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Recent Case

ANTITRUST LAW - INSURANCE - INSURANCE COMPANY - PHARMACY PROVIDER AGREEMENT DO NOT CONSTITUTE THE "BUSINESS OF INSURANCE" UNDER THE MCCARRAN-FERGUSON ACT AND ARE NOT EXEMPT FROM FEDERAL ANTITRUST SCRUTINY. *Group Life & Health Ins. Co. v. Royal Drug Co.,* 99 S. Ct. 1067 (1979).

In *Group Life & Health Insurance Co. v. Royal Drug Co.,*[1] a divided United States Supreme Court held that pharmacy agreements[2] entered into by Blue Shield[3] and participating Texas pharmacies did not constitute the "business of insurance"[4] within the meaning of the McCarran-Ferguson Act[5] and were, therefore, not exempt from examination under the federal antitrust laws.[6] In reaching its conclusion, the Court narrowed an immunity conferred on the insurance industry by Congress following the landmark decision in *United States v. South-Eastern Underwriters Association*[7] in which the Court held that the comprehensive language of the Sherman Act[8] applied to the "business of insurance" as interstate commerce.[9]

Respondents in *Royal Drug,* eighteen independent pharmacy owners in San Antonio, Texas, brought suit against Blue Shield and three pharmacy operators in federal district court,[10] contending that petitioners' retail price-fixing agreements[11] for drugs and

1. 99 S. Ct. 1067 (1979).

2. *See* note 13 and accompanying text *infra.*

3. Group Life & Health Insurance Company was known as Blue Shield of Texas (Blue Shield). 99 S. Ct. at 1071.

4. *See* note 15 *infra.*

5. 15 U.S.C. §§ 1011-1015 (1976). See notes 15 and 17 *infra,* for the text of relevant sections of the Act.

6. 99 S. Ct. at 1083-84. The Court, however, refused to speculate on the result of such an examination and stressed that it did not hold the activities of petitioners illegal for antitrust purposes, but viewed the issue as "an entirely separate question, not now before use." *Id.* at 1072. It was further noted that "[i]t is axiomatic that conduct which is not exempt from the antitrust laws may nevertheless be perfectly legal," a position reiterated by the Justice Department's amicus brief, which indicated that the pharmacy agreements probably did not offend the antitrust laws. *Id.* at n.5.

7. 322 U.S. 533 (1944).

8. Act of July 2, 1890, ch. 647, 26 Stat. 209 (1890) (current version at 15 U.S.C. §§ 1-7 (1976)).

9. 322 U.S. at 560-62.

10. 415 F. Supp. 343 (W.D. Tex. 1976).

11. An agreement fixing maximum prices is as much of an anathema to the antitrust laws as the fixing of minimum prices. Though it may be argued that a ceiling on prices inures to the public benefit, that same ceiling can quickly become a price floor. *See, e.g.,* United States v. Socony-Vacuum Oil Co., 310 U.S. 150 (1940). "Under the Sherman Act a combination formed for the purpose and with the effect of raising, depressing, fixing, pegging, or stabilizing

pharmaceuticals violated section one of the Sherman Act.[12] Under these agreements participating pharmacies consented to furnish prescription drugs to Blue Shield's policyholders at two dollars for each prescription, and Blue Shield contracted to reimburse the pharmacies for their acquisition costs for the drugs prescribed.[13] Respondents alleged that as a result Blue Shield's policyholders did not patronize respondents' businesses and that petitioners' actions thus constituted an unlawful group boycott under the federal antitrust laws.[14]

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the price . . . in interstate commerce is illegal *per se*." *Id.* at 223. *See also* Kiefer-Stewart Co. v. Joseph E. Seagram & Sons, Inc., 340 U.S. 211 (1951) (resale price maintenance).

The per se categorization evidences a judicial determination that certain practices have such anticompetitive purposes and effects that a full factual analysis is not necessary because it would sacrifice deterrence and increase the cost of judicial administration. Antitrust analysis presently entails increased judicial interest in the facts of each case, even though the ultimate finding may be that a per se offense exists. The list of per se restraints, which preclude detailed factual considerations, is being narrowed. Millstein, *Changing the Per Se Analysis in Counseling and Cases*, Nat'l L.J., Dec. 25, 1978, at 22, col. 1. The current approach being used by the courts has been summarized as follows:

> The question is whether the particular restraint, in some ways similar to but in other ways different from a classic per se offense, should be characterized as a per se violation. In many cases, it is not possible to determine whether a particular business practice should be characterized as a per se violation without conducting something that looks suspiciously like the factual analysis that the per se rules are supposed to avoid.

Id.

12. Section 1 of the Sherman Act declares illegal "every contract, combination . . . or conspiracy in restraint of trade or commerce among the several States." 15 U.S.C. § 1 (1976). Since the language of the Act indicates no limitation on its scope, literally applied, it could invalidate most agreements. It was construed early in its history, however, as prohibiting only unreasonable restraints on trade or commerce. *See* Standard Oil Co. of N.J. v. United States, 221 U.S. 1 (1911). Though the pharmacy agreements in *Royal Drug* were express, inferences of the existence of agreements will also be made from the circumstances. *See, e.g.,* Goldfarb v. Virginia State Bar, 421 U.S. 773 (1975) (numerous attorneys voluntarily following minimum fee schedule adopted by county bar association and suggested by state bar association violated § 1 of the Sherman Act).

13. 99 S. Ct. at 1072. The Court found that the amicus curiae brief of the United States provided a useful illustration of the operation of a pharmacy agreement. The following example was supplied by the Justice Department:

> Suppose the usual and customary retail price for a quantity of Drug X charged both by "participating" Pharmacy A and "non-participating" Pharmacy B is $10.00, and the wholesale price (or acquisition cost) to both is $8.00. If an insured buys Drug X from Pharmacy A, the insured pays $2.00. Pharmacy A receives $2.00 from the insured and $8.00 from Blue Shield, or $10.00 total. If an insured buys Drug X from Pharmacy B, the insured pays Pharmacy B $10.00, and receives $6.00 (75 percent of the difference between the retail price and $2.00) from Blue Shield. While Pharmacy B receives the same as Pharmacy A, the insured must pay $4.00 for the drug and also must take steps to obtain reimbursement.
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> If the pharmacy's acquisition cost for the drug is $5.00 rather than $8.00, the situations of Pharmacy B and the insured are unchanged. But now Pharmacy A will receive only $5.00 from Blue Shield, for a total of $7.00.

Id. at n.3.

14. 99 S. Ct. at 1071.

Group boycotts or concerted refusals to deal are recognized as per se offenses under the antitrust laws. *See, e.g.,* Klor's, Inc. v. Broadway-Hale Stores, Inc., 359 U.S. 207 (1959), and note 12 *supra*. Even though the group boycott is labeled as a per se violation, it is often treated as being subject to the rule of reason. *See* McCormick, *Group Boycotts - Per Se Or Not Per Se, That Is The Question,* 7 SETON HALL L. REV. 703 (1976); Comment, *Boycott: A Specific Definition Limits the Applicability of a Per Se Rule,* 71 NW. U. L. REV. 818 (1977).

Among the well-known rule of reason cases are Board of Trade of the City of Chicago v.

The district court made four findings in deciding to dismiss the case. It found that (1) petitioners' conduct constituted the "business of insurance";[15] (2) the state of Texas regulated the insurance industry within the meaning of the McCarran-Ferguson Act;[16] (3) the boycott exception to the Act was inapplicable;[17] and (4) the federal antitrust laws were likewise inapplicable. Royal Drug appealed from the grant of summary judgment to the United States Court of

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United States, 246 U.S. 231 (1918), and Standard Oil Co. of N.J. v. United States, 221 U.S. 1 (1911). Justice Brandeis' opinion in *Chicago Board of Trade* states the basic formulation of the rule of reason analysis.

> [T]he legality of an agreement or regulation cannot be determined by so simple a test, as whether it restrains competition. Every agreement concerning trade, every regulation of trade, restrains. To bind, to restrain, is of their very essence. The true test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition. To determine that question the court must ordinarily consider the facts peculiar to the business to which the restraint is applied; its condition before and after the restraint was imposed; the nature of the restraint and its effect, actual or probable. The history of the restraint, the evil believed to exist, the reason for adopting the particular remedy, the purpose or end sought to be attained, are all relevant facts. This is not because a good intention will save an otherwise objectionable regulation or the reverse; but because knowledge of intent may help the court to interpret facts and to predict consequences.

246 U.S. at 238.

The Court recently delineated the contours of the rule of reason by stating, "Contrary to its name, the Rule does not open the field of antitrust inquiry to any argument in favor of a challenged restraint that may fall within the realm of reason. Instead, it focuses directly on the challenged restraint's impact on competitive conditions." National Soc'y of Professional Eng'rs v. United States, 435 U.S. 679, 688 (1978) (ethical canon prohibiting competitive bidding by engineering society members held violative of the Sherman Act).

15. Section 2(b) of the McCarran-Ferguson Act provides in relevant part, "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 . . . ." 15 U.S.C. § 1012(b) (1976). An exception to this rule was that after June 30, 1948, the Sherman Act, 15 U.S.C. §§ 1-7 (1976); Clayton Act, 15 U.S.C. §§ 12-27 (1976); and Federal Trade Commission Act, 15 U.S.C. § 41-58 (1976), would apply to the "business of insurance" "to the extent that such business . . . [was] not regulated by State Law." 15 U.S.C. § 1012(b) (1976).

This antitrust exemption has been termed "a prime candidate for interpretive controversy." Rosdeitcher, *Recent Judicial Interpretations of the McCarran Act Antitrust Exemption*, 13 FORUM 873-874 (1978). Its effect was to inform the states that they could preclude application of the antitrust laws to the business of insurance by enacting state regulatory legislation during the moratorium period ending June 30, 1948. *Id.* at 875. Such state regulation, however, could not save boycotts from federal antitrust scrutiny. *See* note 17 *infra.*

In addition, especially considering the trend of recent decisions, questions arise on whether states have sufficiently "regulated" the business of insurance to invoke federal antitrust immunity. Rosdeitcher, *supra*, at 877. A decision that closely scrutinized and delineated the degree of state regulation for federal antitrust purposes was Cantor v. Detroit Edison Co., 428 U.S. 579 (1976). For an extensive analysis of that case, see Comment, *The State Action Exemption in Antitrust: From Parker v. Brown to Cantor v. Detroit Edison Co.*, 1977 DUKE L.J. 871.

16. *See* TEX. INS. CODE ANN. art. 21.21, § 1 (Vernon 1963). The express purpose of the state statute was "to regulate trade practices in the business of insurance in accordance with the intent of Congress as expressed in the [McCarran-Ferguson] Act . . . by defining, or providing for the determination of, all such practices in this state which constitute unfair methods of competition or unfair or deceptive acts or practices and by prohibiting the trade practices so defined or determined." *Id.*

17. The boycott exception defined in § 3(b) of the original McCarran-Ferguson Act has survived intact in the present version: "Nothing contained in this chapter shall render the said Sherman Act inapplicable to any agreement to boycott, coerce, or intimidate, or act of boycott, coercion or intimidation." 15 U.S.C. § 1013(b) (1976).

Appeals for the Fifth Circuit.[18] The court of appeals reversed, finding that Blue Shield's pharmacy agreement plan was not part of the "business of insurance" even though some effect on rates and policyholders might result and that, therefore, the federal antitrust laws were applicable.[19] The Supreme Court subsequently granted certiorari to resolve the intercircuit conflicts on the meaning of "business of insurance" under the McCarran-Ferguson Act.[20]

The McCarran-Ferguson Act marked a congressional attempt to partially restore the tradition begun in *Paul v. Virginia*[21] that "[i]ssuing a policy of insurance is not a transaction of commerce,"[22] but instead a local transaction within the exclusive domain of the states.[23] The *Paul* doctrine was expanded in the *Hooper v. California*[24] decision that the insurance business in general, like an isolated policy sale, was not commerce within the meaning of the commerce clause.[25] Congressional action to restore the traditional approach was necessary because the Court's holding in *United States v. South-Eastern Underwriters Association* "left a major segment of the economy in a disquieting state of uncertainty."[26] The McCarran-Ferguson Act was the direct response to this decision,[27] as Congress endeavored to enact legislation that would preserve state power to tax and regulate the business of insurance.[28]

The Act limited federal regulation and provided for application of the antitrust laws only if insurance company activities were not

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18. 556 F.2d 1375 (5th Cir. 1977). *See* 415 F. Supp. at 347-50.

19. 556 F.2d at 1387.

20. 99 S. Ct. at 1071-72. The Fifth Circuit's position differed from that of the Third, Fourth, and D.C. Circuits. *See, e.g.,* Proctor v. State Farm Mut. Auto. Ins. Co., 561 F.2d 262 (D.C. Cir. 1977); Frankford Hosp. v. Blue Cross, 554 F.2d 1253 (3d Cir. 1977); Anderson v. Medical Serv. of D.C., 551 F.2d 304 (4th Cir. 1977).

21. 75 U.S. (8 Wall.) 168 (1869). For more than seventy-five years following that decision, many practices clearly violative of the Sherman and Clayton Acts developed in the insurance industry. Most notable among these practices was concerted ratemaking, which, absent the commerce exemption, would have been punished. Rosdeitcher, *supra* note 15, at 875.

22. 75 U.S. (8 Wall.) at 183.

23. *Id.*

24. 155 U.S. 648 (1895).

25. *Id.* at 655.

26. Comment, *Policyholder Standing Under the Boycott Exception to the McCarran-Ferguson Act,* 10 U. CONN. L. REV. 419, 423 (1972). *See* E. SAWYER, INSURANCE AS INTERSTATE COMMERCE 3 (1945).

27. See generally FTC v. Travelers Health Ass'n, 362 U.S. 293, 299-302 (1960); 91 CONG. REC. 1085-93, 1478-86 (1945); SAWYER, *supra* note 26, at 50-51.

The South-Eastern Underwriters Association was comprised of nearly two hundred fire insurance companies and twenty-seven individuals that collectivel controlled 90% of the fire insurance business in six states. 322 U.S. at 534-35. Among the alleged Sherman Act violations were fixing of premiums and agents' commissions and threatening policyholders of nonmember companies with withdrawal of all Association services. *Id.* at 535-36.

28. 99 S. Ct. at 1076 n.16. This was the primary concern of Congress; the applicability of the antitrust laws was a secondary consideration. *Id.* at n.18. Even before the *South-Eastern Underwriters* decision, Congress had examined proposals to exempt the insurance industry from the Clayton and Sherman Acts and within three weeks of the decision the House of Representatives approved a blanket exemption bill. *Id.* at 1076-77. *See* 90 CONG. REC. 6565 (1944).

the "business of insurance" and were not regulated by state law.[29] Moreover, the Sherman Act was made applicable without restriction only to acts of boycott, coercion, or intimidation.[30] A three-year moratorium ending July 1, 1948, allowed states a respite during which to adjust to the new Act.[31] The legislative history of the Act shows that Congress clearly neither intended to, nor did, overrule the *South-Eastern Underwriters* decision, but that the "business of insurance" was the underwriting and spreading of risk and that, therefore, only this activity was exempt from federal antitrust scrutiny.[32]

The *Royal Drug* Court began by citing with approval its position in *Barry v. St. Paul Fire & Marine Insurance Co.,*[33] that "the starting point in a case involving construction of the McCarran-Ferguson Act, like the starting point in any case involving the meaning of a statute, is the language of the statute itself."[34] The majority immediately distinguished between application of the antitrust exemption to the "business of insurance" rather than to the "business of insurers."[35] Since the argument that the Act conferred state supremacy in the regulation of all insurance company activities had earlier been rejected,[36] the Court's task in *Royal Drug* was determining whether the pharmacy agreements were "within the ordinary understanding of . . . [the] phrase ['business of insurance'], illumined by any light to be found in the structure of the Act and its legislative history."[37]

In reaching a negative determination, the Court focused on both treatises and case law to confirm that the essential elements of an insurance contract are underwriting and spreading risk, elements that were adjudged absent from the pharmacy agreements. While the *Royal Drug* petitioners argued that the pharmacy agreements did underwrite risks, the Court found their position fallacious in that it confused Blue Shield's obligations to its policyholders under the

29. 15 U.S.C. § 1012(b) (1976). This is § 2(b) of the Act. *See* note 15 *supra.*

30. 15 U.S.C. § 1013(b) (1976). This is § 3(b) of the Act. *See* note 17 *supra.*

31. 91 CONG. REC. 1443 (1945) (remarks of Senators McCarran and Ferguson). *See* McCarran, *Federal Control of Insurance: Moratorium Under Public Law 15 Expired July 1,* 34 A.B.A.J. 539, 539-40 (1948). *See also* 91 CONG. REC. 478 (1945) [exchange between Senators McKellar and Ferguson); 91 CONG. REC. 1444 (1945) (exchange between Senators Pepper and McCarran).

32. 99 S. Ct. at 1078.

33. 438 U.S. 531 (1978). The *Barry* Court agreed with the United States Court of Appeals for the First Circuit that a valid antitrust boycott claim existed when three medical malpractice insurers agreed not to deal with the fourth's policyholder physicians so that the insureds would be compelled to accept a reduced form of coverage.

34. 99 S. Ct. at 1073.

35. *Id.*

36. *See* SEC v. National Sec. Inc., 393 U.S. 453, 459-60 (1969). In that case a merger of two insurance companies was held not to be the "business of insurance." Since the statute was not enacted to regulate the "business of insurance," federal antitrust examination was permissible even though the Arizona Director of Insurance had approved the merger pursuant to statute. *Id.* at 460.

37. 99 S. Ct. at 1073.

drug policies with its agreements with the participating pharmacies. The policies insured the risk that policyholders would not be able to pay for prescription drugs, and Blue Shield promised to pay all costs above the two dollar drug deductible, which made policyholders indifferent about the pharmacy agreements. The majority opinion viewed these agreements as "merely arrangements for the purchase of goods and services by Blue Shield"[38] and found, as had the court of appeals, that "by minimizing costs and maximizing profits . . . [they] inure[d] principally to the benefit of Blue Shield."[39] Though the Court did not dispute that arrangements between the participating pharmacies and Blue Shield might be sound business practice, any arguable benefit to policyholders in the form of premium reductions was not sufficient to distinguish the pharmacy agreements from "countless other business arrangements that may be made by insurance companies to keep their costs low and thereby also keep low the level of premiums charged to their policyholders."[40]

The opinion also discussed the contractual insured-insurer relationship, referred to as "[a]nother commonly understood aspect of the business of insurance."[41] The Court rejected Blue Shield's argument that while the pharmacy agreements were not between Blue Shield and its policyholders, they, nevertheless, fell within the exemption because of their influence on the reliability of the insurance contract. Instead the Court found that this erroneous interpretation would protect almost every decision of an insurance company from federal antitrust scrutiny, "a result . . . plainly contrary to the statutory language, which exempts the 'business of insurance' and not the 'business of insurance companies.' "[42]

The Court's discussion in *Royal Drug* of the McCarran-Ferguson Act emphasized that cooperative ratemaking efforts were intended to be exempt from the antitrust laws "[b]ecause of the widespread view that it is very difficult to underwrite risks in an informed and responsible way without intraindustry cooperation."[43] The final version of the Act was based largely on a bill suggested by the National Association of Insurance Commissioners (NAIC), but

38. *Id.* at 1074.

39. 555 F.2d at 1381.

40. 99 S. Ct. at 1075. The Court indicated that Blue Shield's agreements constituted the "business of insurance" no more than would an insurance company's contract with a large retail drug chain to require policyholders to buy drugs only from that chain or a company's acquisition of a drug store chain in order to lower costs of paying policyholder claims. *Id.*

41. *Id.*

42. *Id.* at 1076. The Court did recognize the correctness of the SEC v. National Sec., Inc., 393 U.S. 453, 460 (1969), holding that peripheral activities of insurance companies exist that are so closely related to the companies' status as reliable insurers that such activities also qualify for the "business of insurance" exemption. The proper focus, nevertheless, continues to be on the insurance company-policyholder relationship. 99 S. Ct. at 1075-76.

43. *Id.* at 1078.

Congress rejected a proposal of seven enumerated exclusions from the Sherman Act.[44] Noting that the remarks of Senators both during the floor debates and otherwise focused on a cooperative ratemaking exemption the Court opined that "[t]here is not the slightest suggestion in the legislative history that Congress in any way contemplated that arrangements such as the Pharmacy Agreements in this case, which involve the mass purchase of goods and services from entities outside the insurance industry, are the 'business of insurance.' "[45]

As further support for its position, the majority noted that when the McCarran-Ferguson Act was passed, corporations organized to provide medical services and hospitalization for their members, such as Blue Shield, were considered neither engaged in the "business of insurance" nor subject to state insurance laws.[46] Moreover, such organizations themselves have historically sought to avoid state regulation and taxation by arguing against being classified as insurance companies.[47] Thus, the Court found it "next to impossible to assume that Congress could have thought that agreements (even by insurance companies) which provide for the purchase of goods and services from third parties at a set price are within the meaning of . . . [the] phrase ['business of insurance']."[48]

Finally the majority reiterated the principle that "exemptions from the antitrust laws are to be narrowly construed,"[49] whether they are implicit or express statutory exemptions.[50] The *Royal Drug*

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44. *Id. See* 90 CONG. REC. A4403-08 (1944). These specific practices all included intra-industry cooperation or concerted activities. "None involved contractual arrangements that insurance companies might make with providers of goods or services to reduce the costs to the companies of meeting their underwriting obligations to their policyholders." 99 S. Ct. at 1078.

45. 99 S. Ct. at 1079-80. The dissent found other reasons for the lack of discussion of provider agreements. *See* notes 54-55 and accompanying text *infra.* The majority, nevertheless, indicated that such agreements were not among the NAIC's suggested exemptions. 99 S. Ct. at 1079 n.30. *See* 90 CONG. REC. A4406 (1944).

46. 99 S. Ct. at 1080. *See, e.g.,* Jordan v. Group Health Ass'n, 107 F.2d 239 (D.C. Cir. 1939); California Physicians' Serv. v. Garrison, 28 Cal. 2d 790, 172 P.2d 4 (1946); Commissioner of Bank Ins. v. Community Health Serv., 129 N.J.L. 427, 30 A.2d 44 (1943).

In *Jordan v. Group Health* the nonprofit corporation that provided medical benefits to members in return for a fixed annual premium contracted with physicians, hospitals, etc. in order to obtain lower prices than if each member contracted separately. The circuit court concluded that Group Health's activities of getting services to its members identified it as a consumer cooperative with functions separate from those of insurance or indemnity companies, the principal, if not exclusive, concern of which was risk. 107 F.2d at 247.

47. 99 S. Ct. at 1082. *See* Weller, *The McCarran-Ferguson Act's Antitrust Exemption for Insurance: Language, History, and Policy,* 1978 DUKE L.J. 587, 624 n.174. One commentator noted that though insurance experts have often expressed amazement at the arguments of the "Blues" (Blue Cross and Blue Shield), many courts have sided with the companies' position. Denenberg, *The Legal Definition of Insurance,* 30 J. INS. 319, 322 (1963).

48. 99 S. Ct. at 1082.

49. *Id.* at 1083. *See, e.g.,* Abbott Labs v. Portland Retail Druggists Ass'n, 425 U.S. 1 (1976) (Nonprofit Institutions Act); Connell Constr. Co. v. Plumbers & Steamfitters Local Union No. 100, 421 U.S. 616 (1975) (National Labor Relations Act); Federal Maritime Comm'n v. Seatrain Lines, Inc., 411 U.S. 726 (1973) (§ 15 of the Shipping Act); United States v. McKesson & Robbins, 351 U.S. 305 (1956) (Miller-Tydings and McGuire Acts).

50. 99 S. Ct. at 1083.

Court held application of the principle "particularly appropriate . . . because the Pharmacy Agreements involve[d] parties wholly outside the insurance industry."[51] The Court also noted "that an exempt entity forfeits antitrust exemption by acting in concert with nonexempt parties."[52] The danger in finding that the pharmacy agreements constituted the "business of insurance" because of their cost-reducing features lay in the potential validation of all cost control agreements insurers might make. The Court, therefore, affirmed the judgment of the court of appeals that Congress did not exempt the "business of insurers" under the McCarran-Ferguson Act, but exempted only the "business of insurance."[53]

Mr. Justice Brennan filed a dissenting opinion, in which he stated that the pharmacy agreements should be considered part of the "business of insurance."[54] As did the majority, he felt it important to examine the background of the McCarran-Ferguson Act, but took issue with the view that the lack of congressional discussion about insurer-third party provider agreements established by negative inference their exclusion from the "business of insurance." The dissent relied instead on the general language of the Act to support a broad exemption and cited language from *SEC v. National Securities, Inc.*[55] that the legislative history of the Act does not elucidate on the meaning of "business of insurance."[56]

The dissent did not dispute the majority's view that continuing state regulation of insurance as it existed prior to *South-Eastern Underwriters* was Congress' motive in enacting the federal insurance law nor did it reject the relevance of considering what the states in 1945 viewed and regulated as insurance. Logically, however, the majority agreed with the Court's statement in *SEC v. Variable Annuity Life Insurance Co.*,[57] that "insurance is an evolving institution . . . the forms [of which] have greatly changed even in a generation."[58] The dissent contended, however, that a determination of the scope of the McCarran-Ferguson Act required not only an analysis of the proximity between challenged transactions and those recog-

51. *Id.*

52. *Id. See, e.g.*, Ramsey v. UMW, 401 U.S. 302 (1971) (union forfeits its antitrust exemption if it agrees with one group of employers to impose a wage scale on other bargaining units); Case-Swayne Co. v. Sunkist Growers, Inc., 389 U.S. 384 (1967) (exempt agricultural cooperative under Capper-Volstead Act loses exemption when it conspires with nonexempt parties).

53. 99 S. Ct. at 1083-84. The Court perceived serious anticompetitive consequences if it exempted the provider agreements and cited recent studies indicating that physicians and other health care providers dominated Blue Shield plan boards of directors, leading to rapid escalation of health care costs. *Id.* at 1083-84 n.40.

54. *Id.* at 1084.

55. 393 U.S. 453 (1969).

56. 99 S. Ct. at 1084. *See* 393 U.S. at 459.

57. 359 U.S. 65 (1959).

58. *Id.* at 71.

nized as elements of insurance but also an examination of the historical setting of the Act. The minority's conclusion was that Blue Shield's pharmacy agreements enjoyed the status of the "business of insurance" under both counts.[59]

The "common ground" of both the majority and minority was agreement that the policy between Blue Shield and its insureds unquestionably constituted the "business of insurance."[60] Even though policies expressly providing drug benefits were unavailable during the 1930's and 1940's, analogous noncash payment policies providing hospital and medical services existed.[61] Moreover, state regulation of service-benefit plans was widely in effect by the time the Act was passed,[62] and the plans themselves were a commonly recognized form of insurance.[63] Congress adopted an enabling act for such a plan in the District of Columbia in 1939[64] and in 1946 referred to Blue Shield type programs as "insurance" in debates on these plans as an alternative to national health insurance.[65] Thus, the dissent urged that "[t]he status of service-benefit policies as 'insurance,' both logically and historically, . . . sufficiently established . . . the first premise in an analysis of the status of the Pharmacy Agreements at issue in this case."[66]

After determining that service-benefit plans were "insurance," the minority opinion addressed the question of "whether at least some contracts with third parties to procure delivery of benefits to Blue Shield's insureds would also constitute the 'business of insurance.' "[67] The majority's absolute refusal to classify the challenged provider agreements as such was viewed as erroneous and unsupported by previous decisions of the Court and the legislative history

59. 99 S. Ct. at 1086-87.

60. *Id.* at 1087. Of no consequence was the difference between Blue Shield's payments to its insureds in goods and services and the first health insurance companies' payments in cash. *Id.*

61. *Id.* The hospital benefit concept dates from 1929; medical services began to be offered in 1939. R. EILERS, REGULATION OF BLUE CROSS AND BLUE SHIELD PLANS 15 (1963). Over twenty million people were enrolled in service-benefit plans, which comprised 61% of the hospitalization insurance market, when the McCarran-Ferguson Act was passed. *A National Health Program, Hearings Before the Senate Committee on Education and Labor,* 79th Cong., 2d Sess. 173 (1946).

62. 99 S. Ct. at 1087. Before 1939, twenty-four states had enabling acts that expressly subjected service-benefit plans to state insurance department regulation. *See* Rorem, *Enabling Legislation for Non-Profit Hospital Service Plans*, 6 LAW & CONTEMP. PROB. 528, 531-32 (1939); Comment, *Group Health Plans: Some Legal and Economic Aspects*, 53 YALE L.J. 162, 174 (1943). By the time the Act was passed, thirty-five states had enabling legislation. F. HEDINGER, THE SOCIAL ROLE OF BLUE CROSS AS A DEVICE FOR FINANCING THE COSTS OF HOSPITAL CARE 51 (1966). The *Royal Drug* dissent listed these states. *See* 99 S. Ct. at 1087 n.6 and 1088 n.7.

63. 99 S. Ct. at 1088.

64. *See* H.R. 6266, 76th Cong., 1st Sess. (1939); H.R. Rep. No. 1247, 76th Cong., 1st Sess. (1939); 84 CONG. REC. 11224 (1939).

65. *A National Health Program, supra* note 61, at 55, 83, 108, 172, 558.

66. 99 S. Ct. at 1089.

67. *Id.*

of the Act. Specifically, the dissent noted that underwriting of risk has not always been deemed an indispensable characteristic of the "business of insurance."[68] The dissent emphasized Congress' knowledge of service-benefit policies as insurance and stressed that common sense mandated a conclusion that Congress viewed contracts necessary to effectuate those policies as within the "business of insurance" category.[69]

After arguing that some provider agreements constituted the "business of insurance," Justice Brennan's final concern was whether the agreements in question met the test. Respondents urged a negative answer in accordance with the court of appeals holding and indicated that though the payment of a set amount (here two dollars) to the druggists might be proper and necessary, the freeze on the markup and limiting of reimbursement to acquisition costs was price-fixing, an anticompetitive practice that was not the "business of insurance."[70] Citing historical precedent,[71] the dissent rejected respondents' contentions and regarded anticompetitiveness as irrelevant because "[a]n antitrust exemption by its very nature must protect some transactions that are anticompetitive; an exemption that is extinguished by a finding that challenged activity violates the antitrust laws is no exemption at all."[72]

Several reasons were found by the dissent to support the inclusion of the challenged provider agreements within the circle of exemptions. First, the contractual arrangement did affect costs and, therefore, both rate-setting and insurer reliability.[73] The unnecessarily high correlation between rates and drug prices in a drug-benefits policy illustrated the more than incidental connection between the contract, policy, and premium. Thus, the minority found that Blue Shield's pharmacy agreements had sufficient nexus to basic insurance elements to be considered the "business of insurance." Second,

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68. *Id. See, e.g.*, FTC v. National Cas. Co., 357 U.S. 560 (1958) (advertising of insurance is within scope of the McCarran-Ferguson Act). In addition, various horizontal arrangements between insurers were non-risk spreading but constituted, nevertheless, the "business of insurance," a concession the majority made despite "failure to fit within . . . [the risk-spreading] formula." 99 S. Ct. at 1089.

69. 99 S. Ct. at 1090-91. The dissent further opined,

> *Some* kind of provider agreement becomes a necessity if a service-benefits insurer is to meet its obligations to the insureds. The policy before us in this case, for example, promises payment of benefits in drugs. Thus, some arrangement must be made to provide those drugs for subscribers. Such an arrangement obtains the very benefits promised in the policy; it does not simply relate to the general operation of the company . . . .

Id.

70. *Id.* at 1091.

71. According to the dissent, early service-benefit plans fixed more of the payment to participating providers then did the *Royal Drug* markup fixing. *Id.* at 1091-92.

72. *Id.* at 1092.

73. *Id. SEC v. National Sec. Inc.* recognized this effect as relevant to the "business of insurance" determination. *See* 393 U.S. at 460.

the agreements exemplified legitimate efforts to reduce the unpredictable aspects of the risk assumed, specifically by advance contracting for a price in order to minimize the "pay off" variable due to market fluctuations.[74] The court of appeals had recognized the risk of bankruptcy for service-benefit plans that paid costs regardless of their amount, but recommended periodic rate structure adjustment to reflect inflation as a solution to the problem.[75]

The dissent recognized the necessity of a case-by-case approach to the "business of insurance" problem, though the minority felt that the concept of provider agreements for benefits promised in a service-benefit policy was necessary to accomplish the duties under such a policy. Nonetheless, the dissenting opinion acknowledged that all provider agreements would not qualify as the "business of insurance" under the McCarran-Ferguson Act proviso.[76] The ultimate recommendation was that reversal and remand were necessary since the court of appeals had not decided whether petitioners' actions were state regulated or if they fell within the boycott exception.[77]

The *Royal Drug* decision is not surprising in view of present interest in increased federal regulation of the insurance industry.[78] Its effect is to erode the almost complete immunity the enterprise has enjoyed from federal antitrust suit. Until recently, for example, the boycott exception, though broadly worded, has been consistently interpreted narrowly to apply only to intra-industry blacklisting.[79] Therefore, consumers have not enjoyed the protection that the McCarran-Ferguson Act could provide and have been forced to rely on ineffective state legislation.[80]

Present indications are that time may be running out for the insurance antitrust shield, for the 96th Congress will undoubtedly consider changes in the Act. *Group Life & Health Insurance Co. v. Royal Drug Co.* thus reinforces a trend toward antitrust scrutiny of the insurance industry, "the last key sector of the national economy generally free of federal regulation."[81]

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74. 99 S. Ct. at 1093.
75. 556 F.2d at 1382.
76. 99 S. Ct. at 1093-94.
77. *Id.* at 1095. *See* note 17 *supra.*
78. *See* note 81 and accompanying text *infra.*
79. Blacklisting refers to the coercive practice by groups of insurance companies against other insurers. Members of the group direct agents not to write policies in the name of companies on the "list" and threaten agents with loss of their agency unless they obey the directive. Comment, *supra* note 26, at 419 n.5 (1978).
80. *Id.* at 419.
81. Hallett, *Is Time Running Out on the Insurance Industry?*, Legal Times of Washington, Mar. 2, 1979, at 14, col. 1. [Casenote by Mary Pauline Finan]