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Antitrust Law: The state Action Exemption. (Cantor v. Detroit Edison Co.)

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RECENT DECISIONS

Antitrust Law — The State Action Exemption— In *Cantor v. Detroit Edison Co.*,¹ a retail druggist selling light bulbs charged that the local utility company, Detroit Edison, was using its monopoly power in the distribution of electricity to restrain competition in the sale of light bulbs.² The alleged anticompetitive behavior was a “lamp exchange program” through which Detroit Edison customers received free electric light bulbs in exchange for burned-out ones. Thus, the price charged for electric power reflected the added cost of supplying “free” light bulbs. When the state began to regulate Detroit Edison in 1909, the company did not eliminate this pricing practice. Thereafter, the Michigan Public Service Commission periodically approved tariffs for electric power which included the cost of the replacement bulbs. Once approved, the electric rates could not be changed or the light bulb exchange discontinued without the Commission’s approval. As a result of this distribution system, Detroit Edison provided fifty percent of the standard size electric light bulbs used in southeastern Michigan homes.

The lower courts³ held that the Detroit Edison lamp exchange program was state action exempted from antitrust liability under *Parker v. Brown*.⁴ In a closely decided case, the Supreme Court reversed.⁵ The plurality decided that the *Parker* rationale should not be extended to cover private action which was merely approved by the state and which must be continued while the state approval remains effective. Consequently, according to the court, the *Parker* rule offered Detroit Edison no protection from the antitrust law. The Court remanded the case for an application of the federal antitrust laws.

1. 96 S. Ct. 3110 (1976).

2. Petitioner’s complaint asserted that respondent’s light bulb exchange program violated §§ 1 and 2 of the Sherman Act, 15 U.S.C. § 2 (1970), and § 3 of the Clayton Act, 15 U.S.C. § 14 (1970).

3. *Cantor v. Detroit Edison Co.*, 392 F. Supp. 1110 (E.D. Mich. 1974), *aff’d*, 513 F.2d 630 (6th Cir. 1975) (unpublished decision).

4. 317 U.S. 341 (1943).

5. Justice Stevens wrote the plurality decision, joined in by Justices Brennan, White and Marshall. Chief Justice Burger and Justice Blackmun wrote concurring opinions. Justice Stewart wrote a dissenting opinion in which Justices Powell and Rehnquist joined.

According to the plurality in *Cantor*, the application of the *Parker* rule to Detroit Edison's lamp exchange program would be a gross distortion of that decision. The Court came to this conclusion by first assuming that certain facts in the *Parker* case were necessary to the decision. Thus the *Cantor* holding depends on the factual distinctions perceived by the court between that case and *Parker*.

*Parker v. Brown*⁶ involved a program under the California Prorate Act which regulated the marketing of raisins in that state. This program was specifically intended to restrict competition among growers and maintain prices in the distribution of their product to packers in order to "prevent economic waste in the marketing of agricultural products"⁷ in the state. An Agricultural Prorate Advisory Commission consisting of one state official, the Director of Agriculture, and eight members appointed by the governor, administered the program. The purpose of the Commission was to set quotas on raisin production in various areas of the state and to establish procedures to be followed in the marketing of the raisins. Even though the Commission set the production quotas, private producers played an important role in the operation of the program. For example, petitions for specific quotas and regulations came from the raisin producers themselves. Following commission approval of the petitions, consent of sixty-five percent of the producers in the area was necessary to establish the program as law.

Upon these facts the *Parker* Court established the state action exemption doctrine, holding that "[t]he state . . . as sovereign, imposed the restraint as an act of government which the Sherman Act did not undertake to prohibit."⁸ Although the court acknowledged the impact of private action on the marketing program, it relied on the totality of circumstances to determine that the program was essentially state action. The court observed that, although the producers made the proposals and voted on referenda, it was the state itself "which adopt[ed] the program and which enforce[d] it with penal sanctions, in the execution of a governmental policy."⁹ Thus,

6. 317 U.S. at 346.

7. *Id.* at 352.

8. *Id.*

9. *Id.*

in *Parker* the exemption rested on the fact that the state as sovereign was the primary decisionmaker in the implementation of the anticompetitive program.

After *Parker* was decided in 1943, the Supreme Court did not reexamine the state action exemption doctrine until the 1951 case of *Schwegmann Bros. v. Calvert Corp.*¹⁰ In that case the Court again emphasized the necessity for the state to be the prime mover in the anticompetitive program. In *Schwegmann* the plaintiff challenged a state fair trade law which required retailers to comply with private resale price maintenance agreements for trademarked commodities, even though they were not parties to the agreement. The Court held that state authorization of a price fixing agreement does not give it immunity from antitrust liability under the *Parker* rationale.¹¹ According to the Court, "when a state compels retailers to follow a parallel price policy, it demands private conduct which the Sherman Act forbids."¹² This holding was based on the statement in *Parker* that a state cannot immunize the anticompetitive conduct of private parties.¹³ Thus, the *Schwegmann* Court characterized the retailer's price fixing agreement as private action, but made no real attempt to distinguish it from the raisin marketing plan in *Parker*. Both cases involved a blend of public and private action, but *Schwegmann* failed to give an adequate rationale for the different outcomes in the two cases.

The Court's most recent treatment of the state action exemption prior to *Cantor* was *Goldfarb v. Virginia State Bar*,¹⁴ in which it again applied the Sherman Act in spite of an attempt to invoke the *Parker* exemption. The plaintiffs in *Goldfarb* challenged the minimum fee schedules for attorneys' services which the local bar claimed were "prompted" by the state bar, a state agency by law.¹⁵ According to the Court, the

10. 341 U.S. 384 (1951).

11. Some writers have suggested that the *Parker* rationale was modified by the *Schwegmann* ruling. See Donnem, *Federal Antitrust Law Versus Anticompetitive State Regulation*, 39 ANTITRUST L.J. 950, 960 (1970).

12. 341 U.S. at 389.

13. 317 U.S. at 350.

14. 421 U.S. 773 (1975). For a complete discussion of the effect of *Goldfarb* on the *Parker* doctrine, see Tyler, *Goldfarb v. Virginia State Bar: The Professions are Subject to the Sherman Act*, 41 MO. L. REV. 1 (1976).

15. VA. CODE § 54-49 (1974) provides:

ORGANIZATION AND GOVERNMENT OF VIRGINIA STATE BAR. — The Supreme Court of Appeals may, from time to time, prescribe, adopt, promulgate and amend

“threshold inquiry” in determining whether the *Parker* state action exemption applies is “whether the activity is required by the State acting as sovereign.”¹⁶ This threshold inquiry resolved the case because the State of Virginia through its supreme court rules did not require the minimum fee schedules of either the local or state bar. *Goldfarb* interpreted *Parker* to mean that “[i]t is not enough that . . . anticompetitive conduct is ‘prompted’ by state action; rather, anticompetitive activities must be compelled by direction of the State acting as a sovereign.”¹⁷

Thus, in over three decades, the Supreme Court only twice sought to clarify the *Parker* doctrine. The simple fact that the *Cantor* decision comes less than two years after the previous state action exemption case in itself suggests a new attitude by the Court toward the *Parker* doctrine. Both of the earlier cases emphasized the limiting language of *Parker* that “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”¹⁸ However, *Cantor* went much further than either *Schwegmann* or *Goldfarb* in narrowing the *Parker* exemption. The language in *Cantor* suggests that a doctrine which has seemed immune to Supreme Court scrutiny is now likely to be further circumscribed by that Court. The Court has begun to limit the doctrine by a case-by-case adjudication of specific factual situations.

This case-by-case approach to the state action exemption is expressly called for in *Cantor*. The plurality explicitly rejected any attempt to fashion “a rule which would govern . . . in all future cases presenting state action issues”¹⁹ The *Cantor* Court’s methodology was to view several of the facts in *Parker* as essential to the *Parker* rule. Thus, these facts must now be found in any case claiming the state action exemption.

rules and regulations organizing and governing the association known as the Virginia State Bar, composed of the attorneys at law of this State, to act as an administrative agency of the Court for the purpose of investigating and reporting the violation of such rules and regulations as are adopted by the Court under this article to a court of competent jurisdiction for such proceedings as may be necessary, and requiring all persons practicing law in this State to be members thereof in good standing.

16. 421 U.S. at 790 (1974).

17. *Id.* at 791.

18. 317 U.S. at 351.

19. 96 S. Ct. at 3123.

According to the Court, one of the distinguishing facts of *Parker* was the identity of the defendants. *Parker* involved official action taken by state officials, while the only defendant in *Cantor* was a private utility company. By making this distinction, the plurality necessarily implied that the raisin producers in *Parker* would not have been protected from antitrust suit. The Court stated that “[w]hat sort of charge might have been made against the various private persons who engaged in a variety of different activities implementing that program is unknown and unknowable because no such charges were made.”²⁰ Thus, *Parker* was interpreted as a shield for the state officials only. This language in *Cantor* precludes an interpretation of the state action exemption which would protect the entire state program from antitrust scrutiny.²¹ Yet, many state regulatory systems depend at least partially on the participation of private parties. Under *Cantor* these private parties are now subject to antitrust liability and thus may be less willing to participate in the state program.

Moreover, the plurality’s interpretation of *Parker* was illogical. That decision protects a state agricultural program by insulating the public officials from antitrust liability. But according to *Cantor*, this protection of the public officials would not also protect the program. The plaintiff could still have destroyed the state program using another route, by suing the raisin producers for their part in the program. This tactic effectively would have ended the participation of the producers in the raisin marketing program. Since the producers’ participation was essential to the program, the state’s regulation of raisin production would have failed as a result. If the identity of the defendants in *Parker* was determinative, as the *Cantor* court held, *Parker* offered very little real protection for state action.²²

The second factual distinction relied on by the *Cantor* Court was the dominance of the private party in the decision-making process. In *Parker* the primary decisionmaker was the state agency, while in *Cantor* the state action amounted to “little more than approval of a private proposal.”²³ This dis-

20. *Id.* at 3122.

21. *Id.* at 3120.

22. The dissent contended that the plurality has thus “trivialized [*Parker*] to the point of overruling it.” *Id.* at 3129.

23. *Id.* at 3123.

tion led the plurality to conclude that it would not be unfair to subject the Detroit Edison Company to antitrust suit for its lamp exchange program.²⁴ The Court recognized that in some cases imposing liability on the private party would be unfair, but it did not allow this concern to blossom into an umbrella of state action protection for any private interest group adept at manipulating state agencies or legislatures to approve their anticompetitive programs.

This manipulation of state agencies and legislatures by private parties is further discouraged by *Cantor* because the Court refused to apply the *Noerr* doctrine²⁵ as well as the *Parker* rule. *Eastern Railroad Presidents Conference v. Noerr Motor Freight, Inc.*²⁶ held that the concerted lobbying activities of the railroad defendants to oppose legislation desired by the plaintiffs was not prohibited by the Sherman Act. The rationale of the *Noerr* doctrine is that antitrust considerations are outweighed by the first amendment right to petition the government for redress of grievances and by the desirability of public participation in government, even when that participation is to promote private interests. However, in *California Motor Transport Co. v. Trucking Unlimited*²⁷ the Court made clear that a "sham" participation in governmental processes will not be protected by the *Noerr* doctrine. *Cantor* further clarified the availability of the *Noerr* doctrine by holding that its protection is limited to private petitioning to affect actions of state governments. *Parker* thus protects the resulting state action from antitrust scrutiny, but neither case offers protection when the state merely authorizes private action rather than acting itself.

The dissenting opinion in *Cantor* contended that the *Noerr* doctrine should be applied to the case.²⁸ Justice Stewart viewed the lamp exchange program as a two-step process. First, a pri-

24. Compare the dissenting view:

This attempt to distinguish between the exemptive force of mandatory state rules adopted at the behest of private parties and those adopted pursuant to the State's unilateral decision is flatly inconsistent with the rationale of *Noerr*.

Id. at 3134.

25. *Eastern R.R. Presidents Conference v. Noerr Motor Freight, Inc.*, 365 U.S. 127 (1961). For an analysis of the relationship between *Noerr* and *Parker*, see Handler, *Twenty-Fourth Annual Antitrust Review*, 72 COLUM. L. REV. 419 (1972).

26. 365 U.S. 127 (1961).

27. 404 U.S. 508 (1972); *accord*, *Otter Tail Power Co. v. United States*, 410 U.S. 366 (1973).

28. 96 S. Ct. at 3133.

vate party proposes a tariff. This action is protected by the *Noerr* doctrine. Once the state approved the proposal, the state compelled the private party to engage in anticompetitive conduct in obedience to law. This activity should be protected by *Parker*, as interpreted by *Goldfarb*.

The plurality rejected the dissent's argument that the *Noerr* doctrine was relevant to the *Cantor* case. According to the Court, *Noerr* "did not involve any question of either liability or exemption for private action taken in compliance with state law."²⁹ In other words, the Detroit Edison Company could safely petition the state legislature to adopt a tariff which included a lamp exchange program. But the *Noerr* protection would then have no effect on a later suit against the company when it complied with the tariff it successfully petitioned for.

Although the *Cantor* plurality refused to apply the *Noerr* doctrine to a state action situation, it did apply another theory. According to the Court, "the standards for ascertaining the existence and scope of [the *Parker*] exemption surely must be at least as severe as those applied to federal regulatory legislation."³⁰ This reasoning led the Court to conclude that the long line of cases³¹ which have established an immunity from antitrust liability for federal regulatory legislation in conflict with the prohibitions of the Sherman Act can now be applied by analogy to state action cases. The standard adopted by *Cantor* from the federal immunity cases is that the regulatory activity is exempt only to the extent necessary to protect the achievement of the aims of the particular legislation.³² This rationale offers a more flexible test for state action exemption. Under the federal implied immunity decisions there can be a total exemption, a partial exemption, or no exemption at all.³³ Accordingly, the *Cantor* Court found only a partial exemption for the action of the Detroit Edison Company. The rate setting was ruled valid only insofar as prices are set for the electric power and

29. *Id.* at 3122.

30. *Id.* at 3120.

31. *Gorden v. New York Stock Exchange*, 422 U.S. 659 (1975); *United States v. National Ass'n of Securities Dealers*, 422 U.S. 694 (1975); *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321 (1963); *United States v. Borden Co.*, 308 U.S. 188 (1939).

32. Authorities cited *supra* note 31. See also *Silver v. New York Stock Exchange*, 373 U.S. 341 (1963).

33. In the implied federal immunity decisions the Court found either a total exemption, partial exemption, or no exemption at all. See *Handler, Twenty-Fourth Annual Antitrust Review*, 72 COLUM. L. REV. 1, 14 (1972).

not for the bulbs. Using the same rationale, state regulation of insurance companies, professionals or tradesmen may in the future be held only partially exempt from antitrust scrutiny.

The *Cantor* Court not only added flexibility to the *Parker* doctrine, but it also squarely faced the difficult substantive issues involved. The most important question in a *Parker* situation is whether the state and federal policies actually conflict. The policies of the two sovereigns were in direct conflict in the *Parker* case. The agricultural marketing program was governmental regulation, the very purpose of which was to avoid the consequences of unrestrained competition in the raisin industry, an essential industry to the economy of California. The state regulation of public utilities in *Cantor* presents no similar conflict between state economic policy and federal antitrust policy. Consequently, the application of the antitrust laws to the lamp exchange program does not impair the state's interest in regulating the distribution of electricity. The Court held that the *Parker* rationale does not apply because "[t]he mere possibility of conflict between state regulation and federal antitrust policy is an insufficient basis for implying an exemption from the federal antitrust laws."³⁴

Even though the Court found no conflict between state and federal policy in *Cantor*, it stated further that "even assuming inconsistency [between state and federal policy] we could not accept the view that the federal interest must inevitably be subordinated to the State's."³⁵ Thus, the plurality did not proceed to specify when the state policy promoting the anticompetitive behavior would prevail. However, Justice Blackmun, concurring, advocated a special rule of reason:³⁶ antitrust scrutiny should be less strict when the state has sanctioned the particular anticompetitive activity. This diluted rule of reason would allow more factors to figure in the calculus of harm and benefit than does the classic rule of reason analysis. Factors such as the state's concern for health and safety or the importance of substituting the state itself for the forces of competi-

34. 96 S. Ct. at 3120.

35. *Id.* at 3119.

36. *Id.* at 3126. The traditional "rule of reason" in antitrust cases provides that only unreasonable restraints are unlawful under the Sherman Act. This rule allows a defendant to justify anticompetitive behavior by showing that its benefits outweigh its harms. See *Standard Oil Co. v. United States*, 221 U.S. 1 (1911).

tion, would tend to make the activity permissible, in spite of its anticompetitive effect.

Justice Blackmun actually advocated a substantive economic review of the state action.³⁷ His analysis is a type of judicial review not dissimilar to that engaged in by the Supreme Court in the 1930's to interpret the due process clause.³⁸ Just as in the 1930's, a federal judiciary of "nine old men" would now be substituting its economic judgment for that of the state legislators. Concededly, in any antitrust case, the courts must exercise some degree of economic judgment. However, under the traditional rule of reason cases, these economic judgments are not applied in the context of conflicting state legislation. In cases involving state action, any judicial holding that the anticompetitive behavior is sufficiently unreasonable to justify antitrust liability will necessarily impinge upon the sovereignty of the states and the functions of their legislators in our federalist system. Thus, Justice Blackmun's proposal for the application of a special rule of reason to state action presents the most innovative approach. In any event, his proposals are unlikely to be followed because a plurality of the Court has indicated a contrary approach toward the limitation of the *Parker* doctrine.

The plurality decision suggests that the Court will not use substantive economic evaluations of state programs to limit the *Parker* doctrine. Instead, the Court has intimated its preference for a procedural review of state economic regulation. This review would evaluate the nature of decision-making procedure within the state regulatory scheme. If the state is in fact actively making and implementing the decision, then the *Parker* umbrella of protection will cover the anticompetitive program.

The *Cantor* approach of scrutinizing the decision-making process could be improved by including procedural due process protections for those affected by the anticompetitive state regulation. The *Cantor* Court established that the federal antitrust immunity cases apply by analogy to state action exemption cases.³⁹ The federal immunity cases have developed a rule

37. An elaborate argument in favor of the substantive evaluation of state anticompetitive regulations can be found in Slater, *Antitrust and Governmental Action: A Formula for Narrowing Parker v. Brown*, 69 Nw. U. L. Rev. 71 (1974).

38. See generally Verkuil, *State Action, Due Process and Antitrust: Reflections on Parker v. Brown*, 75 COLUM. L. REV. 328 (1975).

39. 96 S. Ct. at 3120.

that federal regulatory statutes lose their immunity from anti-trust scrutiny when the acts fail to provide a mechanism to safeguard the public interest.⁴⁰ If significant individual rights are infringed, then those affected must be offered an opportunity for a hearing which comports with due process. The application of this rule to the state exemption cases would offer strong protection to the consumer against special interest legislation that is passed and then conveniently forgotten.

When the *Cantor* Court held that state action exemption should not be more broadly applied than federal immunity doctrine, the first step was taken toward applying the due process requirements of the federal immunity cases to the state exemption cases. It is unfortunate that a standard which would treat equally both state and federal action which conflicts with the antitrust law was not adopted at this point.

However, full parity of treatment for similarly competitive state and federal laws may not be the fruits of *Cantor*. The decision contains some troublesome indications that the Court is prepared to subject state regulation to a stricter scrutiny than federal regulation. First, the Court refused to decide what course should be taken when state policies conflict with the policies of the antitrust law. However, the entire decision intimated a negative view toward anticompetitive state regulations.⁴¹ Secondly, the Court indicated that the private parties in *Parker* were probably not immune to antitrust suit. Since most state economic regulation depends to some extent upon the participation of private parties, *Cantor* has transformed the *Parker* doctrine into a meaningless gesture of respect rather than an actual protection for state programs.

The weakness of the *Cantor* decision is considerable. *Parker* is virtually overruled by the Court's focus on the identity of the defendants and the nature of the state program. In addition, crucial questions concerning the treatment of conflicting state and federal policies have been deferred for later adjudication. Nevertheless, the *Cantor* decision can be praised for finally beginning to define a doctrine that for over three

40. See, e.g., *Otter Tail Power Co. v. United States*, 410 U.S. 366 (1973).

41. "The Court has consistently refused to find that regulation gave rise to an implied exemption without prior determining that exemption was necessary in order to make the regulatory act work, and even then only to the minimum extent necessary." 96 S. Ct. at 3120.

decades has troubled lower courts and has fostered a growing trend toward anticompetitive state-sanctioned economic regulation.⁴² That further definition of the state action exemption is sorely needed is evidenced by the inconsistent application⁴³ of the *Parker* exemption to the expanding state regulation of the economy in such areas as insurance, agriculture, public utilities, trades, businesses, and professions.⁴⁴ *Cantor* holds implications for all of these state regulated activities.⁴⁵ The decision promises a case-by-case delimitation of the scope of the *Parker* doctrine and should immediately signal lower courts to apply more conservatively the state action exemption. *Parker's* umbrella of protection for state economic regulation is beginning to close.

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42. See generally Verkuil, *State Action, Due Process and Antitrust: Reflections on Parker v. Brown*, 75 COLUM. L. REV. 328 (1975).

43. See, e.g., Posner, *The Proper Relationship Between State Regulation and the Federal Antitrust Laws*, 49 N.Y.U. L. REV. 693 (1974). Comment, 84 YALE L.J. 1164 (1975).

44. For a discussion of the recent trend toward increased state anticompetitive regulations, see Verkuil, *State Action, Due Process, and Antitrust: Reflections on Parker v. Brown*, 75 COLUM. L. REV. 328 (1975).

45. The effects of *Cantor* have already been felt in Wisconsin. There has been a re-evaluation of the state regulation of professionals. As a result, a legislative committee has endorsed a constitutional amendment transferring the power to regulate lawyers from the state supreme court to the legislature. It is further proposed that a new occupational licensing board be created which would assume the regulatory powers now held by boards consisting of members of the occupation being regulated. These proposals would make the state more prominent in the decision-making process, and any anticompetitive activity less subject to antitrust attack under the *Cantor* standard.