

Antitrust and the Securities Industry Lessons from the Shipping Industry

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NOTES

ANTITRUST AND THE SECURITIES INDUSTRY: LESSONS FROM THE SHIPPING INDUSTRY

Since the landmark case of *Silver v. New York Stock Exchange*¹ in 1963, the securities industry, the SEC, the Justice Department, and the public have speculated on the impact that application of antitrust principles might have on activities of the securities industry. Much has been written on this subject,² but the effect has been noticeably slight on both the SEC and the courts. Yet antitrust issues remain, and the recent case of *Federal Maritime Commission v. Aktiebolaget Svenska Amerika Linien*³ (*Swedish American*) indicates that perhaps the Supreme Court will require the regulatory agencies to consider antitrust principles more fully in their determinations.

I

THE INTERPLAY OF AGENCY CONTROL AND ANTITRUST PREMISES

Both antitrust laws⁴ and regulatory agency statutes⁵ represent a congressional attempt to regulate the economy in the public interest while promoting our basic economic theories. Although these two types of regulation are often rationalized as being complementary,⁶

¹ 373 U.S. 341 (1963).

² *E.g.*, Johnson, *Application of Antitrust Laws to the Securities Industry*, 20 Sw. L.J. 536 (1966); Sterling, *Stockbrokers Going Public: Antitrust Aspects of Exchange Rules*, 13 U.C.L.A.L. REV. 563 (1966); Note, *Antitrust and the Stock Exchange: Minimum Commission or Free Competition?*, 18 STAN. L. REV. 213 (1965); Note, *The Application of Antitrust Laws to the Securities Industry*, 10 WM. & MARY L. REV. 136 (1968).

³ 390 U.S. 238 (1968).

⁴ The basic antitrust legislation is found in three acts: the Sherman Antitrust Act, 15 U.S.C. §§ 1-7 (1964); the Clayton Act, 15 U.S.C. §§ 12-27 (1964); and the Federal Trade Commission Act, 15 U.S.C. §§ 41-58 (1964).

⁵ Some of the more important regulated industries include:

a) Communications: Federal Communications Act of 1934, 47 U.S.C. §§ 151-609 (1964);

b) Foreign shipping: Shipping Act of 1916, 46 U.S.C. §§ 801-42 (1964);

c) Power: Federal Power Act, 16 U.S.C. §§ 791a-828c (1964);

d) Railroads, motor and water carriers: Interstate Commerce Act, 49 U.S.C. §§ 1-1022 (1964);

e) Securities: Securities Exchange Act of 1934, 15 U.S.C. §§ 78a-hh (1964).

⁶ *See, e.g.*, *Northern Natural Gas Co. v. FPC*, 399 F.2d 953, 959 (D.C. Cir. 1968). Judge J. Skelly Wright stated that "the two forms of economic regulation complement each

in reality they quite often meet in the courtroom in what Judge Medina has characterized as a "head-on collision."⁷ This collision occurs when an administrative agency takes anticompetitive action, such as setting uniform rates or permitting a merger, to create improved service in the regulated industry. Many such actions would result in a per se violation of the antitrust laws were it not for the regulatory statutes. Frequently a party injured by this action will seek judicial relief in an antitrust proceeding. The court must then decide which will be the appropriate tribunal for hearing the claims of the aggrieved party: the court, the agency, or both; and if they are to have concurrent jurisdiction, who will hear the claims first?⁸

The opposing positions on this issue are fairly well defined. Two principal arguments support agency control: (1) greater uniformity in the decisions if only one forum, the agency, hears the disputes;⁹ and (2) expertise of the administrators in a narrow and technical area.¹⁰ Contrariwise, supporting resort to judicial application of anti-

other." *Id.* The basis for this statement is that both antitrust laws and agency regulation share the common purposes of: (1) the most efficient allocation of resources possible; and (2) the stimulation of innovation for better service at a lower cost.

⁷ *United States v. Morgan*, 118 F. Supp. 621, 694 (S.D.N.Y. 1953). In this case the Justice Department initiated antitrust proceedings against a number of stockbrokers. One of the court's considerations was whether the dispute should be resolved in the courts under antitrust principles or left to the discretion of the SEC. Judge Medina began his inquiry into this issue in the following manner:

The plain truth of the matter is that the legal questions now under discussion form an area of head-on collision between the SEC on the one hand and the Antitrust Division of the Department of Justice on the other.

Id.

⁸ If judge and administrator have concurrent jurisdiction, the doctrine of primary jurisdiction may be applicable. This doctrine "requires judicial abstention in cases where protection of the integrity of a regulatory scheme dictates preliminary resort to the agency which administers the scheme." *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321, 353 (1963). The usual reasons given to justify prior administrative action are basically the same as those justifying the use of antitrust exemptions: (1) expertise of the administrator and (2) uniformity of result. For a discussion of this closely related doctrine of primary jurisdiction see generally K. DAVIS, ADMINISTRATIVE LAW TEXT §§ 19.01-09 (1959).

⁹ Uniformity was the first argument advanced and was cited in the case generally thought to be the father of the primary jurisdiction doctrine, *Texas & Pac. Ry. v. Abilene Cotton Oil Co.*, 204 U.S. 426 (1907):

[I]f the power existed in both courts and the Commission to originally hear complaints on this subject, there might be a divergence between the action of the Commission and the decision of a court . . . [T]hus a conflict would arise which would render the enforcement of the act impossible.

Id. at 441.

¹⁰ See, e.g., *United States Nav. Co. v. Cunard S.S. Co.*, 284 U.S. 474 (1932), where the Court held that plaintiff must first go to the Shipping Board for determination because of the complexity of the issue:

Their business involves questions of an exceptional character, the solution of which may call for the exercise of a high degree of expert and technical knowl-

trust principles is the contention that the competitive ideal should be paramount, as competition achieves our desired goals of increasing productivity and the total wealth of society.¹¹ Furthermore, only judges can be truly impartial, for regulatory agencies tend to lose their reforming zeal and are even prone to become spokesmen for those whom they regulate.¹²

Although these opposing views are debated in other situations, a principal point of conflict concerns antitrust exemptions. The exemptions represent an effort to accommodate the policies of antitrust and regulatory agency control by creating immunities from antitrust suits¹³ in some areas of agency jurisdiction.¹⁴ They may be created expressly by statute,¹⁵ by judicial decisions alone,¹⁶ or impliedly in the regulatory legislation.¹⁷ In recent years antitrust advocates have been fairly successful, for there has been a noticeable erosion in the antitrust

edge. Whether a given agreement among such carriers should be held to contravene the act may depend upon a consideration of economic relations, of facts peculiar to the business or its history, of competitive conditions in respect of the shipping of foreign countries, and of other relevant circumstances, generally unfamiliar to a judicial tribunal, but well understood by an administrative body especially trained and experienced in the intricate and technical facts and usages of the shipping trade; and with which that body, consequently, is better able to deal.

Id. at 485.

¹¹ See Kestenbaum, *Primary Jurisdiction to Decide Antitrust Jurisdiction: A Practical Approach to the Allocation of Functions*, 55 GEO. L.J. 812 (1967); Schwartz, *Legal Restriction of Competition in the Regulated Industries: An Abdication of Judicial Responsibility*, 67 HARV. L. REV. 436 (1954).

¹² See Huntington, *The Marasmus of the I.C.C.: The Commission, The Railroads, and The Public Interest*, 61 YALE L.J. 467 (1962). The author argues that the ICC has lost its vitality because of increasing affiliation with the carriers it was supposed to be regulating and in reality became a "defender of the status quo." *Id.* at 507. See also Note, *Regulated Industries and the Antitrust Laws: Substantive and Procedural Coordination*, 58 COLUM. L. REV. 673, 697 (1958).

¹³ An antitrust immunity is not the only reason that certain anticompetitive actions and policies are permitted. In *Board of Trade of the City of Chicago v. United States*, 246 U.S. 231 (1918), for example, the Board of Trade's "call" rule was upheld, since it was justified under the rule of reason. Similarly, many of the exchange rules questioned today might be upheld under this approach even if there were no antitrust immunities.

¹⁴ It is estimated that there are over 20 such exemptions. Pogue, *The Rationale of Exemptions from Antitrust*, 19 ABA. ANTITRUST SECTION 313, 314 (1961). For a summary of some of the more important exemptions see *Antitrust Exemptions*, 33 ABA. ANTITRUST L.J. 1 (1966-67).

¹⁵ *E.g.*, agreements and conduct of ocean shipping conferences that have been approved by the Federal Maritime Commission, 46 U.S.C.A. § 814 (Supp. 1969); and certain activities in the railroad industry, Reed-Bullwinkle Act, 49 U.S.C. § 5b(9) (1964).

¹⁶ *E.g.*, professional baseball. *Federal Baseball Club v. National League*, 259 U.S. 200 (1922).

¹⁷ An implied statutory exemption existed in the securities industry until *Silver v. New York Stock Exchange*, 373 U.S. 341 (1963). This case destroyed the complete immunity, but an implied partial immunity still exists to a yet undetermined extent.

exemptions and previously immune industries are now challenged in the courts.¹⁸

II

ANTITRUST PRINCIPLES AND THE SECURITIES INDUSTRY

A. *The Statutory System*

Long before the SEC was created, exchanges policed themselves. The New York Stock Exchange, for example, was regulated by its Constitution and Rules of the Board of Governors.¹⁹ Today, under the Securities Exchange Act of 1934,²⁰ the exchanges continue to be largely self-regulated,²¹ and the SEC has the unique status of "supervisor of 'self-regulators.'"²² This supervisory position is designed to permit review of exchange practices to assure that the exchanges exercise their delegated powers in the public interest.²³

Unfortunately, the two statutory provisions enabling the SEC to control the exchanges are not well adapted to solving the disputes that have arisen concerning anticompetitive exchange practices. Section 6,²⁴ which requires an exchange to register, provides that the rules of the exchange must be "just and adequate to insure fair dealing and to protect investors."²⁵ Conceivably, this section could be interpreted as a requirement that antitrust criteria be considered when the rules are formulated. However, the sanction, revocation of regis-

¹⁸ The exemptions have lost their vitality in such diverse fields as:

- a) organized labor: *Local 189, Amalgamated Meat Cutters v. Jewel Tea Co.*, 381 U.S. 676 (1965); *U.M.W. v. Pennington*, 381 U.S. 657 (1965);
- b) insurance: *United States v. Chicago Title & Trust Co.*, 242 F. Supp. 56 (N.D. Ill. 1965);
- c) banking: *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321 (1963);
- d) natural gas: *United States v. El Paso Natural Gas Co.*, 376 U.S. 651 (1964);
- e) securities: *Silver v. New York Stock Exchange*, 373 U.S. 341 (1963).

See generally Orrick, *The Recent Erosion of Certain Antitrust Exemptions*, 10 ANTITRUST BULL. 667 (1965).

¹⁹ See, e.g., 2 CCH N.Y.S.E. GUIDE.

²⁰ 15 U.S.C. § 78a-hh (1964).

²¹ The purpose of the self-regulation provisions of the Securities Exchange Act was to delegate governmental power to working institutions which would undertake, at their own initiative, to enforce compliance with ethical as well as legal standards in a complex and changing industry.

Silver v. New York Stock Exchange, 373 U.S. 341, 371 (1963) (Stewart, J., dissenting).

²² SEC, SPECIAL STUDY OF SECURITIES MARKETS pt. IV, at 501 (1963) [hereinafter cited as SPECIAL STUDY].

²³ *Id.* at 723.

²⁴ 15 U.S.C. § 78f (1964).

²⁵ 15 U.S.C. § 78f(d) (1964).

tration,²⁶ for non-compliance with section 6 is a means of enforcement too potent and inflexible to foster active SEC regulation in the area of antitrust. Section 19(b)²⁷ provides a potentially more flexible approach to antitrust control. It gives the SEC the power to change existing exchange rules if

such changes are necessary or appropriate for the protection of investors or to insure fair dealing in securities traded in upon such exchange or to insure fair administration of such exchange²⁸

Section 19(b) appears to confer broad regulatory powers upon the SEC, but historically it has been a weak section.²⁹ Perhaps its underlying weakness is that the standard of "fair administration" has not been defined by case law. In particular, it is unclear whether this standard authorizes the SEC to apply antitrust concepts in deciding if a rule should be changed. The one case³⁰ decided by the SEC under section 19(b) involved a NYSE rule regarding the expulsion of members and non-members. In interpreting "fair administration" and ordering an alteration of the rule, the SEC clearly considered antitrust principles.³¹ Since this 1941 decision, however, antitrust principles apparently have not been a significant factor in SEC decisions.³²

The SEC is far from taking the lead in resolving disputes raising antitrust issues. In large part this is the fault of the statute. First, section 19(b) is couched in permissive language and neither compels the SEC to look at exchange rules as a matter of course nor sets out definite criteria to be used in examining rules. This deficiency is probably responsible for the dearth of proceedings expressly involving antitrust principles. Second, the Commission does not have authority to change rules across the board but is limited to specified areas.³³

²⁶ 15 U.S.C. § 78s(a) (1964).

²⁷ 15 U.S.C. § 78s (1964).

²⁸ 48 Stat. 898 (1934), 15 U.S.C. § 78s(b) (1964).

²⁹ 2 L. LOSS, *SECURITIES REGULATION* 1182 (1961).

³⁰ *The Rules of the New York Stock Exchange*, 10 S.E.C. 270 (1941).

³¹ It seems to us, therefore, that the Rule would operate as an unreasonable and unjustified restraint upon interstate commerce and that enforcement of the Rule would violate one of the basic purposes of regulation under the Act, a purpose which is closely related to the public policy regarding unreasonable restraints and the maintenance of fair competition as declared by Congress in the Sherman Act, the Clayton Act, and the Federal Trade Commission Act.

Id. at 287.

³² Recently, and probably as a result of the *Silver* decision, the SEC again raised the antitrust factor by declaring that "antitrust considerations should receive the closest scrutiny." SEC Securities Exchange Act Release No. 8239, at 2 (Jan. 26, 1968).

³³ 15 U.S.C. § 78s(b) (1964). There are thirteen areas where the SEC may change or alter exchange rules, the last of which is "similar matters." Whether this provision could be defined as including all exchange rules is doubtful, for the statutory listing of specified areas of authority could be interpreted as an intent to limit the areas of SEC intervention.

Third, the SEC is not required to examine exchange rules in advance of their taking effect, and the Commission has not assumed affirmative power to approve or disapprove all rules.³⁴ Finally, no statutory antitrust exemption clearly delineates the balance of jurisdiction between the Commission and the courts concerning possible antitrust violations. Nevertheless, people are injured by exchange practices, and some forum should exist to consider antitrust charges.

B. *Antitrust and the Courts*

Among specific exchange practices that clearly raise antitrust questions are minimum commission rates;³⁵ rules formulated to restrict multiple trading in listed securities;³⁶ restrictive exchange membership requirements that tend to control entry into the market;³⁷ and even proposals for eliminating the paperwork backlogs currently plaguing brokerage houses.³⁸ Not surprisingly, commentators and aggrieved parties have attacked exchange practices and demanded that some tribunal be made available for examining the anticompetitive practices of the exchanges.³⁹

Until 1963, however, persons raising antitrust issues were without a forum. The SEC, either because of timidity⁴⁰ or a belief that section

³⁴ In *United Funds, Inc. v. Carter Products, Inc.*, [1961-1964 Transfer Binder] CCH FED. SEC. L. REP. ¶ 91,288 (Md. Baltimore City Cir. Ct. 1963), the court stated at 94,284 that "[s]ection 19(b) of the Securities Exchange Act gives the S.E.C. full authority and power to approve or disapprove changes in the rules of a registered exchange." However, the statute does not expressly grant such power to the SEC and the Commission itself has never assumed the role of approving or disapproving rules or rules changes before they have been given effect.

³⁵ N.Y.S.E. CONST. art. XV, in 2 CCH N.Y.S.E. GUIDE 1701-12. Several commentators have selected the minimum commission rate structure for particular criticism. See, e.g., Note, *Antitrust and the Stock Exchange: Minimum Commission or Free Competition?*, 18 STAN. L. REV. 213 (1965).

The Justice Department, in a recent memorandum to the SEC, has recommended that the minimum commission schedule be abolished within five years and replaced with open competition among brokers to determine rates. N.Y. Times, Jan. 18, 1969, at 1, col. 7 (city ed.).

The plight of the institutional investor has received a good deal of comment, and in response, Congress has authorized the SEC to undertake a study of the problems of the institutional investor. 15 U.S.C.A. § 78s(e) (Supp. 1969). Perhaps this study will result in rules changes regarding the rate structure of commissions.

³⁶ E.g., N.Y.S.E. Rule 394, in 2 CCH N.Y.S.E. GUIDE 2394.

³⁷ N.Y.S.E. CONST. art. IX, in 2 CCH N.Y.S.E. GUIDE 1401-15; N.Y.S.E. Rules 301-21, in 2 CCH N.Y.S.E. GUIDE 2301-21.

³⁸ Note, *The Back Office Problem and the Antitrust Laws*, 69 COLUM. L. REV. 299 (1969).

³⁹ See generally sources cited in note 2 *supra*.

⁴⁰ The SEC is not immune to the lethargy that can affect any administrative agency. A past Chairman of the SEC has stressed the need for continual re-examination of the agency's goals:

19(b) was inapplicable or inappropriate, did not consider these problems. The courts created an implied antitrust exemption that forbade their hearing antitrust suits in the securities industry. Wishing to avoid a clash with the SEC, courts interpreted section 19(b) as reserving jurisdiction in that agency and withdrew from activity in this area.⁴¹

This mutual abdication could last only until a particularly harsh case forced one of the forums to grant relief. Influenced perhaps by the gradual erosion in antitrust exemptions, the courts yielded first, in *Silver v. New York Stock Exchange*.⁴² Silver, a non-member broker, had direct wire connections to a member firm for receiving over-the-counter quotations. Under a rule of the New York Stock Exchange the wires were ordered removed. Silver was given neither notice nor an opportunity for a hearing on this decision which greatly reduced his business. In an antitrust suit against the exchange, the Supreme Court ruled that the implied antitrust exemption extended to those rules that were within the jurisdiction of the SEC, but that the issue before the Court involved an "interpretation" of a rule rather than the rule itself. The Court then held that interpretation was outside the SEC's jurisdiction and, by this rather technical holding, granted relief to Silver.

Other aggrieved investors and brokers, heartened by the outcome in *Silver*, initiated antitrust suits involving various exchange rules and practices,⁴³ but their enthusiasm proved to be premature. Courts

I firmly believe that any institution—private or public—can be run honestly and tirelessly and yet at the same time it can die. Rigor mortis will set in if all of us do not reexamine ourselves, find out where the industry has been moving, and accordingly re-define our responsibilities.

Cary, *Self-Regulation in the Securities Industry*, 49 A.B.A.J. 244 (1963).

⁴¹ Of course there were views to the contrary. In *United States v. Morgan*, 118 F. Supp. 621, 697 (S.D.N.Y. 1953), Judge Medina argued that congressmen were aware of antitrust principles when the Securities Exchange Act of 1934 was enacted and that "they intended no exemption to the Sherman Act; and it is hardly probable that they would inadvertently accomplish such a result."

⁴² 373 U.S. 341 (1963).

⁴³ In *Cowen v. New York Stock Exchange*, 371 F.2d 661 (2d Cir. 1967), an employee of a member firm of the exchange was discharged for being involved in a tainted transaction. He brought an antitrust suit against the exchange on the ground of procedural unfairness in its failure to give him a hearing. Unlike *Silver*, the plaintiff had been given notice of the charges against him and the reasons for his dismissal; the suit was dismissed.

Thill Securities Corp. v. New York Stock Exchange, [1967-1969 Transfer Binder] CCH FED. SEC. L. REP. ¶ 92,189 (E.D. Wis. 1968), involved more than the procedural questions of *Silver* and *Cowen*. Plaintiff, a non-member firm, brought an antitrust suit against the exchange after being denied access to the trading floor under the rules of the exchange.

subsequently have limited the holding in *Silver* to its facts, to circumstances of extreme unfairness resulting from the denial of procedural safeguards. These plaintiffs' lack of success indicates the continued reluctance of courts to permit direct antitrust suits in the securities industry.

Undoubtedly the most significant post-*Silver* case is *Kaplan v. Lehman Brothers*.⁴⁴ *Kaplan* raised the highly controversial question of an exchange's power to set minimum commission rates for its member brokers, as the NYSE has been doing since its founding under the Buttonwood Tree Agreement in 1792.⁴⁵ For round lot transactions, brokers are required to charge the same per-share rate regardless of the number of shares involved; it therefore costs ten times as much to trade 1,000 shares as it does to trade 100 shares, even though the costs of making these transactions are not appreciably different.⁴⁶ Plaintiffs in *Kaplan*, who carried out large transactions, alleged that the minimum commission requirement violated the antitrust laws, since if competition were permitted among brokers their brokers' fees would have been eleven percent less.⁴⁷

Their case rested on section 19(b)(9) of the Exchange Act, which gives the SEC power to alter exchange rules dealing with the "fixing of reasonable rates of commission." Focusing on the word "reasonable," plaintiffs claimed that the minimum commission rates were unreasonable since the costs involved were not dependent upon the size of the transaction although the commissions were. The court refused to rule on the reasonableness issue, holding that, since section 19(b)

The real basis for this case is an attack on the limited membership of the NYSE. With only 1,366 natural persons allowed a seat, and the corresponding privilege of trading on the exchange, many thousands of brokerage firms are excluded by the high cost of buying one seat. This case has yet to be decided on the merits because of a venue challenge; however, the *Silver* rationale seems to bar any recovery. At least implicitly, the SEC has jurisdiction under § 19(b)(5) or the catch-all provision of § 19(b)(13), and there is thus an implied exemption from the antitrust statutes.

⁴⁴ 250 F. Supp. 562 (N.D. Ill. 1966), *aff'd*, 371 F.2d 409 (7th Cir.), *cert. denied*, 389 U.S. 954 (1967).

⁴⁵ B. SHULTZ, *THE SECURITIES MARKET—AND HOW IT WORKS* 2 (1963). *THE SPECIAL STUDY*, pt. 2, at 295 states:

The avowed objectives of organizing the NYSE in 1792 were the setting of minimum commission rates and the establishment of a preference for members of the Exchange in their dealings with other members . . .

⁴⁶ *SPECIAL STUDY*, pt. 2, at 320.

⁴⁷ It is clear that but for the 1934 Act, the agreement to fix the prices of brokerage commissions would be a per se violation of antitrust laws. *United States v. National Ass'n of Real Estate Bds.*, 339 U.S. 485, 489 (1950); *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 218 (1940); *United States v. Trenton Potteries Co.*, 273 U.S. 392, 396-98 (1927).

confers jurisdiction over exchange rates on the SEC, the antitrust exemption denied the court power to hear the case.⁴⁸

The real injustice in a case such as *Kaplan* is not its failure to strike down minimum commission rates⁴⁹ or other exchange practices, but its failure to provide a forum in which grievances can be aired. The *Kaplan* court refused jurisdiction on the unwarranted assumption that the SEC would act on antitrust problems. But even if the Commission does not act, its jurisdiction over such problems brings the antitrust exemption into play and bars judicial relief.⁵⁰ The *Silver* Court is the only court that has heard the merits of an antitrust grievance, and the SEC has heard only one proceeding under section 19(b).

Present inaction is intolerable; fairness demands that some forum listen to and decide cases where genuine antitrust grievances are raised. Recent cases in the shipping industry suggest a method by which the securities exchanges might be more effectively regulated in antitrust matters.

III

ANTITRUST PRINCIPLES IN THE SHIPPING INDUSTRY⁵¹

Despite distinct differences in subject matter, the securities and shipping industries are strikingly similar in the manner of their regulation. Each industry was self-regulated before its respective regulatory agency was created, and each has remained, through statutory

⁴⁸ A similar result was achieved under the Investment Company Act of 1940 in a suit premised on a Robinson-Patman Act violation. The court in *Baum v. Investors Diversified Services, Inc.*, 286 F. Supp. 914 (N.D. Ill. 1968), *aff'd*, CCH FED. SEC. L. REP. ¶ 92,405 (7th Cir. Apr. 18, 1969), held that an antitrust exemption existed because of SEC jurisdiction under § 22 of the Investment Company Act.

⁴⁹ An effective challenge to minimum commission practices may be forthcoming shortly. The Justice Department has taken a position in favor of competitive rates on the ground that the present rate structure, "by sheltering firms from competition, leads to inefficiency, and high costs, and may have contributed to the serious clearing problems in the brokerage industry." CCH FED. SEC. L. REP. ¶ 77,658, at 83,440.

⁵⁰ The [*Kaplan*] court . . . did not cite a single instance where the S.E.C. exercised its § 19(b) powers over rates, for the simple reason that the S.E.C. never has. The dangerous precedent established is that unused regulatory power, power guided by no clearly delineated competitive standard and direction, constitutes regulatory pervasiveness sufficient to invoke an antitrust immunity. If S.E.C. rate power is pervasive, the S.E.C. seems unconcerned about it. After 33 years and the NYSE's adoption of five rate increases (at minimum rates), the S.E.C. has never convened a rate hearing or instituted a formal rate investigation

Petitioner's Brief for Certiorari at 36, *Kaplan v. Lehman Bros.*, 389 U.S. 954 (1967).

⁵¹ For a broad discussion of this general topic see Comment, *Accommodations of Antitrust Law and Ocean Shipping Regulation*, 4 TEXAS INT. L.F. 393 (1968).

design, a primarily self-regulated industry despite the presence of a regulatory agency.⁵²

Self-regulation in the shipping industry is accomplished through the conference system. The conference is an organization of steamship lines that controls shipping rates and practices in one trade route; that is, from one geographical point to another.⁵³ Conferences were developed in the late nineteenth century when an excess of cargo space caused cut-throat price competition that jeopardized the survival of many lines. The conferences' pricefixing practices were clearly anticompetitive but, as a practical matter, were necessary to stabilize chaotic conditions and were essential to the continued existence of many steamship lines.

In 1916 Congress enacted the Shipping Act⁵⁴ to regulate the industry and decided to retain the conferences as a part of the statutory scheme. Under the Act, however, the conferences are required to submit any agreements to the Federal Maritime Commission for approval before they become effective.⁵⁵ The FMC has the power to approve or "disapprove, cancel or modify any agreement,"⁵⁶ according to statutory standards. Unlike the Securities Exchange Act, which is silent as to antitrust exemptions, the Shipping Act expressly exempts from the antitrust laws those agreements approved by the FMC.⁵⁷

For a number of years antitrust problems in the shipping industry were treated in the same way as similar problems are currently treated in the securities industry. If the regulatory agency had jurisdiction, the courts would not entertain the suit, regardless of whether the agency actually acted on the matter. Early case law extended the statutory antitrust exemption by bringing within its protection unapproved agreements as well as those specifically approved by the FMC.

⁵² The principal objection to such an analogy is that antitrust exemptions result from historical developments within each specific industry. The exemptions were created to meet the specific problems of each area and neither the statutes nor the case law has attempted to draw binding precedents from one area to another.

A reading of the cases will indicate that most judges treat each area quite distinctly. Justice Goldberg, for example, wrote the majority opinion in *Silver* that permitted antitrust suits in the securities industry for the first time and yet vigorously dissented when the Court reopened the path to antitrust litigation in organized labor. Local 189, Amalgamated Meat Cutters v. Jewel Tea Co., 381 U.S. 676, 697 (1965) (Goldberg, J., dissenting).

⁵³ For an excellent discussion of the conference system and its ratemaking function see Note, *Rate Regulation in Ocean Shipping*, 78 HARV. L. REV. 635 (1965).

⁵⁴ 46 U.S.C. § 801 (1964).

⁵⁵ 46 U.S.C.A. § 814 (Supp. 1969).

⁵⁶ *Id.*

⁵⁷ *Id.*

In *United States Navigation Co. v. Cunard Steamship Co.*,⁵⁸ for example, a private antitrust suit was brought on the theory that a dual-rate agreement had not been approved by the Shipping Board (predecessor to the FMC). The Court dismissed the suit on the ground that the controversy was within the jurisdiction of the Shipping Board.

The courts, however, gradually began to look differently at the administrative agency's role in the shipping industry. Although in 1952 the Supreme Court was still deferring to the agency under the familiar reasons of uniformity and expertise,⁵⁹ in 1954 the courts began to pressure the FMC into taking a more active role. In *Isbrandtsen Co. v. United States*⁶⁰ the District of Columbia Circuit required the agency to hold a hearing on, and approve, conference agreements *before* the agreements became effective; this decision effectively eliminated the situation in which an agency's failure to act could create an antitrust immunity. The court used language that could be appropriately applied to the securities industry:

This pre-approval illegality [of conference rules] stems from the fact that the Shipping Act specifically provides machinery for legalizing that which would otherwise be illegal under the antitrust laws. The condition upon which such authority is granted is that the agency entrusted with the duty to protect the public interest scrutinize the agreement to make sure that the conduct thus legalized does not invade the prohibitions of the anti-trust laws any more than is necessary to serve the purposes of the regulatory statute.⁶¹

Even greater pressure was put on the agency by the Supreme Court in *Federal Maritime Board v. Isbrandtsen Co.*⁶² Here the Board had authorized a dual-rate system by a conference, but this approval notwithstanding, the Court overruled the agency. This decision has been credited with making the agency more aggressive and receptive to antitrust principles when considering the actions and proposals of the conferences.⁶³

Recent developments have increased the pressure to assure that competition plays as great a role as possible in the shipping industry.

⁵⁸ 284 U.S. 474 (1932). This case had been followed by other cases in the shipping industry, including *Far East Conference v. United States*, 342 U.S. 570 (1952).

⁵⁹ *Far East Conference v. United States*, 342 U.S. 570, 574-75 (1952).

⁶⁰ 211 F.2d 51 (D.C. Cir.), *cert. denied*, 347 U.S. 990 (1954).

⁶¹ *Id.* at 57 (footnotes omitted).

⁶² 356 U.S. 481 (1958).

⁶³ Comment, *Ocean Shipping Conferences and the Federal Maritime Commission*, 53 CORNELL L. REV. 1070, 1076 (1968).

The antitrust exemption has been restricted to the rule expressly formulated in the statute; *i.e.*, only those agreements approved by the FMC are exempt. In *Carnation Co. v. Pacific Westbound Conference*⁶⁴ the conference increased the shipping rates for evaporated milk without seeking prior approval of the FMC, and Carnation brought an antitrust action. Under the *Cunard* decision, the traditional defense of the antitrust exemption would have been binding on the Court since rate changes are clearly within the jurisdiction of the FMC. The Court, however, noted that only approved agreements fall within the statutory exemption and held that "the implementation of rate-making agreements which have not been approved by the Federal Maritime Commission is subject to the antitrust laws."⁶⁵

A second development is the formulation of the criteria the FMC must consider when it approves or disapproves the rules and agreements of a conference. If it is true that agencies tend to be spokesmen for the regulated industries, a want of standards creates the danger that agency approval is a ritual that broadens the antitrust immunity without considering the public interest. A 1961 amendment added to the existing standards of the Shipping Act a requirement that conference rules be disapproved if "contrary to the public interest."⁶⁶ Since this public interest standard had been interpreted in other regulatory statutes as requiring the agency to investigate antitrust principles,⁶⁷ it opened the way for a new approach in examining conference agreements.

The first test of this standard under the Shipping Act came in *Federal Maritime Commission v. Aktiebolaget Svenska Amerika Linien (Swedish American)*,⁶⁸ where a conference adopted two rules that clearly would have violated the antitrust laws were it not for the regulatory statute.⁶⁹ The FMC refused to approve these rules under the public interest standard "because the anticompetitive activity under the agreement invades the prohibitions of the antitrust laws more than is necessary to serve the purposes of the Shipping Act and

⁶⁴ 383 U.S. 213, *modified*, 383 U.S. 932 (1966).

⁶⁵ *Id.* at 216.

⁶⁶ 46 U.S.C.A. § 814 (Supp. 1969).

⁶⁷ See *California v. FPC*, 369 U.S. 482, 484-85 (1962); *United States v. R.C.A.*, 358 U.S. 334, 351 (1959).

⁶⁸ 390 U.S. 238 (1968).

⁶⁹ The first was a "tying" rule of the conferences prohibiting agents who sold tickets on conference lines from selling tickets on competing nonconference lines. The second was the "unanimity" rule, which required unanimous action by conference members before the maximum commission rates of travel agents could be changed. *Id.* at 240.

is therefore contrary to the public interest."⁷⁰ Before the Supreme Court, the conference argued that making antitrust principles one of the standards for disapproval would, in effect, repeal the statutory exemptions. The Court held, however, that antitrust principles were an appropriate concern of the FMC. The Court reasoned that some anticompetitive agreements would be justifiable and thus give meaning to the exemption.⁷¹

This method of infusing antitrust principles into the regulatory framework of the shipping industry is a sound approach. Since the conferences initiate all rules and agreements, the desired self-regulatory scheme is preserved. By requiring the agency to give *prior* approval to all rules and to consider antitrust principles, the desired application of these principles is achieved. A potential plaintiff is thus assured that at least one forum has examined the antitrust ramifications of proposed industry practices. Finally, limiting the statutory exemption to approved agreements permits antitrust litigation by aggrieved parties in all other situations.⁷²

IV

FUTURE ANTITRUST DIRECTIONS IN THE SECURITIES INDUSTRY

Even before *Swedish American* there were indications that changes would be forthcoming in the application of antitrust principles to the securities industry. The New York Stock Exchange recognized that SEC regulation is "an important bulwark of our antitrust immu-

⁷⁰ Investigation of Passenger Steamship Conferences Regarding Travel Agents, 10 F.M.C. 27, 35 (1966) (footnote omitted).

⁷¹ 390 U.S. at 245. The technique of requiring regulatory agencies to take account of antitrust principles is not entirely unique. See, e.g., *McLean Trucking Co. v. United States*, 321 U.S. 67 (1944), where the Court sustained an ICC-approved merger as in the public interest because substantial economies justified and offset the anticompetitive aspects of the merger.

⁷² See, e.g., *Sabre Shipping Corp. v. American President Lines, Ltd.*, 285 F. Supp. 949 (S.D.N.Y. 1968). Plaintiff brought an antitrust suit alleging that he was driven out of business by low rates that were fixed by a conference and later raised after he had gone out of business. The conference agreement on the low rates was filed with the FMC and allowed to go into effect upon the filing even though the FMC had not taken action either to approve or disapprove the rates. The defendant conferences moved to dismiss the suit on the grounds of the antitrust exemption. The court, however, citing both *Carnation* and *Swedish American*, held that the conferences were not immune from antitrust litigation until the conference agreements were actually approved by the FMC. Since this agreement was not approved, the suit was not dismissed.

nity."⁷³ and the SEC itself was careful at least to pay lip service to the antitrust implications of its work.⁷⁴ Moreover, a judicial concern with the crudeness of implied antitrust exemptions was apparent. Courts noted that such exemptions are "strongly disfavored."⁷⁵ The *Swedish American* decision indicates that a court hearing *Kaplan v. Lehman Brothers* today might not consider itself without jurisdiction; an institutional argument based on the lack of antitrust considerations by any forum would be a timely alternative to the argument of reasonableness made in *Kaplan*. It is significant in this regard that Chief Justice Warren, in his dissent to the Court's denial of certiorari in *Kaplan*,⁷⁶ protested vigorously against the judiciary's "blunderbuss approach"⁷⁷ of using section 19(b) to create an antitrust immunity.

Arguably the implied antitrust exemption of the securities industry could be totally removed and the courts opened to antitrust suits in which such disputes could be resolved.⁷⁸ This suggestion, made by the Justice Department during the minimum commission rate controversy,⁷⁹ is not sound, however. Without some type of antitrust exemption, the exchanges would be in a continual state of uncertainty as to what acts they could undertake. Furthermore, private antitrust

⁷³ We hear it said that this intrusion on profitability was none of our business, neither the Stock Exchange's business nor the SEC's. But I take a contrary view. I submit it was not only a concern and responsibility of the NYSE, but that oversight review by the SEC is mandated by the 1934 Act. It comprises an important bulwark of our anti-trust immunity.

CCH FED. SEC. L. REP. ¶ 77,667, at 83,463 (Remarks of Robert W. Haack, President of the NYSE, Jan. 22, 1969).

⁷⁴ SEC Securities Exchange Act Release No. 8239 (Jan. 26, 1968):

This necessarily contemplates that full consideration be given to the policies of the antitrust laws [I]t is clear that antitrust considerations should receive the closest scrutiny.

Id. at 2.

⁷⁵ "Repeals of the antitrust laws by implication from a regulatory statute are strongly disfavored." *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321, 350 (1963).

⁷⁶ See text accompanying notes 44-51 *supra*.

⁷⁷ *Kaplan v. Lehman Bros., cert. denied*, 389 U.S. 954, 957 (1967) (Warren, C. J., dissenting).

⁷⁸ It is not clear that removing the exemptions would actually open the courts, since the courts might resort to the doctrine of primary jurisdiction to achieve the same results as those presently reached under the antitrust exemptions.

⁷⁹ The conclusion which emerges from the record of this proceeding is that the system of fixed minimum commissions is not justified or needed "to make the Securities Exchange Act work." Indeed, the present system has produced serious detriments by fragmenting the market and leading to undesirable practices and market restrictions. As a consequence, not only are the antitrust laws applicable, but the objectives of the Exchange Act also are inconsistent with the present rate structure.

CCH FED. SEC. L. REP. ¶ 77,658, at 83,442.

suits could easily be used to circumvent the SEC and might so undermine the Commission that it would cease to be an effective regulator. Finally, the courts are ill-equipped to handle technical securities industry matters,⁸⁰ and they would be plagued with too many "garden-variety customer-broker suits."⁸¹ The SEC is better equipped than the courts in both expertise and staff to fully investigate antitrust issues. It is the appropriate forum to handle antitrust disputes,⁸² and the exemptions, therefore, should not be removed.⁸³

However, because *Swedish American* suggests that the *Kaplan* decision is vulnerable, it is incumbent on the SEC to act decisively in considering antitrust principles before the courts permit more comprehensive application of the antitrust laws to the securities industry. The shipping industry provides a good model. No sweeping revision of the existing statutory framework is required. The basic self-regulatory scheme is sound, since it is desirable that the industry's rules be proposed by the exchanges themselves.⁸⁴ The two changes that are necessary if the SEC is to give real content to antitrust principles are in approach rather than in organization and must parallel the developments in the shipping industry: the courts must take a more active role in overseeing the SEC's activities, and the SEC itself must take more initiative in applying antitrust principles.

The courts' role must be to assure that antitrust principles are given genuine consideration. It should no longer be sufficient for the courts merely to look for potential SEC jurisdiction under section 19(b) and, upon finding it, disqualify themselves on the ground of an

⁸⁰ As the district court stated in *Kaplan*, "Ratemaking is a matter for which the courts are ill-equipped, and accordingly a matter traditionally committed to an administrative agency." 250 F. Supp. at 566.

⁸¹ *Colonial Realty Corp. v. Bache & Co.*, 358 F.2d 178, 183 (2d Cir. 1966).

⁸² This is the conclusion of the SPECIAL STUDY, pt. IV, at 724:

It is the belief of the Special Study that if self-regulation is to function effectively and with due regard for all aspects of the public interest, including the interest in vigorous self-regulation, the forum for review of self-regulatory action should be the agency already established as the official, expert guardian of the public interest in the field of securities; i.e., the Commission.

⁸³ Neither should the securities industry be given a blanket antitrust immunity as has been proposed. Wall St. J., Apr. 26, 1965, at 1, col. 6. To do so would free the Commission from all scrutiny, whereas past experience indicates that agencies promote the public interest more effectively if under some form of supervision.

⁸⁴ The SPECIAL STUDY generally endorses the self-regulation framework and recommends that it be retained:

[T]he basic statutory design of substantial reliance on industry self-regulation appears to have stood the test of time and to have worked effectively in most areas. In other words, the study has concluded that the demonstrated strengths and benefits of self-regulation outweigh its disclosed inadequacies

SPECIAL STUDY, pt. IV, at 504.

antitrust exemption. In the shipping industry the courts filled this role by requiring the agency to hold hearings and give specific approval of rules,⁸⁵ overruling agency decisions that failed to follow certain standards,⁸⁶ refusing to grant antitrust immunity to unapproved rules,⁸⁷ and affirming that the content of the agency's investigation included consideration of antitrust principles.⁸⁸ Courts should now take similar steps to achieve this desired infusion of antitrust principles into securities industry regulation.

As the *Swedish American* decision indicates, however, the major burden of applying antitrust principles must fall primarily on the regulatory agency. The SEC lacks the well-defined grant of authority that the Shipping Act's standard of "public interest" gives to the FMC. However, section 19(b) of the Exchange Act contains a standard of "fair administration" that is sufficiently broad to permit the formulation of antitrust principles.⁸⁹ The SEC has recently recognized an obligation to apply antitrust principles.⁹⁰ Unfortunately, to date there have been no sweeping changes in SEC proceedings to assure significantly greater regulation of the exchanges under section 19(b). Of course, the legal underpinnings are to no avail unless the courts require changes or SEC personnel themselves decide to adopt a more aggressive posture. Certainly the new-found powers of the FMC in applying antitrust principles have been to a large degree a result of "more dynamic leadership."⁹¹

⁸⁵ *Isbrandtsen v. United States*, 211 F.2d 51 (D.C. Cir.), cert. denied, 347 U.S. 990 (1954).

⁸⁶ *Federal Maritime Bd. v. Isbrandtsen Co.*, 356 U.S. 481 (1958).

⁸⁷ *Carnation Co. v. Pacific Westbound Conference*, 383 U.S. 213, modified, 383 U.S. 932 (1966).

⁸⁸ *Federal Maritime Comm'n v. Aktiebolaget Svenska Amerika Linien* (Swedish American), 390 U.S. 238 (1968).

⁸⁹ Turner, *The Scope of Antitrust and Other Economic Regulatory Policies*, 82 HARV. L. REV. 1207, 1234, 1238 (1969). The author suggests that the language of regulatory statutes is sufficiently broad to permit an aggressive agency to take an active role in innovation and control.

⁹⁰ SEC Securities Exchange Act Release No. 8239 (Jan. 26, 1968).

Manuel Cohen, the past Chairman of the SEC, expressed a desire to have the SEC, not the courts, take prime responsibility in the antitrust area:

We firmly believe that in matters like . . . commission rates that the Commission with its responsibility and concern for these matters is in the best position to comprehend and reconcile the diverse factors and considerations that may bear upon the public interest in the manifold circumstances under which questions may arise. Ad hoc determinations in the antitrust courts of complex matters such as these could have an undesirable impact upon the quality of the markets and the interests of the investing public.

111 CONG. REC. 19022 (1965).

⁹¹ Comment, *Ocean Shipping Conferences and the Federal Maritime Commission*, 53 CORNELL L. REV. 1070, 1076 (1968).

If the SEC is to meet the standards of *Swedish American* and use its regulatory powers with antitrust considerations in mind, several new approaches will be required. Under its broad mandate to regulate to assure the "fair administration" of exchanges,⁹² the Commission should assume the power to approve or disapprove proposed rules and should require, as does the FMC, that all new rules and modifications of rules be submitted in advance for its consideration. Using the power given by section 19(b) to alter existing rules, it should also periodically re-examine old rules. In both situations open hearings should be held. As in *Swedish American*, the agency should make an initial determination of whether, in the absence of the statute, the rule would violate antitrust principles. If so, the rule should be disapproved unless the exchange meets its burden of justification.⁹³ A rule that is not approved should not be protected under the antitrust exemption. An approved rule, however, should be immune to direct attack in the courts.

The SEC has much to gain by taking the initiative in regulating antitrust matters in the securities industry. Such action is likely to decrease the possibility of expanded judicial activity in securities regulation. More important, investors and brokers who feel they have been damaged by industry practices will be assured of a forum that will hear the merits of their grievances.

Robert W. Wild

In the SEC there has been a recent change of leadership as Hamer H. Budge replaced Manuel F. Cohen as Chairman in February 1969. CCH FED. SEC. L. REP. Current Vol., Law Report Letter No. 243 (Feb. 26, 1969).

⁹² There is apparently no question about the SEC's power under § 19(b) to approve or disapprove proposed rules. See, e.g., *United Funds, Inc. v. Carter Products, Inc.*, [1961-1964 Transfer Binder] CCH FED. SEC. L. REP. ¶ 91,288, at 94,284 (Md. Baltimore City Cir. Ct. 1963).

⁹³ The broad standard of *Silver* might be considered:

[E]xchange self-regulation is to be regarded as justified in response to antitrust charges only to the extent necessary to protect the achievement of the aims of the Securities Exchange Act.

373 U.S. at 361.