotkin 2650-51, 2683-84, 2698-99, 2707-09. See also Ferraro 2355-56.

title insurance while dangerously shrinking insurance company profits.²⁰² [53]

133. In order to show that the December 1981 increase (and its accompanying justification) were carefully reviewed by the Connecticut Insurance Department, respondents called Waldo R. DiSanto, Chief of the department's Property and Casualty Division. DiSanto testified that his discussions with the Connecticut Rating Bureau

...centered around the expense component in the rates, more specifically the, in my terms, the disproportionate allowance for commissions paid in connection with title insurance.²⁰³

DiSanto further testified that in his view the agent's commission component of title insurer expenses was "very high,"²⁰⁴ that it was the main problem area in title insurance,²⁰⁵ and that it was driving the cost of title insurance up.²⁰⁶ But having identified this crucial aspect of rate making, DiSanto immediately conceded that he was powerless to do anything about it. He testified as follows:

Q. Did you address with the people with whom you met at this time possible methods of trying to control what you perceived to be these excessive commissions?

A. Yes, commissions, in my view, commissions in the title insurance system have kind of become a sour point, if I can describe it that way, and it has been kind of a constant item for discussion when I meet with or when I had met with title insurance people, the rating organization member representatives.

And I had discussed alternative ideas to reflect or to limit a more appropriate, in my view more appropriate, commission expense.

Q. Were you ever successful in trying to achieve this goal?

A. I guess not because the commissions are still about where they were. [54]

Q. Is there any reason why you have not been able at this point to address this problem?

A. Yes. The function of the Insurance Department, the Insurance Commissioners Office, in connection with the review of rates is to require that the components in the rate making structure submitted by either an insurance company or by a rating organization on behalf of companies is, in fact, valid and supported and accurate.

However, our statutes do not provide the authority of the Insurance Commissioner to establish the amount or a minimum or maximum expense. It is only that if in the filing the companies or bureaus say the commission or company expenses or taxes are percent A, B and C, that they must specifically support that and they must be

²⁰² Plotkin 2684, 2706-09.

²⁰³ DiSanto 2737. See also DiSanto 2756; RX 114-114A.

²⁰⁴ DiSanto 2738.

²⁰⁵ DiSanto 2797.

²⁰⁶ DiSanto 2738.

accurate, but the Commission does not have the authority to say it must be limited to a certain amount.

Now, in the commission area the discussions and the alternative suggestions, in my view, would have required statutory changes, which is not within the function of the Insurance Department or my division. We can suggest, well, that is all we could do.

So that was one of the alternatives of me doing it from that standpoint.

In balance, the commissions in those days are pretty much still in effect. So I guess we have not been successful in changing them.

Q. And just to follow up on that, is this a matter that you have made an effort to address in the course of your regulatory scrutiny of the title insurance industry?

A. Yes, sir.²⁰⁷

And at Tr. 2809, DiSanto added—

JUDGE NEEDELMAN: Tell me whether this is a fair conclusion or not. You have recognized the importance in rate making of the commission paid by the insurer to the agent, correct?

THE WITNESS: Yes.

JUDGE NEEDELMAN: But Connecticut in no way regulates the commission arrangement between the insurer and the agent? [55]

THE WITNESS: That is correct. It is my understanding, with the exception of a few states that have different arrangements, that this commission is not dissimilar from that paid in other states.

In fact, I believe in some states it may be higher.²⁰⁸

134. DiSanto approved the December 1981 filing on January 15, 1982.²⁰⁹

135. By the beginning of 1985, all respondents were no longer active in the Connecticut Rating Bureau.²¹⁰

Wisconsin

136. The Wisconsin title insurance rating bureau (The Wisconsin Title Insurance Rate Service Organization, hereinafter "Wisconsin Rating Bureau"), was authorized under the state's insurance law to establish a joint rate schedule for its members after receiving a license from the Commissioner of Insurance in 1969.²¹¹

137. The Wisconsin Rating Bureau was subject to a wide array of latent powers possessed by the insurance commissioner, but there is little evidence that these powers were used to influence bureau rate making. To illustrate, while the insurance commissioner was required

²⁰⁷ DiSanto 2738-41.

²⁰⁸ DiSanto 2809. See also DiSanto 2793, 2802-03; CX 156Z-7.

²⁰⁹ RX 113.

²¹⁰ Ferraro 2301, DiSanto 2727-28.

²¹¹ Donohoe 1614; JXA, pp. 243, 253, 257-59; CX 107; RX 293-RX 295.

to examine the Wisconsin Rating Bureau at regular intervals, no examination was ever made. Similarly, while the Wisconsin insurance statute gives the commissioner the authority to reject rates established by the bureau through a process of hearings, no hearing has ever been held in Wisconsin on any insurance rate filing, and no rate suspension order has ever been issued.²¹² [56]

138. Rate filings by the Wisconsin Rating Bureau were made under a "use and file" system. This system allows rates to become effective on a date determined by the insurers so long as the rates and any supporting data were filed with the insurance commissioner and made public within 30 days after the effective date. In actual practice, however, the members of the Wisconsin Rating Bureau filed their rate manuals in advance of the effective date, and did not implement major new rate changes until after they were formally stamped as approved by the commissioner's office.²¹³

139. The "use and file" approach of Wisconsin reflects a state policy of not interfering with private rate setting on the assumption that market competition would largely determine rates.²¹⁴

140. By authorizing rating bureaus, however, Wisconsin further assumes that since there has been a departure from its basic policy of relying on competition amongst insurers, the rate making process will be closely reviewed.²¹⁵

141. The standard for review of title insurance rates in Wisconsin is that rates should not be excessive, inadequate, or unfairly discriminatory.²¹⁶ [57]

142. The Wisconsin Rating Bureau made major rate filings in 1971, 1981, and 1982.²¹⁷ In response to the 1971 filing, the Office of the

²¹² Donohoe 1652-53, 1666; Wirtz 1779, 1784-85; JXA, pp. 254, 275-76, 279-80, 296-97. Hearings are only required if a rate is disapproved. JXA, p. 254. The burden of proof in such a hearing is on the insurance commissioner, and considering the limited resources of the insurance department, it is doubtful that he could prevail. According to an official of the state insurance department "[t]he statute was set up, the staffers in the office believe, this way to keep the commissioner and the department from interfering with the rate setting mechanism except in very unusual situations." Wirtz 1786. There is no requirement under Wisconsin law that each insurance rate filing be subject to public notice, comment, and hearing, or that a written decision, appealable to the state courts, be issued with respect to each rate filing.

²¹³ Donohoe 1621-22, 1652, Wirtz 1749-50; JXA, p. 251; RX 301.

²¹⁴ Donohoe 1666, Wirtz 1785-86, 1805-06.

²¹⁵ Wirtz 1806-08. See also CX 293C and JXA, p. 243 (i.e., it is Wisconsin policy "to regulate such cooperation in order to prevent practices that tend to bring about monopoly or to lessen or destroy competition").

²¹⁶ JXA, p. 246.

²¹⁷ In addition, throughout the period 1971-1984, amendments, forms, revisions, compilations, and endorsements were filed by the Wisconsin Rating Bureau. CX 111A to CX 114Z-25, CX 120A-CX 121D, CX 125A-CX 126E; RX 312-RX 315, RX 342-RX 344S, RX 356-RX 356A, RX 359-RX 359B, RX 363-RX 363C, RX 372, RX 373-RX 373D, RX 380-RX 380C, RX 384. The rate adjustments accompanying these filings were neither supported by justifications nor for the most part were they closely reviewed; in fact, the insurance

Commissioner raised some questions about the bureau's reasons for limiting search and examination charges to the southeastern counties of the state only. The issue was eventually resolved by the publication of state-wide search and examination charges. The 1971 rates, which represented historical rates charged before the formation of the bureau, were approved although supporting justification was not provided until 1978.²¹⁸

143. Between the 1971 and the 1981 filing (and continuing to 1984), the Wisconsin Rating Bureau retained Arthur D. Little to draw up a statistical reporting system and income and expense plans to be used in justification of rates. The use of these plans is contemplated by the Wisconsin insurance statute which requires the Commissioner to promulgate reasonable rules for reporting loss and expense experience and authorizes the use of a rating bureau to assist the Commissioner in compiling these data.²¹⁹ The [58] Arthur D. Little materials, however, were never intended to be used for determining the reasonableness or propriety of the insurers' reported expenses.²²⁰

144. The 1981 filing represented a substantial increase (11 percent) in title insurance rates including the rate for search and examination. While the filing and supporting Arthur D. Little data were checked for accuracy before the rate was allowed to go into effect (*i.e.*, not disapproved), the Office of the Commissioner of Insurance made no inquiry into insurer expenses, notwithstanding recognition by the state office that title rates cannot be effectively regulated without such a scrutiny.²²¹ A key official of the state's Office of the Commissioner of Insurance testified as follows:

Q. Now, the department didn't have any idea what an efficient company's expenses would be for search and examination services?

A. No.

Q. But it is your opinion that you would really have to study the search and

department believed that the rating bureau may have pulled the rates "out of the air." Wirtz 1793. See also Donohoe 1661, Wirtz 1759-62, 1768-69, 1771-76, 1802-03, 1807-08.

²¹⁸ Donohoe 1618-27, 1657-59, Wirtz 1764, 1796, 1810-11; CX 110A-G; RX 348 to 348Z-81. The original geographical limitation reflected the fact that branches of the title insurers were concentrated in the Milwaukee area. In the remainder of the state, approved attorneys (whose search and examination charges were not regulated) were the predominant providers of search and examination services. See CX 262" T".

²¹⁹ Donohoe 1627-33, Grabski 1689-90, Wirtz 1763-65, Plotkin 2574-98, JXA, p. 260; RX 334 to RX 334Z-19, RX 348 to RX 348Z-81, RX 351, RX 353 to RX 353Z-13, RX 355, RX 361 to RX 361Z-12, RX 370 to RX 370Z-17, RX 375 to RX 375U, RX 383 to RX 383Z-21, RX 496 to RX 496Z-23, RX 498 to RX 498Z-32. Arthur D. Little also represented the Wisconsin Rating Bureau in successfully opposing statutory revisions requiring specific justification data for each rate change and setting maximum search and examination fees. Donohoe 1634-40, 1653, Plotkin 2585-87; RX 320-RX 326A.

²²⁰ Plotkin 2650-51, 2704-07. See also RX 336A.

²²¹ Wirtz 1750-57, 1776-83.

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examination expenses of the individual companies in order to effectively regulate the charges for search and examination expenses?

A. Yes.²²²

The same official made the following over-all assessment of title insurance supervision in Wisconsin—

Q. Now, for the most part, the people in the insurance department are not concerned with title insurance, is that right? [59]

A. It was not a major line of insurance that we devoted a lot of staff discussion to.²²³

145. Another rate increase (again including the charge for search and examination) was filed by the Wisconsin Rating Bureau in October 1982. The Office of the Commissioner gave this filing a cursory reading to the point that the supporting materials (statistical data and a pro forma analysis) were not even checked for accuracy before the rate increase was accepted.²²⁴

146. The Wisconsin Rating Bureau was dissolved, effective December 31, 1984.²²⁵

Arizona

147. The Arizona title insurance rating bureau (Title Insurance Rating Bureau of Arizona, hereinafter "Arizona Rating Bureau") was authorized under the state's insurance statute to establish joint rates for its members after being licensed in 1968 by the director of the Department of Insurance.²²⁶

148. The Arizona Rating Bureau was subject to a wide range of latent powers possessed by the state's insurance director including the power to audit the bureau's records and revoke its license, and broad authority to hold public hearings, promulgate rules, and issue orders discontinuing bureau practices found to be inconsistent with the insurance statute.²²⁷ That actual use of these powers, however, is more hypothetical than real as shown by the fact that during the entire period 1968 to 1981 the insurance [60] department conducted no examination of the Arizona Rating Bureau although there is a

²²² Wirtz 1778-79. See also Wirtz 1777-78, 1826. See also Plotkin 2577-78 for evidence that Wisconsin insurance officials have acknowledged that excessive insurer expenses is a major concern.

²²³ Wirtz 1782. See also Wirtz 1790-91.

²²⁴ Wirtz 1775-76, 1816-17, 1823-24, Plotkin 2600-05; CX 123A to CX 124Z-25; RX 374-RX 378.

²²⁵ RX 385.

²²⁶ Wilkie 2107-08; JXA, pp. 87, 91-92, 94, 101-10; CX 2-CX 5"T"; RX 48-RX 50A.

²²⁷ JXA, pp. 93-110.

statutory requirement for such an examination at least once every five years.²²⁸

149. The rate filings of the Arizona Rating Bureau were made pursuant to the "file and use" approach. Under this approach, the rating bureau filed rates and its members waited 15 days before using them. If no action was taken by the director during the 15 day waiting period, the rates were deemed approved under a "deemer" provision. Notwithstanding the "file and use" system, in actual practice the Arizona Rating Bureau's rate submissions were not put into effect until actually stamped "approved" by the director.²²⁹

150. The general statutory standard for rate scrutiny in Arizona is that rates should not be inadequate, excessive, or unfairly discriminatory.²³⁰ In reviewing rates, the Department of Insurance is broadly directed to give due consideration to maintaining the stability of rate structures, assuring the financial solvency of title insurers during periods of economic depression, and attracting capital to the title insurance business.²³¹ [61]

151. The Arizona insurance statute also mandates that rate filings should be accompanied by adequate justification, and the Director of the Insurance Department, with the assistance of the rating bureau, is required to promulgate rules relating to statistical plans for use by the rating bureau in reporting the expense experience of its members as justification for rate increases.²³²

152. Against the background of the statutory scheme outlined in Findings 147-151, and putting aside minor rate amendments, adjustments, and endorsements filed throughout the period 1968 to 1980,²³³

²²⁸ Bethel 1992-93, Wilkie 2109; JXA, p. 109; RX 93A. No public hearing was ever held in Arizona on joint rates filed by the Arizona Rating Bureau.

²²⁹ Wilkie 2108, Barberich 2228-30, 2265; JXA, p. 92. If a rate filing was disapproved, a hearing had to be held. JXA, p. 93. A hearing could also be held at the request of a third party who objected to a rate filing. In actual practice, however, no rate filing of the Arizona Rating Bureau was disapproved, and no hearings on title insurance rates filed by the Arizona Rating Bureau was ever held. Wilkie 2128-29. Hearings were held on allegations that insurers or their agents had given illegal inducements to realtors in order to obtain business. RX 45-RX 47H. There is no requirement under Arizona law that insurance rate filings must be subject to public notice, comment, and hearings, or that a written decision, appealable to the state courts, be issued with respect to each rate filing.

²³⁰ JXA, p. 91. In addition, the Arizona code elaborates on this broad statutory standard by providing that due consideration should be given to rate stability, encouraging growth in assets of insurers during periods of high business activity, providing for financial insolvency in periods of depression, and the desirability of paying dividends to induce capital investment. JXA, p. 91.

²³¹ JXA, p. 91.

²³² JXA, pp. 92-94.

²³³ CX 10A-CX 18"O". There is nothing in the record indicating that justifications were submitted with these ancillary filings, and the record is inconclusive as to the kind of review, if any, to which they were subject. See Wilkie 2118-20; Barberich 2230-31, 2264-66. A 1968 rate filing by the Arizona Rating Bureau, which remained the basic title insurance rates throughout the period 1968 to 1983, apparently represented the rates of the Arizona Rating Bureau members before the bureau was formed, but these rates had not been filed with

the Arizona Rating Bureau seemed to spend most of its time between 1977 and 1983 responding to a change in the insurance law that added settlement or escrow rates to the title insurance schedule.²³⁴ During this period, several rate consultants, including Arthur D. Little, put together financial reporting and statistical plans mainly intended to show that the bureau's collectively established escrow rates did not produce excess profits.²³⁵ These efforts culminated in a September 18, 1980 submission from Arthur D. Little containing a detailed analysis of the economic performance of the title insurance industry from 1972 to 1979, and designed to [62] show that title insurance and escrow rates were not excessive.²³⁶ Following this submission, the Department of Insurance announced on November 3, 1980, that an investigation of the Arizona Rating Bureau would be conducted along the following lines:

- 1) An examination of the rate-making procedures and methodology used by the [Arizona Rating Bureau] with respect to the development of title insurance and escrow rates for use in Arizona;
- 2) a determination as to whether the title insurance and escrow rates as filed by [Arizona Rating Bureau] are reasonable and not excessive, inadequate or unfairly discriminatory;
- 3) an analysis of the methodology used for measuring the profitability of title insurers and their agencies, including an analysis of the Arthur D. Little statistical plan which has been filed on behalf of [Arizona Rating Bureau];
- 4) an evaluation of the extent to which there is competition among title insurers doing business in Arizona; and
- 5) the identification of areas which the rate-making methodology, including any statistical plan, together with the level of competitive activity among insurers might be improved.²³⁷

The Arizona Rating Bureau was also informed that-

...the Department has not, as yet, approved the statistical plan prepared and filed on behalf of [Arizona Rating Bureau] by Arthur D. Little. Hopefully, this examination

the Department of Insurance prior to 1968. Bethel 1968, 1971, Wilkie 2074-77, 2107, 2112-13, Barberich 2289; CX 8A to Z-12; RX 60A. While the 1968 rate filing brought an inquiry from the Department of Insurance as to how the "risk" component of the filed inclusive rate was derived (Wilkie 2080, 2087-88; RX 69A), there is no convincing evidence that the rate was either justified by the bureau or reviewed by the state. See Wilkie 2113-14, Barberich 2263-64, 2289; RX 60A.

²³⁴ Wilkie 2091-96, 2121-23, Barberich 2243-44; RX 63-RX 63Z, RX 83-RX 83G.

²³⁵ Wilkie 2092-99, 2121-26, Plotkin 2607-16; CX 9A to Z-52; RX 63-RX 63Z, RX 67-RX 67E, RX 91 to RX 92Z-16, RX 493 to RX 493Z-17.

²³⁶ Plotkin 2617; RX 92 to Z-16.

²³⁷ RX 93-RX 93A.

will provide the Department with the necessary evaluation of this statistical plan so that the plan can be approved or modified as our needs require.²³⁸ [63]

153. Before the Arizona investigation could be completed,²³⁹ however, a federal civil complaint challenging the propriety of the joint fixing of escrow rates by the Arizona Rating Bureau was filed by the United States, followed shortly by a *parens patriae* federal suit brought by Arizona.²⁴⁰ After the entry of a final judgment in the Department of Justice's case on December 16, 1981, the Arizona Rating Bureau went out of business for all purposes (*i.e.*, the fixing of title, search and examination, and escrow rates), and its corporate charter was revoked on October 1, 1983.²⁴¹

Ohio

154. The Ohio Title Insurance Rating Bureau (hereinafter "Ohio Rating Bureau") was authorized to file a joint rate manual for its members after being licensed by the Ohio Department of Insurance in 1972.²⁴²

155. The practices of the Ohio Rating Bureau, including rate making, were subject to a wide array of latent powers possessed by the insurance superintendent including the right to review rates, conduct audits, hold public hearings, suspend or revoke the bureau's license, promulgate statistical plans, and issue orders directed at practices that were unfair, unreasonable, or inconsistent with the insurance statute.²⁴³ [64]

156. The rate filings of the Ohio Rating Bureau were made pursuant to the "file and use" approach—after a 15 day waiting period, which could be extended for an additional 15 days, the rate became effective unless it was disapproved by the Superintendent of Insurance.²⁴⁴

²³⁸ RX 93A-RX 93B.

²³⁹ The Arizona Insurance Department investigation apparently did not get much beyond retaining an actuarial consulting firm, Tillinghast, Nelson and Warren, to review the Arthur D. Little material. The Tillinghast firm agreed with Arthur D. Little's conclusion that the rates were not excessive. Bethel 1975, Barberich 2251, 2270, 2281, 2289; RX 93-RX 93B, RX 96 to RX 96Z-1.

²⁴⁰ Wilkie 2102-06; RX 97" T", RX 98C.

²⁴¹ Wilkie 2106; RX 99.

²⁴² Smith 2961-62, JXA, pp. 219-20; RX 233.

²⁴³ JXA, pp. 218-25. That at least some of these powers are purely latent is shown by the fact that no audit was ever conducted by the Department of Insurance although the statute requires an audit at least once every five years. Smith 3033. There is no requirement under Ohio law that insurance rate filings must be subject to public notice, comment, and hearings, or that a written decision, appealable to the state courts, be issued with each rate filing.

²⁴⁴ JXA, pp. 218-19; Ratchford 3101-02. Rate filings are only made public after the effective date. Ratchford 3087. While the Ohio statute does not require explicit prior approval of rates (see §3935.04(D), Ohio

157. The general statutory standard for rate review in Ohio is that rates shall not be excessive, inadequate, or unfairly discriminatory. In considering whether this standard has been met, the insurance superintendent is directed to consider “[p]ast and prospective loss experience,” a “reasonable margin for underwriting profit and contingencies,” dividends, past and prospective expenses, and “all other relevant factors.”²⁴⁵

158. Between 1972 and 1983, all rates filed by the Ohio Rating Bureau covered “risk” only. None of these filings purported to contain charges for search and examination services or settlement services.²⁴⁶

[65]

159. The Ohio Department of Insurance considered all filings of the Ohio Rating Bureau as covering risk only, and as specifically not including charges for search and examination and settlement services.²⁴⁷

160. Respondents independently set and published charges for search and examination services and settlement services. These charges were not submitted for review to the Ohio Department of Insurance.²⁴⁸

Revised Code, JXA, p. 218), in practice the state apparently has acted under the assumption that prior approval is required. Compare Ising 3050 with Ising 3061. See also Ratchford 3101-02.

²⁴⁵ JXA, p. 217.

²⁴⁶ Smith 2966, 3036; CX 75F, CX 84F, CX 101F, CX 238G. Major rate filings were made in 1972, 1978 and 1981. Soon after the 1972 filing, the Ohio Rating Bureau retained Dr. Irving Plotkin of Arthur D. Little to draw up statistical and financial plans intended, essentially to show profit calculated on the basis of a return on total capital invested. Plotkin also did pro forma analyses of rate increases filed by the bureau. Plotkin testified that although he was compensated by the Ohio Rating Bureau for the work done on these rate matters, he was actually in an adversary position in dealing with the bureau since for all practical purposes he was taking his direction from a Department of Insurance which was hostile to the bureau. Plotkin 2508-10, 2511-13. Plotkin's perception of an adversary relationship is not shared by his sponsors. A few months prior to the September 17, 1981, Ohio filing, an officer of respondent Lawyers Title expressed the following thoughts about Arthur D. Little's role in Ohio rate making:

While Lawyers Title is certainly not the only company in Ohio, I wonder if we would not find that many other companies would not feel similarly about the suggested rate increases. Before asking Arthur D. Little to massage these suggested revisions, I suggest that we try to determine if the suggestions would be palatable to the majority of [Ohio Rating Bureau] members. CX 335. See also CX 330A in which Dr. Plotkin is described by the Ohio Department of Insurance as an “advocate” of the Wisconsin Rating Bureau.

While the principal rate filings and supporting papers of the Ohio Rating Bureau, including the Arthur D. Little submissions, were reviewed by the insurance department (Smith 2963, 2986-90; CX 93A; RX 235-RX 235B, RX 239-RX 239A, RX 241-RX 241B, RX 249-RX 249B, RX 276, RX 277), the record indicates that these rates were approved notwithstanding reservations within the department about the adequacy of the justification, especially the use of the rate of return on total capital as a basis for rate making. Smith 3015; CX 330A-B, CX 331. A minor endorsement filed in 1979 was rejected because it lacked justification (RX 259-RX 260) but other amendments and endorsements, which were filed during the period 1980 to 1983, apparently were approved with little or no accompanying justification. Smith 3030-31; CX 97A, CX 99A.

²⁴⁷ Ising 3060; RX 289. See also RX 290-RX 290B.

²⁴⁸ Malaker 825-26, Sinkhorn 900, Smith 3036-37.

161. Complaint counsel's entire case on the search and examination issue in Ohio rests on the supposition that because rates were justified on the basis of rate of return on total capital they must of necessity be inflated to include such non-risk elements as the cost of conducting a search and examination and settlement.²⁴⁹ While the record [66] indicates that Ohio risk rates may be higher than risk rates elsewhere,²⁵⁰ there is no evidence to support the complaint allegation that respondents have used the rating bureau to establish uniform charges for search and examination and settlement services.

162. Respondents are no longer members of the Ohio Rating Bureau.²⁵¹

Idaho

163. The establishment in 1974 of the Idaho title insurance rating bureau (Idaho Title Insurance Service Organization, Inc., hereinafter "Idaho Rating Bureau") as a medium for establishing joint rates, was authorized by the Idaho insurance statute which requires that a title insurance rating bureau obtain a license from the Director of the Department of Insurance, and that it have as its members at least six title insurers who together account for 50 percent of the title insurance premiums written in the state. The license was granted after a hearing before the insurance department.²⁵²

164. The Idaho Rating Bureau was subject to inspections by the Department of Insurance, and on three occasions the department made an audit of the financial records of the bureau.²⁵³ Other latent powers of the department included the authority to revoke the bureau's license, to issue orders condemning practices that were inconsistent [67] with the insurance statute, and to hold hearings on

²⁴⁹ See CX 91A to Z-154. Neither side in this litigation pressed the argument that rates in rating bureau states are higher or lower than rates elsewhere, or that states which actively supervise rating bureaus have lower or higher rates than states which have little supervision. As far as this record will allow, comparisons cannot be made because the cost of conducting the search and examination differs from state to state. See Bethel 1914-15.

²⁵⁰ See CX 171. The record also indicates that on some occasions an insurance company agent will not charge a large customer for search and examination. Waiwood 1109.

²⁵¹ Smith 3038.

²⁵² JXA, pp. 184-85; CX 46A-CX 49A.

²⁵³ Mitchell 2907, Fraundorf 3444-45; JXA, pp. 168-70, 175-76, 180, 184-86, 188; RX 194 to RX 195Z-15, RX 201-RX 202, RX 204-RX 204A, RX 206-206N, RX 224-RX 224S. After its 1976 examination, the insurance department required the Idaho Rating Bureau to take steps to resolve an apparent conflict of interest between the official duties of one of the bureau's officers and the officer's outside insurance business. RX 196-RX 200.

rates. Hearings, which are only required when a rate is disapproved, were not held on any of the bureau's rate filings.²⁵⁴

165. The joint rate filings of the Idaho Rating Bureau were made pursuant to Section 41-2706 of the *Idaho Code* which requires a 30 day waiting period and the affirmative prior approval of the Director of the Department of Insurance²⁵⁵ (in contrast to the "file and use" or "use and file" approaches previously noted in Connecticut, Wisconsin, Ohio, Arizona, and Montana).

166. Approval of rates, according to the Idaho insurance statute, is presumably based on a determination by the Director of the Department of Insurance that the proposed rates are not excessive, inadequate, or unfairly discriminatory. The statute further provides that in reviewing title insurance rates the director should take into account the state's policy of maintaining stability in insurance rate structures, the necessity for protecting the financial solvency of title insurers and their agents in periods of economic depression by encouraging growth in periods of business expansion, and the desirability of inducing capital to be invested in the industry by assuring a reasonable margin of underwriting profit.²⁵⁶

167. The Idaho insurance statute further provides that all title insurance rate must be justified but insurers are given wide latitude as to the form of the justification—*i.e.*, experience, judgment, statistical data, the experience of other insurers or rating bureaus, and any other factors deemed relevant.²⁵⁷ [68]

168. Under the statutory scheme outlined in Findings 163-167, the Idaho Rating Bureau filed its first major rate proposal on October 3, 1975. Consideration of this filing was suspended as the Department of Insurance convened a public hearing to consider its Amended Regulation No. 25, which related to the use of inclusive rates and a variety of other matters—minimum rates, reissue rates, cancellation fees, the application of the basic rate schedule to special situations, and the amount of insurance that could be purchased in a particular transaction. Following promulgation of Amended Regulation No. 25, the Idaho Rating Bureau refiled its manual and justification (including agent income tax returns) which the Department held open for public inspection for 30 days. During that time, the rate was referred to the

²⁵⁴ Mitchell 2922, 2939; JXA, pp. 173-74, 180-81. There is no requirement under Idaho law that insurance rate filings must be subject to public notice, comment, and hearings, or that a written decision, appealable to the state courts, be issued with each filing.

²⁵⁵ Fraundorf 3446; JXA, pp. 180-82.

²⁵⁶ JXA, p. 181.

²⁵⁷ JXA, P. 181.

department's outside title insurance consultant. The consultant provided his analysis, and on January 20, 1976, the department approved the filing, effective March 1, 1976.²⁵⁸

169. The Idaho Rating Bureau filed its only other across-the-board rate increase with the Department of Insurance on December 15, 1980. After subpoenaing data from the members relating to insurer expenses, and on the recommendation of a retained consultant, the department approved the manual effective February 16, 1981, contingent upon the receipt of still additional material from two insurers explaining large increases in expenses in 1978.²⁵⁹

170. There is no convincing evidence that the Idaho Insurance Department has failed to consider any insurer expense which might impact on rates, including agent retention expense.²⁶⁰ [69]

171. The Idaho Rating Bureau was dissolved, effective November 29, 1984.²⁶¹

Montana

172. The Montana title insurance rating bureau (The Montana Title Insurance Service Organization, Inc., hereinafter "Montana Rating Bureau") was authorized to establish joint rates for its members after being licensed by the Commissioner of Insurance on July 19, 1982.²⁶²

173. Under Montana insurance law, the activity of a rating bureau, including joint rate making, is subject to the latent power of the insurance commissioner to inspect the bureau and if warranted revoke its license, hold hearings on rating bureau practices, and issue orders requiring compliance with the insurance statute.²⁶³

174. The Montana Rating Bureau filed its jointly fixed rates under a "file and use" system whereby rates for title insurance become effective as soon as they are filed with the Department of Insurance.²⁶⁴

175. The statutory standard for reviewing title insurance rates in

²⁵⁸ Mitchell 2883-91; CX 56A-58S; RX 167-RX 182V.

²⁵⁹ Mitchell 2891-98, RX 183-RX 193. Miscellaneous rate adjustments, forms, and endorsements were filed and approved throughout the period 1974-1984 with apparently little or no review by the insurance department. Mitchell 2925-39, Fraundorf 3434-42; CX 62A-71B; RX 207-RX 223.

²⁶⁰ See Mitchell 2941-51, Fraundorf 3447-48, 3451-53.

²⁶¹ Mitchell 2907-08; RX 203-RX 205.

²⁶² Statton 2855-57; JXA, pp. 196-97, 200-06; CX 36-CX 40G.

²⁶³ JXA, pp. 196-97, 200-02, 210-12. In practice, Montana held no hearings respecting title insurance rates filed by the Montana Rating Bureau. Statton 2869. There is no requirement under Montana law that insurance rate filings must be subject to public notice, comment, and hearings, or that a written decision, appealable to the state courts, be issued with respect to each rate filing.

²⁶⁴ Statton 2864; JXA, p. 200; CX 343B.

Montana is that the rates should not be excessive, inadequate or unfairly discriminatory.²⁶⁵ The [70] Montana insurance statute further provides that title insurance rate filings must contain supporting data, and the insurance department is directed, with the aid of the rating bureau, to promulgate statistical plans that could be used to determine whether rates met the statutory standards.²⁶⁶

176. Under the statutory scheme outlined in Findings 172-175, the Montana Rating Bureau made its only major rate filing, which included charges for search and examination, on February 22, 1983. Citing as justification for an increase, nationwide loss figures, a decline in operating profits, and reduced home sales, the bureau's filing included a commitment to gather statistical data and undertake a profitability study for all underwriters and agents in Montana during the year 1984 in order to provide further support for the rate.²⁶⁷

177. In connection with the February 22, 1983 filing, a representative of the Montana Rating Bureau met with officials of the Montana insurance department, and apparently was told that while the increase would go into effect immediately, additional support would have to be provided in the form of financial data showing the profitability of agents and insurance companies for the past five years. There is no evidence that this material was ever provided.²⁶⁸

178. As far as this record will allow, Montana insurance officials examined agent retention expenses both before and after the creation of the Montana Rating Bureau, and there is no evidence that the state's method of dealing with the problem, [71] *i.e.*, by giving the insurance commissioner specific authority to disapprove excessive fees, has been ineffectual.²⁶⁹

²⁶⁵ JXA, pp. 199, 208-09. The broad statutory language is further refined by definitions of excessive ("unreasonably high for the insurance provided under circumstances where a reasonable degree of competition does not exist in the area with respect to the classification to which such rate is applicable"), and inadequate ("unreasonably low for the insurance provided such that the continued use of such rate either endangers the solvency of the insurer using the same or...the use of such rate by the insurer using same has, or if continued will have, the effect of destroying competition or creating a monopoly"). JXA, p. 199.

²⁶⁶ JXA, pp. 200, 208-09.

²⁶⁷ Statton 2857-60; CX 41A-W. An October 14, 1984 filing of the Montana Rating Bureau was basically a clarification of the 1983 filing plus an increase in the charges for special endorsements. Statton 2860-63; CX 43A-CX 44E. By the time this filing went into effect on January 2, 1985, respondents had largely withdrawn from the rating bureau. Statton 2856-57, 2862-63; CX 45; RX 225-RX 226, RX 228-RX 230.

²⁶⁸ Statton 2862, 2865-68; CX 41A-W, CX 343A-D; RX 227.

²⁶⁹ Plotkin 2691, 2714-17. Section 33-25-302 of the Montana Title Insurance Act of 1985 provides as follows:

33-25-302. Disapproval of agency contracts. (1) The commissioner may disapprove a title agency contract between a title agent and title insurer, upon appropriate notice to the parties to the contract, if he finds that the contract, together with all amendments and related documents:

(footnote cont'd)

179. Between July 1, 1983, and January 22, 1985, respondents resigned from the Montana Rating Bureau.²⁷⁰

I. SETTLEMENT OR ESCROW SERVICES

180. Settlement services, sometimes referred to as closing or escrow services, embrace the ministerial functions of carrying out the parties' instructions respecting the execution, delivery, and recording of the deed and mortgage and payment of purchase money. The settlement clerk (also known as an "escrow officer" or simply a "closer") [72] may also be called on to pay taxes and fees and he may assist in the calculation or adjustment of prorated items such as utility charges.²⁷¹

181. While the settlement date usually coincides with the date of issuance of the final title policy (the insurer having directed a "bring down" or "mini" record search and examination between the date of the binder and the date of the settlement in order to be certain that no new title defects have surfaced), there is no evidence that this minor extension of the search and examination process somehow transforms the ministerial functions of settlement or escrow into the business of insurance.²⁷²

182. Respondents also claim that the settlement process functions to disclose title defects that do not appear on the public records. For example, the closing officer in reviewing the papers may uncover additional encumbrances on the property, or the closing officer also may require identification of the parties, a procedure which could disclose an attempted forgery. In addition, the closing officer reviews affidavits or other documents upon which the insurer will rely to remove what otherwise would be listed as "exceptions" on Schedule B

(a) does not provide for adequate monitoring of the agent's financial transactions; or

(b) provides for inadequate, unreasonable, or excessive amounts to be paid to or retained by the title agent. Factors the commissioner may consider in this determination include but are not limited to the agent's duties under the contract and the general level of amounts paid to or retained by other title agents in the state performing or assuming comparable duties.

(2) No person may act as a title agent under an agency contract that has been disapproved by the commissioner.

Section 33-25-302 is patterned after the NAIC Model Title Insurance Act. See RX 502Z-114.

²⁷⁰ RX 225-RX 230.

²⁷¹ Fromhold 956-58, Waiwood 1047, Armstrong 1162-63; CX 155D, CX 196Z-60 to Z-65, CX 238F-H, CX 244Z-52 to Z-62, CX 305; RX 409L, T, RX 421E, RX 427Z-135, RX 431Z-116 to Z-118. Depending on local customs, settlement may be done by mail ("escrow closing") or by the parties meeting and exchanging documents ("table closing"). Waiwood 1096, Everbach 1357-59.

²⁷² Ippel 657, Malaker 735, Armstrong 1155-56, 1180, Ferraro 1204, Bonita 1278-79, 1284, Everbach 1330-31; CX 196Z-65, CX 222Z-121; RX 389Z-221.

of the title insurance policy.²⁷³ There is no evidence, however, that these functions need be carried out by title insurers. As far as this record will allow, all aspects of settlement or escrow are adequately performed by real estate brokers, attorneys, banks, independent escrow companies, and title insurers, all of whom [73] aggressively compete for settlement business on the grounds that each is more expert than the others in performing the clerical duties constituting settlement or escrow.²⁷⁴

183. Settlement is treated by respondent insurers as a discrete service which is ancillary to the title insurance business.²⁷⁵

184. The costs which go into making up settlement fees have nothing to do with risk assumption, risk spreading, or any other insurance consideration. These fees are based on such factors as whether the settlement is held in the closer's office or not, how long the closing takes, travel time, highway tolls, the price of gasoline, and parking fees.²⁷⁶

185. Complaint counsel have pressed the issue of alleged illegal fixing of settlement services through rating bureaus in five states—Arizona, Connecticut, Ohio, New Jersey and Pennsylvania (see Findings 186-189).

186. While the complaint alleges that the charges for settlement services were fixed in Arizona (and there can be no question that beginning in 1977 the Arizona Rating Bureau set escrow rates collectively),²⁷⁷ this issue is not properly before the Federal Trade Commission. Settlement or escrow services in Arizona were investigated by federal authorities, and until December 1991 are the subject of a comprehensive judgment [74] as well as the continuing jurisdiction of the United States District Court For The District of Arizona.²⁷⁸

187. Complaint counsel argue that the "risk rate" which prevails in Ohio not only includes a hidden search and examination charge, but

²⁷³ Ippel 654, Sinkhorn 892-97, Fromhold 956-63, Waiwood 1114-16, Armstrong 1162-64, Everbach 1356-61, Bowling 3322-24, 3349-51; CX 196Z-69 to Z-70, CX 222Z-129 to Z-130, CX 244Z-58; RX 399C-D, RX 442H-"T".

²⁷⁴ See Sinkhorn 899-900, Waiwood 1113-16, Armstrong 1176-77, Everbach 1367, 1372, 1401-02, Bowling 3323, 3350-51, 3370-71; CX 196Z-73, CX 316B.

²⁷⁵ Everbach 1363; CX 87M, CX 238C, K, CX 293D, CX 310" T"; RX 263J, RX 327A.

²⁷⁶ CX 276P; RX 4N, RX 8E, RX 9D, E, RX 10C, RX 11D, RX 13A.

²⁷⁷ Wilkie 2095, 2122; RX 63-RX 63Z, RX 67-RX 67E.

²⁷⁸ Civ. 80-769 (Judgment of U.S. District Court For The District of Arizona, December 16, 1981).

also an amount representing a jointly set settlement fee. There was a failure of proof on this issue.²⁷⁹

188. Complaint counsel argue that both the approved attorney (risk) rates and inclusive rates filed in Connecticut were based in part on escrow expenses. While escrow expenses may have been used to justify rate increases,²⁸⁰ there is no evidence that respondents charged uniform settlement or escrow fees in Connecticut.

189. Settlement fees have been included in jointly established rates in Pennsylvania and New Jersey.²⁸¹ The only issue, however, in these states is the authorization question under *Parker* as it relates to attorney-agents. This is treated in Findings 117-123. [75]

J. MOOTNESS

190. Respondents participated in various state title insurance rating bureaus as follows:

Table 1: Participation By Respondents In
Rating Bureaus

<u>State</u>	<u>Respondents (Including First American) Active In Rating Bureau</u>	<u>Active Period Of Rating Bureaus</u>
Arizona	Ticor, Chicago Title, SAFECO, First American, Lawyers Title, Stewart	1968 to 1981-82
Connecticut	Ticor, Chicago Title, SAFECO, First American, Lawyers Title, Stewart	1965 to 1985
Idaho	Ticor, Chicago Title, SAFECO, First American, Lawyers Title	1974 to 1984
Montana	Ticor, Chicago Title, SAFECO, First American, Lawyers Title	1982 to 1984-85
Ohio	Ticor, Chicago Title, SAFECO, First American, Lawyers Title, Stewart	1972 to 1984

²⁷⁹ See Findings 158-161.

²⁸⁰ CX 30Z-18 to Z-19.

²⁸¹ Settlement fees were taken out of New Jersey rating bureau schedules as of August 2, 1983. CX 284C. For inclusion of settlement fees prior to 1983 see CX 277Z-3 to Z-5. Settlement fees were included on rates filed by the Pennsylvania Rating Bureau as of June 1, 1984. CX 136A-B.

Initial Decision

<u>State</u>	<u>Respondents (Including First American) Active In Rating Bureau</u>	<u>Active Period Of Rating Bureaus</u>
Wisconsin	Ticor, Chicago Title, SAFECO, Lawyers Title, First American, Stewart	1969 to 1984
Pennsylvania	Ticor, Chicago Title, SAFECO, First American, Lawyers Title, Stewart	1946 to 1983
New Jersey	Ticor, Chicago Title, SAFECO, First American, Lawyers Title, Stewart	1975 to 1983

Sources: Arizona (CX 2, CX 6A, CX 7A, CX 8A; RX 99, RX 472), Connecticut (Ferraro 2300-01, DiSanto 2727-28; CX 23, CX 24, CX 31A-B, RX 102C), Idaho (Mitchell 2907-09; CX 46B, CX 49F, CX 50A, CX 51, CX 55; RX 166-166A, RX 203-203H, RX 205) Montana (Statton 2856-57; CX 40A-B, CX 41H; RX 226, RX 228-230), Ohio (Smith 3033; CX 72A-C, CX 74A-R), Wisconsin (CX 103-CX 109; RX 385), Pennsylvania (CX 128A-128B, CX 134A), New Jersey (CX 277D, CX 279E, CX 280E, 281D, CX 282E, CX 283E, CX 285D) [76]

191. While respondents are not presently members of any state rating bureaus which jointly fix the rate for search and examination or settlement services, there was no testimony from respondents' officers, or any other evidence that respondents have abandoned the notion of forming title insurance rating bureaus in the future. [77]

III. DISCUSSION

Respondents, who rank among the nation's largest title insurers, have at one time or another been members of rating bureaus which establish uniform rates for title search and examination and settlement services. Participation by respondents in these rating bureaus raises two main questions: first, whether joint rate making respecting search and examination and settlement services relates to the "business of insurance", and is therefore exempt from the antitrust laws under the McCarran-Ferguson Act ("McCarran Act"); and second, whether this joint rate making, even if it is not exempt under the McCarran Act, is nevertheless beyond the reach of the federal antitrust laws by reason of the "state action" (*Parker*) doctrine since the rating bureau activities of respondents reflect a policy of the

relevant states to suspend competition and are actively supervised by these states.

The "Business of Insurance"

In 1945, Congress passed the McCarran Act for the purpose of removing the "business of insurance" from the reach of the federal antitrust laws to the extent that it is regulated by state law.²⁸² The act was passed in response to *United States v. South-Eastern Underwriters Association*, 322 U.S. 533 (1944) which held that insurance transactions were subject to federal regulation under the Commerce clause, and that the antitrust laws, in particular, were applicable to such transactions. In order to assure that *South-Eastern Underwriters* would not interfere with the traditional role of the states in regulating and taxing insurance, the McCarran Act provided that the business of [78] insurance (but not the business of insurance companies) would receive the following exemption:

Congress 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 the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States.

Sec. 2(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, or which imposes a fee or tax upon such business, 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.

Sec. 3(a) Until 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, and the Act of June 19, 1936, known as the Robinson-Patman Anti-Discrimination Act, shall not apply to the business of insurance or to acts in the conduct thereof.

(b) Nothing contained in this chapter shall render the said Sherman Act inapplicable

²⁸² The complaint makes no charge that the subject rating bureaus were not "regulated" by state law within the meaning of the McCarran Act. See RX 486C. While "regulated" in the McCarran Act sense has been found when the general language of the regulatory statute provided for "enforcement through a scheme of administrative supervision," *FTC v. National Casualty Co.*, 357 U.S. 560, 564 (1958), or when the state specifically authorized the questioned activity, *Ohio AFL-CIO v. Insurance Rating Board*, 451 F.2d 1178 (6th Cir.), *cert. denied*, 409 U.S. 917 (1972), see the discussion herein under *State Action Defense* for the more stringent requirements of the *Parker* doctrine.

to any agreement to boycott, coerce, or intimidate, or act of boycott, coercion, or intimidation.²⁸³

As shown by the language cited above, whether the McCarran Act exemption applies to a particular practice engaged in by insurers (such as the joint setting of the rates for search and examination and settlement services) turns on the meaning of the phrase the "business of insurance," an issue which the Supreme Court has recently addressed in two antitrust cases. [79]

In *Group Life & Health Ins. Co. v. Royal Drug Co.*, 440 U.S. 205 (1979), an insurer (Blue Shield), as part of an effort to reduce the cost of meeting prescription drugs claims, entered into "provider" agreements with most of the pharmacies in San Antonio which stated that the prescriptions of policyholders would be filled at a flat rate of \$2 plus a direct payment by the insurer to the pharmacies for the cost of acquiring the drugs. If an insured elected to use a nonparticipating pharmacy, the pharmacy's regular price had to be paid, but Blue Shield would then make reimbursement for 75 percent of the difference between the nonparticipating pharmacy's full price and the \$2 flat fee. The discrepancy in benefits was obviously designed to discourage policyholders from patronizing nonparticipating pharmacies, with the result that a group of 18 pharmacies, who declined to participate in the \$2 plan, challenged the arrangement under the Sherman Act as both a form of price fixing and as a group boycott of nonparticipating pharmacies.

The Court's analysis of the San Antonio plan begins with the caveat that all antitrust exceptions are to be narrowly read so as to cover no more than the objective targeted by Congress for the exemption. Consistent with this basic tenet of statutory construction, all that is exempt from the antitrust laws under the McCarran Act is the "business of insurance" not the business of insurers. *Id.* at 211. Whether a particular practice meets this restrictive standard is to be resolved by deciding whether the putatively exempt practice relates to the spreading of policyholders' risk or underwriting. The opinion further suggested that the questioned practice must be an integral part of the contractual relationship between the insurer and the insured, and that the practice must not involve entities outside of the insurance industry.

While *Royal Drug* does not indicate that all three elements must be

²⁸³ 15 U.S.C. 1011-1013.

present in each instance, it is plain from the opinion that no practice can be subsumed within the “business of insurance” rubric unless the first test is met—the activity must minimally relate to risk spreading amongst policyholders since, according to the Court, risk [80] spreading or “underwriting” is a “critical determinant in identifying insurance.” *Id.* at 213. Having isolated risk spreading as the quiddity of insurance, the Court then held that the San Antonio prescription plan received no antitrust exemption because it only pertained to how risks are paid (*i.e.*, how claims are satisfied) and not to risk spreading.

On the way to this result, the Court sounded a cautionary note against ready acceptance of insurance company assessment of its own risk spreading function with the admonition that notwithstanding the trappings of insurance, insurance company activity does not constitute the “business of insurance” if upon close analysis it is found that there is no real risk to be spread. This was the clear meaning of the heavy reliance in *Royal Drug* on *SEC v. Variable Annuity Life Ins. Co.*, 359 U.S. 65 (1959) in which self-styled “life insurance” companies offered variable annuity contracts that provided no fixed rate of return but only a pro rata participation in the investment portfolios of the companies. Although the contracts were regulated by state insurance commissions and involved some actuarial prediction of mortality, the Supreme Court there held that since by its terms the contract put all the risk on the annuitants and none on the so-called “insurers,” the contracts were not the “business of insurance” within the meaning of the McCarran Act.

In further support of its emphasis on risk spreading as the linchpin of the McCarran Act exemption, the *Royal Drug* Court stated that the primary purpose of the act was to allow for cooperation in insurance rate making because the actuarial uncertainty involved in spreading insurance risks dictated that a prudent insurer would only set its rates after considering the collective claims history of other similarly situated insurers rather than relying solely on its own experience. The Court found support for this presumed need for cooperation in the risk spreading process from the legislative history of the McCarran Act, particularly in the draft bill and accompanying report of the National Association of Insurance Commissioners (NAIC) released on November 16, 1944, in response to *South-Eastern Underwriters*. The NAIC Report, which [81] the Court describes as “particularly significant, because the Act ultimately passed was based in large part on the NAIC bill.” *Royal Drug*, 440 U.S. at 221, was specifically directed at

the need for shared risk experience during the insurance rate making process. Contrasting the relative certainty of the mortality tables used in life insurance with the data that issuers of other forms of insurance (fires, casualty, surety, and inland marine) had to rely on, the NAIC report argued—

The fire, casualty, surety, and inland marine aspects of the insurance business differ widely from life insurance. In life insurance the gross rates are based upon a number of factors, including mortality tables. Mortality tables are based upon the certainty that everyone must die; the time of death is the only uncertainty. In the other fields of insurance there is no guarantee that the contingency insured against will occur at all. As a result rates in these other fields can be estimated with a lesser degree of certainty. Since rates in these other fields are based upon the law of averages it is manifest that the broader the statistical base the more accurate the average. The experience of individual companies is seldom a reliable guide for rate-making purposes. The structure of the fields of insurance under discussion is based upon these facts of common knowledge. Furthermore, many States have by statutory enactment insisted that companies act in concert for the purpose of collecting statistical data for rate making in these other fields in order to utilize these established principles—principles, we may add, which are wholly inconsistent with the unrestricted competition contemplated by Federal antitrust laws. 90 Cong. Rec. A4405 (1944).

Contrary to the position advanced by respondents, however, neither *Royal Drug* nor the legislative history cited above suggests that all insurance company collective rate making is exempt. This is the clear holding of *United States v. Title Ins. Rating Bureau of Ariz.* (“*TIRBA*”), 700 F.2d 1247 (9th Cir.), *cert. denied*, 104 S. Ct. 3509 (1984), which applied *Royal Drug* to deny an antitrust exemption when insurers used a rating bureau to set common rates for escrow services. In *TIRBA*, the fact that the case involved insurers who were engaged in joint rate making was the starting point, not the end of an inquiry which led ultimately to the conclusion that the escrow or settlement services had nothing to do with risk spreading and therefore did not meet the “business of insurance” requirement. In reaching this result, the Ninth Circuit noted that there was [82] no real insurance function at stake since escrow services, which essentially involves clerical transfers of papers and payment of consideration, are performed by separate departments in insurance companies or by separate but related companies, and are not only offered by insurance companies when no insurance is involved, but are offered by firms other than insurers.

It is also especially significant to this case that the *TIRBA* court