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GOVERNMENT SUPERVISED SELF-REGULATION IN THE SECURITIES INDUSTRY AND THE ANTITRUST LAWS: SUGGESTIONS FOR AN ACCOMMODATION

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The oversight mechanism in the securities industry is one of supervised self-regulation. A government agency, the Securities and Exchange Commission (SEC), oversees industry self-regulatory organizations that have statutorily recognized powers to regulate their members. After describing this system's development, Professor Smythe examines the antitrust laws' application to the regulatory scheme. In particular, she considers how courts and the Congress have dealt with questions of antitrust immunity, anticompetitive conduct, and the jurisdiction of the SEC to deal with antitrust matters. She synthesizes a framework for considering these questions in the securities industry, and concludes that the accommodation with the antitrust laws reached in the securities industry may offer a model and a justification for using a system of supervised self-regulation in other industries.

Most federal regulation of private conduct is done directly by the government through administrative agencies. The number of these congressionally created agencies has become so large, and their activities so intrusive into the lives of the citizenry, that in recent years serious questions have arisen about the continued usefulness of this large regulatory apparatus. The federal government's regulatory efforts have been criticized as overbroad and insensitive to specific problems. The current popular solution to the problem of clumsy governmental regulation is *deregulation*.

Another alternative to regulation by the government is organized self-regulation by the private sector. Self-regulation by industrial and professional organizations offers certain advantages over direct governmental regulation. First, the cost of self-regulation is largely underwritten by those being regulated, rather than by the general public through taxation.¹ Second, since self-regulation is undertaken by members of the affected industry or profession, it is arguably more sensitive to the true regulatory needs of the regulated community than is governmental regulation. Consequently, the regulated community is less likely to impose, ostensibly in the public interest, restraints that are

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1. Of course, some members of the public ultimately underwrite the budgets of self-regulatory organizations. Dues are assessed to members of such organizations the cost of which is then passed on to the public. Ultimately, the consumers or users of the regulated product pay for the cost of self-regulation. See *infra* note 10.

overbroad and unnecessary to achieve the objective of the regulatory scheme.²

Leaving the task of important regulation entirely to self-regulatory groups has notable disadvantages, however. Self-regulatory organizations may be less interested in regulation designed to protect the general public than in regulation crafted to restrict competition and reinforce the dominance of the powerful members of the regulated group. Furthermore, if the regulations crafted by such organizations are to have any teeth, they must have the force of law, rather than being mere voluntary standards. Yet the delegation to private economic groups of significant legislative and disciplinary authority over group members runs counter to our system of representative government,³ and, if not restricted in some way, may be an unconstitutional delegation of legislative power.⁴

An alternative to either direct governmental regulation or "pure" self-regulation is a two-tiered scheme of regulation in which a governmental regulatory agency, created by legislation, oversees the workings of self-regulatory organizations that have statutorily recognized powers to regulate their members. In one major industry in this country, the securities and commodity futures industry, such government supervised self-regulation through recognized self-regulatory organizations is the principal mode of regulation.⁵ This statuto-

2. Most people in business, if given the choice between regulation and no regulation, would probably prefer no regulation at all. If faced with a choice of self-regulation or governmental regulation, however, most people probably would prefer a self-regulatory body to a government body. Of course, reasonable people do differ on this point. See, e.g., testimony of Frank Dunne, President, New York Security Dealers' Association before the Senate in the hearings that preceded passage of a statute that enhanced government supervised self-regulation in the securities industry, the Maloney Act, ch. 677, 52 Stat. 1070 (1938) (codified as amended at 15 U.S.C. § 78o-3 (1982)):

[T]here will be no rush for dealers to join up. It has been our experience that the dealers will set up all sorts of reasons for not joining self-regulating associations. In the first place, the majority of dealers do not like what is really self-regulation; secondly, they do not like the expense of it; third, they like to see the other fellow do the job for them.

Regulation of Over-the-Counter Markets, Hearings Before the Senate Comm. on Banking and Commerce, 75th Cong., 3d Sess. 40 (1938) [hereinafter cited as *Senate-Maloney Act Hearings*]. The next two witnesses in the hearings, A.W. Snyder, a broker-dealer from Houston, and Virgil C. McGorrell, a representative of the Maine Investment Dealers Association, believed otherwise. *Id.* at 44-47. See also, Levin, *The Limits of Self-Regulation*, 67 COLUM. L. REV. 603, 639 (1967) (noting that a 1963 proposal to establish a government supervised self-regulatory organization in the broadcast industry was given a cool reception by members of the industry).

3. See Jaffe, *Law Making by Private Groups*, 51 HARV. L. REV. 201 (1937). Professor Jaffe notes that the only recognized political entity is the citizen, and the only recognized group "is the organization of citizens territorially." *Id.*

4. See *A.L.A. Schechter Poultry Corp. v. United States*, 295 U.S. 495 (1935).

5. The securities industry's self-regulatory organizations are supervised by the Securities and Exchange Commission (SEC), established pursuant to § 4 of the Securities and Exchange Act of 1934 (the Exchange Act), ch. 404, 48 Stat. 882 (codified as amended at 15 U.S.C. § 78d (1982)). The commodity futures industry's self-regulatory organizations are supervised by the Commodity Futures Trading Commission (CFTC), established pursuant to the Commodity Futures Trading Commission Act of 1974, Pub. L. No. 93-463, 88 Stat. 1389 (codified as amended as part of the Commodity Exchange Act at 7 U.S.C. §§ 1-24 (1976 & Supp. V 1981)). The CFTC is the successor to the Commodity Exchange Commission, which was part of the Department of Agriculture. Hereafter, unless otherwise stated, the securities and commodity futures industry will be referred to collectively as the securities industry, and their respective federal and self-regulatory overseers will be described generally as securities industry regulators and self-regulators.

rily approved self-regulatory structure has been characterized as "unique,"⁶ and "curious,"⁷ and "unlike any other system in the world."⁸ Each year the self-regulatory organizations expend significant sums and countless personnel hours on compliance and surveillance work. Because their oversight efforts are necessary to ensure fair and safe financial markets, such a commitment, if not made by the self-regulatory organizations, would have to be made by the government and paid for by the taxpayer from general revenues.⁹ Thus, in terms of dollar savings alone, self-regulation in the securities industry provides significant benefits to the general public.¹⁰ As noted above, self-regulatory systems arguably offer other benefits as well. By placing the primary regulation of an enterprise in the hands of those who best understand the business, the regulations that are established by the self-regulatory organizations should be sensitive to the needs of the business and more carefully crafted than they would be if the government was the sole regulator.¹¹

Congressional acceptance of self-regulation as a valuable means of meeting regulatory needs in the securities industry first occurred fifty years ago, when self-regulatory organizations were included in the initial effort to impose governmental regulation on the securities industry. In 1934 when Congress established the Securities and Exchange Commission (SEC) to regulate the trading of securities, it built into the statutory scheme a considerable degree of self-regulation for the nation's stock exchanges. Subsequent acts of Congress promoted new self-regulatory organizations in the securities and commodity futures industry. In 1938 Congress fostered the creation of additional securities

6. S. REP. NO. 29, 94th Cong., 1st Sess. 22, reprinted in 1975 U.S. CODE CONG. & AD. NEWS 200.

7. N. WOLFSON, R. PHILLIPS & T. RUSSO, REGULATION OF BROKERS, DEALERS AND SECURITIES MARKETS § 12.01 (1977).

8. NYSE, ANNUAL REPORT (1981). The New York Stock Exchange (NYSE) is by far the largest stock exchange in the United States. Stock exchanges provide an actual centralized physical locus for the buying and selling of securities. Some members of the stock exchanges do a retail business (buy from, sell to, and broker for, the public) and also execute transactions on the floor of the exchange with other members. Other exchange members do no business with the public and only transact business on the exchange floor.

9. All the major stock exchanges in this country are self-regulatory organizations registered with the SEC pursuant to § 6 of the Exchange Act, 15 U.S.C. § 78f (1982). The principal exchanges, in addition to the New York Stock Exchange, include the American Stock Exchange (AMEX), the Midwest Stock Exchange, the Pacific Stock Exchange, the Boston Stock Exchange, the Philadelphia Stock Exchange, and the Chicago Board Options Exchange. In addition, one association that includes both exchange and nonexchange members is a statutorily recognized self-regulatory organization. That organization is the National Association of Securities Dealers (NASD), and it is registered with the SEC pursuant to § 15a of the Exchange Act of 1934, 15 U.S.C. § 78o-3 (1982). A similar regulatory structure exists in the commodity futures industry.

10. Of course the cost of self-regulation ultimately is passed through to brokerage firm customers in the form of higher fees, so a lessened burden on the taxpayer is accomplished at the expense of securities industry customers. At least one prominent commentator has stated that self-regulation is more expensive than governmental regulation because of the higher salaries in the private sector. See Jennings, *Self-Regulation in The Securities Industry: The Role of the Securities and Exchange Commission*, 29 LAW & CONTEMP. PROBS. 663, 677 (1964). It is debatable whether the same conclusion would be reached today. The level of salaries for government employees now may exceed those employed by self-regulatory organizations.

11. See Jaffe, *supra* note 3. Professor Jaffe cites as justification for self-regulation both the prospect of better regulations and the probability of greater acceptance of such regulations by those participating in self-governance. *Id.* at 212.

industry self-regulatory organizations to police over-the-counter trading by passing the Maloney Act.¹² Thereafter, only one such organization was formed, the National Association of Securities Dealers (NASD). In 1974 Congress responded to the concern that the increased public participation in commodity futures trading required more pervasive regulation than that provided by the government and commodity futures exchanges. Congress passed legislation¹³ that encouraged the creation of a non-exchange self-regulatory organization to regulate off-exchange trading in commodity futures. In 1980 the Commodity Futures Trading Commission (CFTC) approved the establishment of the National Futures Association (NFA), a non-exchange self-regulatory organization patterned after the NASD.¹⁴

If government supervised self-regulation¹⁵ is regarded as reasonably effective for the securities industry, and if such a system might be effective in other industries as well, why has it not been more widely employed as a complement to direct governmental regulation? One reason may be that acceptance of self-regulation in the securities industry is attributable, at least in part, to historical accident. As discussed below, self-regulation in the securities industry preceded governmental regulation by many years. When the framers of the legislation that created the Securities and Exchange Commission began their task, self-regulatory institutions were already there to be used. Another

12. The Maloney Act, ch. 677, § 1, 52 Stat. 1070 (1938) (codified as amended at 15 U.S.C. § 78o-3 (1982)) (generally known as § 15A of the Act).

13. Commodity Futures Trading Commission Act of 1974, Pub. L. No. 93-463, 88 Stat. 1389 (codified as amended as part of the Commodity Exchange Act at 7 U.S.C. §§ 1-24 (1976 & Supp. V 1981)).

14. Even more recently Congress acted to establish an industry self-regulator in the municipal securities area. Section 15B(b)(1) of the Exchange Act, 15 U.S.C. § 78o-4(b)(1) (1982). Municipal securities are regulated pursuant to a complex self-regulatory package in which the Municipal Securities Rulemaking Board promulgates self-regulatory rules and regulations and disciplines members. Other entities, including bank regulatory agencies and the NASD, inspect the municipal firms for compliance. Currently, the SEC has been promoting a self-regulatory organization for the registered investment companies (*see* 15 SEC. REG. & L. REP. (BNA) No. 6, at 301 (Feb. 11, 1983), and *id.* No. 8, at 410 (Feb. 25, 1983) (reprinting Invest. Co. Rel. No. 1C-13044)) and has encouraged the creation of a self-regulatory apparatus for accounting firms as well. *See* 15 SEC. REG. & L. REP. (BNA) No. 2, at 165-66 (Jan. 14, 1982). In addition, Congress recently amended the Exchange Act to permit the SEC to abandon entirely its direct oversight of broker-dealer firms (SECO firms) and to require that all broker-dealers join a national securities association. Pub. L. No. 98-38, § 3, 97 Stat. 205-07 (1983) (amending sections 15(b)(8) and (9) of the Securities Exchange Act, 15 U.S.C. §§ 78o(b)(8) & (9) (1982)).

15. The term "self-regulation" has been subject, periodically, to etymological assaults. For example, during the hearings on the Maloney Act various commentators took issue with the use of the term "self-regulation" to describe the proposed system. They believed a more accurate term would be "cooperative regulation" because, explained the vice president of one broker-dealer, "[w]e are not trying to go off in a corner by ourselves and make rules whereby we can play; we are working hand and glove with the Securities and Exchange Commission, trying to determine how we can work along the same lines with the same objectives." *Senate-Maloney Act Hearings, supra* note 2, at 60 (statement of Nevil Ford, First Boston Corp.). Throughout the period of securities industry self-regulation that has transpired since the passage of the Exchange Act, renewed efforts have been made to characterize the form of the regulation as "cooperative regulation," but the term "self-regulation" seems to have prevailed in the final result. *See, e.g.,* SUBCOMM. ON SECURITIES OF THE SENATE COMM. ON BANKING, HOUSING AND URBAN AFFAIRS, 93D CONG., 1ST SESS., SECURITIES INDUSTRY STUDY 147 (Comm. Print 1973) [hereinafter cited as SECURITIES INDUSTRY STUDY—1973]. The term used in this Article to describe the phenomenon will be "self-regulation."

reason for the limited use of government supervised self-regulatory systems is considerable suspicion that conflicts of interest would prevent self-regulators from vigorously policing the enterprises that pay their salaries.¹⁶ For those industries—such as the pharmaceutical, chemical, and aviation industries—whose activities touch the fundamental public concerns of health and safety (in contrast to industries like the securities industry, whose impact is mainly financial), the concern is that important efforts at public protection will not be pursued vigorously unless the government directly oversees the regulation of the industries.

Finally, there is reason to fear that self-regulatory efforts are often little more than thinly disguised excuses for anticompetitive conduct. This view is reflected in the many judicial opinions over the past century in which voluntary self-regulatory efforts unrecognized by statute have been struck down as violating federal antitrust laws.¹⁷ The antitrust concern has not been absent from assessments of securities industry self-regulatory conduct either. Yet because securities industry self-regulation started more than one hundred years before passage of the Sherman Antitrust Act,¹⁸ and was given official government recognition at a time when Congress was almost uniquely unconcerned with antitrust dogma,¹⁹ the federal courts have had less freedom than usual to strike down securities industry self-regulatory efforts as violating the antitrust laws.

Nonetheless, the parameters of immunity from the antitrust laws currently enjoyed by the securities industry self-regulatory organizations were not self-evident when the first antitrust challenges against such organizations were made, and the reconciliation of securities industry self-regulation to the antitrust laws has been an ongoing challenge to the courts and to Congress. This Article will focus on the results reached thus far in the securities industry. This Article's thesis is that government supervised self-regulation offers a constructive alternative to direct government regulation on the one hand, and to no regulation on the other. The public suspicion that self-regulatory efforts

16. Indeed, the self-regulatory organizations in the securities industry have not escaped criticism in this regard. For a particularly vigorous denunciation of securities industry self-regulation as failing effectively to guard against unsafe financial practices in the securities industry, see H. BARUCH, *WALL STREET: SECURITY RISK* (1971). See also *Study of the Securities Industry, Hearings Before the Subcomm. on Commerce and Finance of the House Comm. on Interstate and Foreign Commerce*, 92d Cong., 1st Sess. 1639-1651 (1971) (testimony of E. Cellar).

17. *E.g.*, *Fashion Orig. Guild of Am. v. FTC*, 312 U.S. 457 (1941); *Eastern States Retail Lumber Dealers Ass'n v. United States*, 234 U.S. 600 (1914). Trade associations, that is, private (unrecognized by statute and unsupervised by government) organizations of businesses engaged in the same or complementary enterprises, are vulnerable to antitrust attack. As will be discussed in this Article, the significant legal distinctions between such trade associations and organizations like the securities industry's self-regulatory organizations are: (1) the existence of ongoing oversight of the latter groups' activities by a federal agency, and (2) the official inclusion of such self-regulatory organizations in a statutory scheme of regulation.

18. 15 U.S.C. § 1 (1982).

19. The first Congress of the New Deal certainly was more concerned with nurturing industry back to health so it *could* compete, than in checking anticompetitive collective conduct. The National Industrial Recovery Act of June 16, 1933, ch. 90, 48 Stat. 195, embodied a massive relaxation of the antitrust laws. This relaxation was repealed by the 74th Congress, ch. 246, 61 Stat. 208 (1935).

are misdirected toward ensuring economic advantage and disregarding public safety should be lessened by the oversight by a government agency that is charged with ensuring that the self-regulatory activities are in the public interest, and by judicial and congressional oversight of that agency's performance.²⁰ Before discussing the antitrust questions, a brief review of the development of a federally recognized self-regulatory scheme in the securities industry may prove useful to an understanding of the historical context in which the antitrust challenges arose.

I. A BRIEF HISTORY OF THE SECURITIES INDUSTRY'S SELF-REGULATION²¹

A. *The Securities Exchange Act of 1934 (the Exchange Act)*

Self-regulation in the securities industry is nearly as old as the federal government. The Philadelphia Stock Exchange was formed in 1790; the New York Stock Exchange (NYSE) was formed in 1792.²² By the time the country's collective political wisdom determined, in the years following the stock market crash of 1929, that such self-regulation was not adequate to police the industry, a substantial self-regulatory structure had already developed, and was already in place in the securities industry.

The structure, at least on paper, was impressive. In 1934 there were at least twenty-one stock exchanges.²³ By far the largest of these was the New York Stock Exchange, which had an authorized membership of 1,375 as of February, 1929.²⁴ The NYSE was governed by a committee consisting of forty members, plus the president and treasurer of the Exchange.²⁵ Much of the governance was done by committees appointed by the governing committee. These included committees on business conduct, stock list, admission, arrangements, publicity, law, and arbitration. Although, as one witness told Congress, membership in an exchange could be regarded as really just membership in a club,²⁶ the NYSE, at least, was a club with an impressive infrastructure for

20. The focus of this Article is on federally recognized self-regulation and the coexistence of such regulation with the federal antitrust laws. The relationship of the antitrust laws to activities of voluntary self-regulatory organizations or to self-regulatory organizations regulated by state governments is not addressed. Federal courts reviewing state approved anticompetitive activity arguably should not perform the same function they perform when determining whether federally recognized self-regulatory activity is reachable under the antitrust laws. In the latter case the task is to reconcile conflicting federal policies. The former case is one of federal preemption; the federal court must determine the extent to which the federal policy (the antitrust laws) was intended to preempt state approval of private anticompetitive conduct.

21. This discussion is intended to be no more than a brief review of the history of securities industry self-regulation. For more comprehensive treatments, see R. DE BEDTS, *THE NEW DEAL'S SEC* (1964); Jennings, *supra* note 10. See also SECURITIES INDUSTRY STUDY, *supra* note 15.

22. F.I. PHILP, *THE PRINCIPAL STOCK EXCHANGES OF THE WORLD* 4 (Spray, ed. 1964). See also SENATE COMM. ON BANKING AND CURRENCY, REPORT ON STOCK EXCHANGE PRACTICES, S. REP. NO. 1455, 73d Cong., 2d Sess. 77 (1934), which states the NYSE was formed in 1791.

23. See *Stock Exchange Regulation, Hearings on H.R. 7852 & 8720 Before the House Comm. on Interstate and Foreign Commerce*, 73d Cong., 2d Sess. 746 (1934) [hereinafter cited as *House Hearings—1934*].

24. S. REP. NO. 1455, *supra* note 22, at 77.

25. *Id.* at 78.

26. *House Hearings—1934*, *supra* note 23, at 346, (testimony of Michael J. O'Brien, Pres.,

regulating the activities of its members. Since the self-regulatory system of the industry had proven inadequate to deal with the speculative excesses and concerted improper trading practices that preceded the market crash,²⁷ it could not continue unchanged. Nonetheless, the long-standing institutions of self-regulation existed, were still intact, and were forces to be reckoned with in 1934 when Congress undertook to devise a new and, it was hoped, more effective structure for the regulation of the securities markets.

From the outset of the hearings held in connection with the drafting of the bill that became the Exchange Act, Congress assumed that its task included incorporating the existing self-regulatory institutions (*i.e.*, the stock exchanges) into the new regulatory system. The proper relationship between these institutions and a new federal securities regulatory agency was the subject of many weeks of hearings before the House and Senate committees drafting the Exchange Act, but no one seriously questioned that self-regulation by the exchanges would continue to play an important role in the regulation of the industry.²⁸

The regulatory structure crafted for the securities industry in 1934 was more a function of political compromise than of logic. The original form of the Exchange Act²⁹ would have given a newly created federal agency detailed,

Chicago Stock Exchange). He was referring to the Chicago Stock Exchange. The House Committee naturally rejected the "club" concept. "The bill proceeds on the theory that the exchanges are public institutions which the public is invited to use . . . , and are not private clubs to be conducted only in accordance with the interests of their members. The great exchanges of this country . . . are affected with a public interest in the same degree as any other great utility." H.R. REP. NO. 1383, 73d Cong., 2d Sess. 15 (1934).

27. The Senate catalogued these shortcomings in its report on the bill that became, with minor revisions, the Exchange Act: "[T]he attitude of exchange authorities toward the nature and scope of the regulation required appears to be sharply at variance with the modern conception of the extent to which the public welfare must be guarded in financial matters." S. REP. NO. 792, 73d Cong., 2d Sess. 4 (1934). The NYSE officials did not openly admit to sharing the common perception that shortcomings in industry self-governance had been very much responsible for the crash. *See, e.g., House Hearings—1934, supra* note 23, at 169 (testimony of Richard Whitney, President of the NYSE). *See also* F. PECORA, WALL STREET UNDER OATH 258-60 (1939); R. DE BEDTS, *supra* note 21.

28. The 1934 House hearings held in connection with the passage of the Exchange Act commenced on February 14, 1934, and ended on March 24, 1934, generating 941 pages of transcript. *See House Hearings—1934, supra* note 23. The Senate hearings were even more extensive. *See Hearings on S. Res. 84 and S. Res. 56 and 97 Before the Senate Comm. on Banking and Currency, 72d Cong., 1st Sess. (1934)* [hereinafter cited as *Senate Hearings—1934*]. Much discussion centered on the appropriate composition of the federal regulatory agency to be created to oversee the self-regulators. The exchange community in general would have preferred to leave things as they had been, *i.e.*, to have no federal regulator overseeing its work. Since that preference was politically untenable, its most intense effort was to create a hybrid commission in which various prominent members of the federal bureaucracy would serve jointly with nominees from the exchanges. *House Hearings—1934, supra* note 23, at 211-12. After much discussion of this proposal in the House hearings, Chairman Rayburn tersely dismissed the idea as being "far . . . afield . . . from the way we do regulate." *Id.* at 395. The House bill that originally passed, H.R. 9323, 73d Cong., 2d Sess. (1934), would have carved a securities division out of the Federal Trade Commission. The Senate bill, S. 3420, 73d Cong., 2d Sess. (1934), created a new agency, the SEC. The Senate proposal prevailed, and the bill that was signed into law, the Exchange Act, ch. 404, § 1, 48 Stat. 881 (codified as amended at 15 U.S.C. §§ 78a-78kk (1976 & Supp. V. 1981)), created a separate SEC.

29. H.R. 7852, 73d Cong., 2d Sess. (1934); S. 2693, 73d Cong., 2d Sess. (1934). The bill was also known as the Fletcher-Rayburn bill for the chairmen of the Senate (Duncan U. Fletcher of New Jersey) and House (Sam Rayburn of Texas) committees considering the bill.

indeed pervasive, authority to regulate the exchanges, the securities traded on the exchanges, and the issuers of these securities. The degree of regulatory power proposed to be given to this new agency was so extensive that even proponents of a meaningful federal regulatory role thought that the intrusion into the existing self-regulatory system went too far.³⁰ The most influential of these was John Dickinson, Assistant Secretary of Commerce, and Chairman of a committee appointed by Commerce Secretary Daniel C. Roper, at President Roosevelt's request, to study stock-exchange regulation. The report from that study (known generally either as the Roper Report or the Dickinson Report) was instrumental in causing changes in the original bill so that in the bill that ultimately became the Exchange Act the industry self-regulatory power was preserved far more than it had been in the original bill.³¹ In testifying before the House Committee on Interstate and Foreign Commerce, Dickinson outlined what he regarded to be the appropriate balance between self-regulation and government regulation:

The Roper committee report went on the theory that if governmental regulation attempts to do too much directly and to control and intervene directly in the first instance over the whole field which it covers, it is in danger of breaking down under its own weight and proving ineffective. In the report of the Roper committee, therefore, . . . the regulatory functions of [the proposed] governmental agency were [to be] held in reserve and were [to be] employed only to supplement and supervise what in the first instance was self-regulation of the exchanges.³²

Or, as another member of the Roper Committee, Federal Trade Commissioner J. M. Landis, viewed the problem, the "desirable thing . . . is to get as much self-regulation as possible and at the same time preserve the public interest."³³

The regulatory structure established by the Exchange Act imposed over the existing self-regulatory organizations a federal regulatory authority, the Securities and Exchange Commission (SEC). The self-regulatory organizations, however, retained primary authority to regulate their members. The SEC's power to intervene in the affairs of a self-regulatory exchange was lim-

30. Some opponents vehemently expressed unhappiness with the bill. Dean Witter, head of the major West Coast firm, told the Rayburn committee that the original bill "provides for such a comprehensive governmental control of industry as to virtually destroy the initiative and independence of American business." *House Hearings—1934*, *supra* note 23, at 403. See R. DE BEDTS, *supra* note 21, at 65-70 for a recounting of the financial community's campaign against the measure.

31. See, e.g., *House Hearings—1934*, *supra* note 23, at 26-27, (testimony of J.M. Landis). Landis was a member of the Roper Committee, and at the time was also a Commissioner of the Federal Trade Commission. According to Landis, the Roper Report was "built upon the theory of trying to get as much self-regulation as is possible out of the exchanges, permitting the administrative authorities to come in on occasions when that self-regulation fails." *Id.* at 26.

32. *Id.* at 513 (testimony of John Dickinson).

33. *Id.* at 27 (testimony of J.M. Landis). See also *id.* at 340 (testimony of Michael J. O'Brien, Pres., Chicago Stock Exchange: "Legislation should not discourage nor render ineffective the efforts of men who desire honestly to regulate themselves.").

ited by the Act³⁴ to instances in which the exchange had either itself violated the Act, or had failed to enforce compliance with the Act by a member or listed company. In such instances, the SEC was authorized either to suspend or revoke the exchange's registration.³⁵ In certain enumerated instances, and with appropriate procedural requirements, the SEC was also empowered to alter or supplement the rules of an exchange should the exchange fail to do so after having been so requested by the SEC.³⁶

The first of these powers, the power to revoke or suspend, was so drastic as to virtually preclude its use as an effective regulatory tool. Only once in the nearly fifty years of SEC oversight of exchange activity did the SEC use it either to suspend or revoke an exchange's registration.³⁷ Consequently, the primary means by which the SEC has exercised regulatory authority over the exchanges has not been through the formal and disruptive processes of revocation and suspension, but through informal communication, interaction, and persuasion.³⁸ As will be seen below, the informality of this oversight effort later raised serious questions about the degree to which SEC oversight power should shield acts of self-regulatory organizations from the antitrust laws, or, to put the matter another way, raised genuine questions about the pervasiveness of the SEC's regulatory authority over the exchanges.

B. The Maloney Act of 1938³⁹—Creation of the NASD

When the Exchange Act was passed, Congress recognized that an important segment of the securities industry lay outside the purview of the statutorily sanctioned system of industry self-regulation—namely, the broker-dealers in over-the-counter securities (*i.e.*, securities that were not listed on an exchange). Under the original Exchange Act, these over-the-counter broker-dealers were subjected to direct regulation by the SEC. Almost immediately after passage of the Exchange Act, however, it became apparent that the task

34. Securities Exchange Act of 1934, ch. 404, § 1, 48 Stat. 881 (1934) (codified as amended at 15 U.S.C. §§ 78a-78kk (1976 & Supp. V 1981)).

35. *Id.* § 19(a)(1) (codified as amended at 15 U.S.C. § 78s(h) (repealed 1975)).

36. *Id.* § 19(b) (codified as amended at 15 U.S.C. § 78s(c) (repealed 1975)).

37. *See In re San Francisco Mining Exchange*, 42 SEC Decisions & Reps. 1004 (April 22, 1966).

38. One of the first clear indications that persuasion, not compulsion, would characterize the SEC-exchange relationship came in 1935 in connection with the SEC's report on exchange governance. In that report, reprinted by the House of Representatives as *REPORT ON THE GOVERNMENT OF SECURITIES EXCHANGES*, H.R. DOC. NO. 85, 74th Cong., 1st Sess. (1935), the SEC, after recommending important changes in the exchanges' governmental structure, stated:

The Commission does not now suggest that legislation be enacted to bring about these recommendations. Its recommendations can be put into effect by the voluntary action of the exchanges themselves without resort to legislation. It hopes that, in the main, these recommendations will be found acceptable and put into effect by the exchanges themselves.

Id. at 17. Nearly forty years later the informal method of oversight practiced by the SEC came under severe criticism in Congress. *See S. REP. NO. 1455, supra* note 22, at 201-04.

39. The Maloney Act, ch. 677, 52 Stat. 1070 (1938) (codified as amended at 15 U.S.C. § 78o-3 (1982)) (generally known as § 15A of the Exchange Act). Senator Francis T. Maloney of Connecticut was the principal sponsor of the legislation.

of directly regulating the over-the-counter market was too burdensome for the SEC. The SEC sponsored extensive conferences with representatives of the over-the-counter broker-dealer community to explore the creation of self-regulatory organizations in the over-the-counter market.⁴⁰ By 1936 an organization called the Investment Bankers Conference had been created,⁴¹ as well as other similar organizations of over-the-counter broker-dealers.⁴² These organizations joined the SEC in advocating to Congress that the Exchange Act be amended to foster the creation of a statutorily sanctioned industry self-regulatory organization to provide for regulation of over-the-counter broker-dealers in a manner similar to that provided by the exchanges for their members. In 1937 Senator Maloney of Connecticut introduced a bill to give effect to that proposal.

The legislative hearings and reports on the bill are surprisingly sparse of comment on the unusual nature of such legislation.⁴³ In introducing the bill, Senator Maloney noted that the "problem" of regulating the markets could be met by "two alternative programs," the more traditional regulation-by-government approach or a scheme of "cooperative regulation in which the task [of regulation would] . . . be largely performed by representative organizations of investment bankers, dealers, and brokers, with the Government exercising appropriate supervision in the public interest, and exercising supplementary powers of direct regulation."⁴⁴ The hearings preceding passage of the Maloney Act devoted considerable discussion to the degree to which the SEC would be authorized to intervene in the self-regulatory activities of the new organiza-

40. See REGULATION OF OVER-THE-COUNTER MARKETS, S. REP. NO. 1455, 75th Cong., 3d Sess. 4-5 (1938).

41. *Id.* at 5. The Conference was formed following the Supreme Court's decision in 1936 declaring the self-governing features of the National Industrial Recovery Act (NRA) unconstitutional. *A.L.A. Schechter Poultry Corp. v. United States*, 295 U.S. 495 (1935). Before the *Schechter* decision, a trade association of over-the-counter broker-dealers known as the Investment Bankers Association had drafted an industry code of practice. Following *Schechter*, the Investment Bankers Conference was formed, with the encouragement of the SEC, to work with the SEC in developing legislation to give congressional sanction to industry self-governance in a manner that would avoid the prohibitions of *Schechter*. See *Senate-Maloney Act Hearings*, *supra* note 2, at 36-37 (testimony of B. Howell Griswold, Jr., Chairman, Investment Bankers Conference). According to Griswold, the conference in 1938 had twenty-one members of the Board of Governors, fourteen district governing committees, and about 1,700 members. *Id.* at 37-38.

42. *E.g.*, the New York Security Dealers Association. See *Senate-Maloney Act Hearings*, *supra* note 2, at 40.

43. A few commentators did recognize the radical nature of the legislation. Representative Boren of Oklahoma, while not criticizing the concept, nonetheless observed that the creation of a private organization with substantial power to regulate its members "strikes at the fundamentals of our American philosophy of government . . ." *Regulation of Over-the-Counter Markets, 1938: Hearings on S. 3255, H.R. 9634 Before a Subcomm. of the House Comm. on Interstate and Foreign Commerce*, 75th Cong., 3d Sess. 15 (1938) [hereinafter cited as *House Hearings—1938*]. Similarly, inserted into the record of the Senate hearings was an editorial from the February 2, 1938 edition of *The Daily Bond Buyer* in which the fear was expressed that the scheme of regulation established by the Maloney Act, if carried to other industries, would "bring about by gradual usurpations of power the fascistic principle of the corporate State." *Senate-Maloney Act Hearings*, *supra* note 2, at 121. Except for these apocryphal comments, there was little mention in Congress of the unusual regulatory program created by the Bill, and there was virtually no thoughtful analysis.

44. S. REP. NO. 1455, *supra* note 40, at 3-4.

tion, but almost no one questioned the propriety of delegating primary regulatory authority over a segment of an industry to a private organization.

The bill as enacted explained the choice of self-regulation over direct governmental regulation largely in negative terms. Governmental regulation, Congress believed,

would involve a pronounced expansion of the organization of the Securities and Exchange Commission; the multiplication of branch offices; a large increase in the expenditure of public funds; an increase in the problem of avoiding the evils of bureaucracy; and a minute, detailed, and rigid regulation of business conduct by law.⁴⁵

Self-regulation, presumably, would avoid these evils, and would effectively regulate business conduct provided that the government stood as watchman, "exercising appropriate supervision in the public interest . . ."⁴⁶

C. *Self-Regulation since 1938*

For nearly twenty years after the passage of the Maloney Act, the systems of self-regulation created in that Act and in the original Exchange Act of 1934 remained virtually intact, with little occurring to cause notice by either the courts or Congress. During that period the exchanges and the NASD proceeded to regulate, govern, and discipline their members with very little interference from the SEC. Starting in the late 1950s, allegations of widespread fraudulent practices in the securities industry led Congress to pass, in 1961, an amendment to the Exchange Act that directed the SEC to conduct an extensive "special study" of the securities markets.⁴⁷ The problems related primarily to an increase in manipulative and other improper trading practices and caused an explosion of investigations by the SEC that led to numerous proceedings against members of the brokerage community.⁴⁸ From April to August 1963, the Commission transmitted its report to Congress. The five volume "Special Study of the Securities Markets"⁴⁹ was an extensive review of the condition of the securities industry and the performance of the self-regulatory organizations. Transmittal of the report to Congress was accompanied by extensive hearings⁵⁰ and resulted in the introduction of some important legisla-

45. *Id.* at 3.

46. *Id.* at 4.

47. Pub. L. No. 87-196, 75 Stat. 465 (1961), amended the Exchange Act to add § 19(d). That section as then amended authorized and directed the Commission to conduct a study of the rules of the securities markets to determine if amendments were necessary for the protection of investors. The deadline was first set at Jan. 3, 1963, but was later extended to April 3, 1963, by Pub. L. No. 87-561, 76 Stat. 247 (1962).

48. See generally H.R. REP. NO. 882, 87th Cong., 1st Sess. 2-4 (1961), reprinted in 1978 U.S. CODE CONG. & AD. NEWS 2257, 2257-59.

49. REPORT OF SPECIAL STUDY OF SECURITIES MARKETS OF THE SECURITIES AND EXCHANGE COMMISSION, H.R. DOC. NO. 95, Pts. 1-5, 88th Cong., 1st Sess. (1963). The "special study" was not the first study of the securities markets undertaken by the Commission, but it was, and remains, the most extensive.

50. See, e.g., *Investor Protection, Parts 1 and 2: Hearings Before the Subcomm. on Commerce and Finance of the House Comm. on Interstate and Foreign Commerce*, 88th Cong., 1st & 2d Sess. 1 (1963-64); *SEC Legislation: Hearings Before the Subcomm. on Securities of the Senate Comm. on Banking and Currency*, 88th Cong., 1st Sess. 1 (1963).

tion.⁵¹ Yet to the extent that the special study and the proposed legislation considered the quality and efficacy of self-regulation, it generally did so favorably.⁵² Indeed, the proposed changes to the system were in the direction of an increased, not a decreased, role for the self-regulatory organizations.⁵³

In the years 1968 to 1970, however, a real crisis overcame the securities industry. An enormous increase occurred in the volume of securities traded, an increase that caught many brokerage firms with inadequate personnel or equipment to deal with the voluminous paperwork attendant upon such large-scale trading. Unable to trace trades, or to identify debt and credit obligations, several large brokerage houses became insolvent.⁵⁴ The self-regulatory

51. Securities Acts Amendments of 1964, Pub. L. No. 88-467, 78 Stat. 565 (codified as amended in scattered sections of 15 U.S.C.).

52. The letter of transmittal from the Commission to Congress contained numerous favorable comments about self-regulation. Letter of Transmittal (August 8, 1963), reprinted in *Investor Protection Parts 1 and 2: Hearings Before the Subcomm. on Commerce and Finance of the House Comm. on Interstate and Foreign Commerce*, 88th Cong., 1st Sess. 37 (1963) [hereinafter *Special Study House Hearings*]. For example, the Commission endorsed the special study's conclusion that "the 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." *Id.* at 37. Similarly, "[r]eliance on self-regulation rests on two principal premises: First, self-regulation provides an alternative to more pervasive direct control by Government, which would be expensive to the taxpayers and burdensome to the industry. Second, it can be a more sensitive means for developing high standards of business conduct." *Id.* at 101-02. For testimony to the same effect, see *id.* at 1216-17 (testimony of William L. Cary, Chairman, SEC).

53. The major changes proposed by the Commission were: (1) requiring that broker-dealers belong to at least one registered self-regulatory organization; (2) raising the general qualifications for securities industry professionals; (3) placing an affirmative requirement on broker-dealers to supervise their employees and making their failure to do so a basis for disciplinary action; and (4) increasing the grounds for disqualifying broker-dealers in circumstances involving financial misconduct. *Id.* at 104-05. Much opposition was engendered regarding the proposal to make membership in a self-regulatory organization mandatory, and in the end it was dropped. The other proposals listed above were generally enacted as various amendments to the Exchange Act. See, e.g., Pub. L. No. 88-467 §§ 6(b), 7(a)(4), 78 Stat. 565, 570-73, 575-76 (1964). For a discussion of the Amendments, see SECURITIES ACTS AMENDMENTS OF 1964, H.R. REP. NO. 1418, 88th Cong., 2d Sess. 1, reprinted in 1964 U.S. CODE CONG. & AD. NEWS 3013. The chief opponents of compulsory membership raised the argument that compelling private business to submit to the control of private regulation was unconstitutional as a violation of the delegation doctrine and, moreover, was simply unfair. For example, Carl L. Shipley, a private practitioner in Washington, D.C., suggested that not only would the Supreme Court's decisions in *Schechter Poultry*, 295 U.S. 495 (1935), and *Carter Coal*, 298 U.S. 238 (1936), be violated if membership were made compulsory but that the impulse to enhance the power of the self-regulatory organizations "closely approaches the kind of corporate state that was developed by Mussolini in Italy." *Special Study House Hearings*, *supra* note 52, at 778, 797. The Commission countered these arguments by insisting that "extensive Commission oversight" would cure any constitutional problems concerning improper delegation. The question of the government compelling membership in a self-regulatory organization is again alive in connection with the makeup of the National Futures Association (NFA). The NFA has recently asked the Commodity Futures Trading Commission to promulgate a rule requiring all off-exchange future commission merchants to join the NFA. See Petition for Commission Rulemaking; Registered Futures Associations, 47 Fed. Reg. 53,031 (1982). The Justice Department is opposing the proposal. See SECURITIES WEEK, Feb. 21, 1983, at 10. In addition, the Exchange Act itself was amended in 1983 to require all broker-dealers registered with the SEC to become members of a self-regulatory organization.

54. For a good review of this period, see SECURITIES INDUSTRY STUDY, REPORT OF THE SENATE COMM. ON BANKING, HOUSING, AND URBAN AFFAIRS, S. DOC. NO. 109 92d Cong., 2d Sess. 7-11 (1972). For a scathing indictment of brokerage industry and self-regulatory inadequacies, particularly of the NYSE, during this period, see H. BARUCH, *supra* note 16, at 298-307 (1971). Among the larger houses that failed or had to be rescued were DuPont, Glorie, Forgan; Hayden, Stone; Goodbody & Co.; and Robinson & Co. See *id.* at 152-53.

organization rules of financial integrity, particularly those of the New York Stock Exchange, proved insufficient to protect customers from financial loss caused by NYSE member firm insolvency. Even more troubling, the surveillance and inspection capability of the self-regulatory organizations proved inadequate to detect and correct these "back office" problems of member firms in time to save the firms from insolvency or their customers from loss.⁵⁵ In the wake of the brokerage house failures that followed the 1968-70 crisis, Congress enacted the Securities Investor Protection Act of 1970,⁵⁶ establishing an insurance mechanism for securities customer deposits similar to that available to bank or savings and loan customers. Following enactment of that legislation, each House of Congress commenced wide ranging hearings into the problems of the securities industry. Much of the inquiry was directed toward the performance of the self-regulatory organizations, especially the NYSE. What emerged from the hearings, four years after they began, was legislation giving the SEC broader powers over registered securities exchanges than it had held previously. Yet although self-regulation came in for serious criticism in the hearings, no one seriously proposed that the system be abolished. Indeed, in the midst of the stormy discussion over the proper future role for self-regulation, Congress created still another securities industry self-regulator, the Municipal Securities Rulemaking Board.⁵⁷

The foregoing history indicates that although the self-regulatory system in the securities industry sometimes has been found wanting, and has been subject to increasing governmental oversight, it occupies a secure place in the regulation of the securities industry, and has achieved broad acceptance by Congress as a complement to governmental regulation. Because securities industry self-regulation has been endorsed so clearly and encouraged by Congress, antitrust challenges to the self-regulatory conduct of securities industry self-regulators should be subject to a different legal analysis than that given to self-regulatory bodies not enjoying such congressional favor. As will be discussed below, however, reconciling the conflicting congressional policies embodied in the Exchange Act and in the antitrust laws has proved to be a difficult process, both for the federal courts and for Congress.

II. ACCOMMODATION OF THE ANTITRUST LAWS TO GOVERNMENT SUPERVISED SELF-REGULATION IN THE SECURITIES INDUSTRY

A. *Basic Questions*

History and experience support the concern that voluntary organizations of members of a trade, industry or profession, if left to their own devices, will be more likely to collude with each other to restrain competition than to police

55. For a description of the problems arising during this crisis period, see STUDY OF UNSAFE AND UNSOUND PRACTICES OF BROKERS AND DEALERS, REPORT AND RECOMMENDATIONS OF THE SEC, H. R. Doc. No. 231, 92d Cong., 2d Sess. (Comm. Print 1971) [hereinafter UNSAFE AND UNSOUND PRACTICES].

56. Pub. L. No. 91-598, 84 Stat. 1636 (1970) (codified at 15 U.S.C. §§ 78aaa-78fff (1982)).

57. See *supra* note 14.

each other to ensure protection of the public.⁵⁸ For that reason, federal judicial and legislative attitudes toward private business organizations consistently reflect a reluctance to grant the organizations much leeway to engage in self-governing activities. As recently as 1982, the Supreme Court has rejected assertions by groups that their self-governing efforts with anticompetitive consequences should be exempted from antitrust sanctions because they were undertaken for a public interest purpose,⁵⁹ and that organizations should be immune from liability under the antitrust laws because of their public interest *raison d'être*, despite the anticompetitive acts of their agents.⁶⁰

In determining whether any organized conduct violates the antitrust laws,⁶¹ courts ought logically address three questions. The first is whether the antitrust laws reach the conduct at all, or whether the conduct is immunized from antitrust review by explicit or implicit statutory directive.⁶² This question may be called the "immunity question."⁶³ Generally, the only conduct that courts will recognize as being exempt (*i.e.*, immune) from antitrust review is that which is immunized by express statutory language. The Supreme Court has stated repeatedly that implicit statutory grants of immunity from the antitrust laws are very difficult to find, and when found will be given only the

58. As will be discussed below, the first three major securities and commodity futures industry cases concerning a reconciliation of regulatory and antitrust law involved, respectively, a group boycott (*Silver v. New York Stock Exch.*, 373 U.S. 341 (1963)), price fixing (*Thill Sec. Corp. v. New York Stock Exch.*, 433 F.2d 264 (7th Cir. 1970), *cert. denied*, 401 U.S. 994 (1971)), and a concerted refusal to deal (*Ricci v. Chicago Mercantile Exch.*, 409 U.S. 289 (1973)).

59. *See, e.g.*, *Arizona v. Maricopa County Medical Soc'y*, 457 U.S. 332 (1982) (*maximum fee schedule* violative of the antitrust laws). *See also* *National Soc'y of Professional Eng'rs v. United States*, 435 U.S. 679 (1978) (prohibition of competitive bidding violative of the antitrust laws).

60. *American Soc'y of Mechanical Eng'rs v. Hydrolevel Corp.*, 456 U.S. 556 (1982).

61. The antitrust provision of particular relevance to self-regulatory activities is § 1 of the Sherman Act, 15 U.S.C. § 1 (1982). That section provides: "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several states, or with foreign nations, is declared to be illegal"

62. Some collective industry efforts are expressly exempted from the antitrust laws by federal statute. These include: (1) organization of agricultural cooperatives pursuant to the provisions of the Capper Volstead Act, 7 U.S.C. §§ 291-292 (1982); (2) joint newspaper agreements pursuant to 15 U.S.C. § 1803 (1982). Other congressional acts confer limited statutory immunity from the antitrust laws upon specified collective members of an industry if the members acts were approved by a federal administrator. These include (1) rail carrier rate agreements if approved by the Interstate Commerce Commission, 49 U.S.C. § 10706 (Supp. V 1981); (2) shipping carrier agreements covering rates, accommodation, poolings, etc., if approved by the Federal Maritime Commission pursuant to 46 U.S.C. § 814 (1976 & Supp. V 1981); (3) consolidations, mergers, purchases, leases etc. between and among air carriers if approved by the Civil Aeronautics Board pursuant to 49 U.S.C. § 1384 (1976 & Supp. V 1981).

In the absence of express statutory exemption, the Supreme Court has been reluctant to find an implied repeal of the antitrust laws, even for conduct overseen and approved by a federal or state regulatory agency. *See, e.g.*, *Cantor v. Detroit Edison Co.*, 428 U.S. 579 (1976) (approval of "tie-in" arrangement by state utilities commission did not immunize the utility's conduct from antitrust review); *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321, 348 (1963). *Philadelphia Nat'l Bank* involved the application of § 7 of the Clayton Act, 15 U.S.C. § 18 (1982) to commercial banking. In that case, the court held that approval by the Comptroller of the Currency of a merger between two major Philadelphia banks did not immunize the merger from judicial review.

63. One commentator has referred to this question as the "repeal question." *See* Linden, *A Reconciliation of Antitrust Law With Securities Regulation: The Judicial Approach*, 45 GEO. WASH. L. REV. 179 (1977).

narrowest scope.⁶⁴ Therefore, unless Congress explicitly has exempted self-regulatory activity from the antitrust laws, immunity from antitrust challenge will exist only if something else in the statutory scheme justifies finding such immunity by implication.

The "something else" that might justify such implied immunity may be the presence of oversight by a government agency. One important task that has confronted Congress and challenged the courts has been to craft a doctrine of immunity for statutorily recognized self-regulatory organizations subject to governmental supervision that does not impair their effectiveness on the one hand, or invite collusive conduct on the other.⁶⁵ In other words, in confronting the immunity question, the key issue concerning the role of the federal regulatory agency is whether the members of a self-regulatory organization should enjoy immunity from judicial antitrust review by virtue of the government's supervisory connection to any objectionable conduct.

A related issue that must be analyzed in connection with the immunity question is immunity from what? Immunity from having *any* governmental entity review the conduct for consistency with antitrust policy? Immunity from having the courts undertake such review? Or is the immunity sought immunity from penalty, rather than from governmental intervention? The separation of immunity-from-review from immunity-from-penalty is usually not made in discussing the immunity question because under the present law there is no provision for limiting private antitrust suits to equitable relief only.⁶⁶

The second question is whether conduct that is not immune from scrutiny under the antitrust laws nonetheless does not violate those laws. This may be called the "conduct question."⁶⁷ By Supreme Court doctrine, the traditional tests for anticompetitive conduct have divided conduct roughly into two major categories. Certain conduct is so inherently anticompetitive that it is considered a *per se* violation of the antitrust laws. Of such conduct, no judicial inquiry is made to determine whether putative benefits to competition of the

64. See, e.g., *Silver v. New York Stock Exch.*, 373 U.S. 341, 357 (1963).

65. The conflict between the antitrust laws and securities regulation has been often noted by commentators, starting with *The Anti-Trust Laws and the Self Regulation of Industry*, Address by John Dickenson, before the American Political Science Association (Dec. 28, 1931), reprinted in 18 A.B.A. J. 600 (1932). Dickenson, who was a key figure in the enactment of the Exchange Act, advocated a generous allowance for self-regulatory conduct under traditional rule of reason antitrust analysis. In more recent years there have been many articles on the subject. See, e.g., Johnson, *Application of Antitrust Laws to the Securities Industry*, 20 Sw. L.J. 536 (1966); Levin, *supra* note 2; Linden, *supra* note 63; Ponsoldt, *The Application of Sherman Act Antiboycott Law to Industry Self-Regulation: An Analysis Integrating Nonboycott Sherman Act Principles*, 55 S. CAL. L. REV. 1 (1981); Note, *The Application of Antitrust Laws to the Securities Industry*, 10 WM. & MARY L. REV. 136 (1968).

66. A recent Reagan administration proposal to amend the antitrust laws to provide for single rather than treble damages in certain instances was abandoned after strong opposition to this measure surfaced in Congress. Lessening the penalties for antitrust violations would surely remove one major concern of the self-regulatory organizations regarding the question of immunity, but would not remove another. The other is the use of federal regulatory oversight to the regulatory scheme.

67. One commentator has called this the "justification question." Linden, *supra* note 63.

activity outweigh the harm to competition.⁶⁸ Anticompetitive conduct that is not a per se violation of the antitrust laws is subject to a balancing test, known as the "rule of reason." The rule of reason is premised on the recognition that all contracts and combinations restrain trade to some degree, and that the Sherman Act was intended to reach only unreasonable restraints.⁶⁹ In its traditional formulation, the rule of reason analysis requires determining whether the long term procompetitive effects of conduct outweigh the short term anticompetitive effects. If the balance is favorable, the conduct will not be considered an "unreasonable" restraint of trade or a violation of the antitrust laws. Under this traditional test, enhancement of competition is on *both* sides of the balance,⁷⁰ and the Supreme Court has rejected the defense to antitrust challenges that the conduct is "reasonable" because it is undertaken to achieve some other desirable societal objective.⁷¹

The issue here is whether, in assessing the anticompetitive conduct of federally recognized self-regulatory organizations, a different balancing test is needed. Regulation is at times indifferent to competition, and in some instances, regulation may have been undertaken specifically to check competition.

The third question that must be asked when determining whether anticompetitive conduct of governmentally recognized and supervised self-regulatory organizations is actionable under the antitrust laws is a question that is peculiarly relevant to organizations with an identified government regulator to oversee their activities: What should be the respective roles of the various organs of government—the federal courts and the federal regulatory agencies—in hearing antitrust challenges to self-regulatory conduct? This question may be called the "jurisdictional question."

For industries regulated by government agencies, the answers to the first and the third questions—on immunity and jurisdiction—are complicated by the many possible ways in which the relationship between the regulated and the regulators may be crafted. The degree of federal regulatory oversight of,

68. Conduct held to constitute a per se violation includes: price fixing, territorial agreements, tying arrangements, agreements not to compete, agreements to limit the supply of a commodity, and group boycotts or concerted refusals to deal. These categories are set out in *Northern Pac. Ry. v. United States*, 356 U.S. 1 (1958). See generally Note, *Monopolies—Restraint of Trade—Associations and Clubs*, 18 CASE W. RES. L. REV. 321, 323 n.22 (1966). In a number of recent cases the Supreme Court and lower federal courts have somewhat blurred the distinction between conduct that is per se unlawful and that which must be analyzed for reasonableness, holding that certain conduct falling technically within a per se category should be analyzed for reasonableness. See, e.g., *Broadcast Music, Inc. v. Columbia Broadcasting Sys., Inc.*, 441 U.S. 1 (1979) (fixing of prices not per se unlawful); *United States Trotting Ass'n v. Chicago Downs Ass'n*, 665 F.2d 781 (7th Cir. 1981) (concerted refusal to deal not per se unlawful).

69. See *Chicago Bd. of Trade v. United States*, 246 U.S. 231, 238 (1918).

70. See, e.g., *Appalachian Coals, Inc. v. United States*, 288 U.S. 344 (1933), in which the Court said that "[g]ood intentions will not save a plan otherwise objectionable," *id.* at 372, but that the essentially pro-competitive purpose of the conduct made the minimal immediate anticompetitive effects of the conduct a reasonable restraint.

71. See, e.g., *National Soc'y of Professional Eng'rs v. United States*, 435 U.S. 679, 688-94 (1978) (pro "public safety" purpose to a rule prohibiting competitive bidding among Society's members held not relevant to rule of reason).

and involvement with, the supervised self-regulatory organization will bear critically on the questions whether the federal regulator has jurisdiction to decide antitrust matters and whether its approval of self-regulatory conduct immunizes the conduct from judicial review or penalty. The touchstone issue in answering these questions is said to be congressional intent,⁷² but usually such intent has to be inferred from the nature of the regulatory scheme, rather than discovered by reference to explicit statutory language. Often, resolving the questions will hinge upon the degree to which it may be said that the scheme of governmental regulation of an industry is "pervasive,"⁷³ or the extent to which the activity in question may be said to have been part of the regulated entity's regulated business and thus afforded different treatment from that given to unregulated business.⁷⁴ The issues regarding pervasiveness and the nature of the conduct are complicated further when the government regulation is of a self-regulatory organization rather than of an ordinary entity (*i.e.*, one without regulatory responsibilities).

Taking first the question whether the conduct of the self-regulatory organization is part of its regulated business, if the self-regulatory organization's business is to regulate members of an industry or profession to ensure that their conduct conforms to vague statutory standards, the organization will need and must have a wide latitude in choosing how to achieve that important but imprecise goal.⁷⁵ To put the matter another way, the line between conduct that is part of the regulated business and conduct that is not is difficult enough to draw for the ordinary business; it is much more difficult to draw for the business of the self-regulatory organization.

Second, with regard to the pervasiveness of government oversight in the regulatory scheme, the breadth of governmental oversight of a self-regulatory organization's activities may be virtually coextensive with those activities. That very breadth of oversight may mitigate against effective governmental

72. See *Otter Tail Power Co. v. United States*, 410 U.S. 366, 373-75 (1973).

73. See 1 J. AREEDA & P. TURNER, *ANTITRUST LAW* § 223b (1978).

74. Public utility rate structures, for example, may be said to be regulated pervasively so that antitrust challenges to such rates should be heard first by the regulatory agency that approved them, and prior approval of such rates by the regulatory agency should immunize the utility from penalty under antitrust laws. Yet, the Supreme Court has refused to exempt categorically the conduct of public utilities from antitrust penalty even when the conduct was part of a rate package approved by a governmental utilities commission. *Cantor v. Detroit Edison Co.*, 428 U.S. 579 (1976). In *Cantor* the state utilities commission had approved an electric company's rate schedule that included the provision of "free" light bulbs to the utility's customer. A very divided Court held that the distribution of light bulbs was an illegal tie-in not made immune from suit by approval of the state's utilities commission because the *raison d'être* of utilities regulation did not reach the sale and distribution of light bulbs.

75. The Exchange Act requires that all self-regulatory organizations registered (and thus officially recognized) under the Act "ha[ve] the capacity to be able to carry out the purposes of [the Act] and to comply, and . . . to enforce compliance by [their] members and persons associated with [their] members, with the provisions of [the Act], the rules and regulation thereunder, and the rules of the [self-regulatory organization]." Exchange Act § 6(b)(2), 15 U.S.C. § 78f(b)(2) (1981). A virtually identical provision for registered securities associations is § 15A(b)(2), 15 U.S.C. § 78o-3(b)(2) (1981). The Exchange Act's purposes include, among other things, protecting interstate commerce, the national credit, the federal taxing power, and the national banking system, and maintaining of fair and honest markets. Exchange Act § 2, 15 U.S.C. § 78b (1981). These are tall orders and not easily reducible to set formulations for their achievement.

involvement with all of the ongoing activities of the self-regulatory organization. Therefore, much self-regulatory activity will take place under the general aegis of governmental supervision but without day to day specific governmental oversight and approval. The extent to which such pervasive but somewhat superficial governmental supervision should shield a self-regulatory organization from antitrust penalty and justify deference to agency jurisdiction is a difficult question.

The answers to the questions about the relationship of the antitrust laws to government supervised self-regulation have evolved mainly in connection with securities industry self-regulation because, as noted, these are the most prominent federally recognized self-regulatory organizations. For nearly a half-century they have enjoyed explicit congressional endorsement for their activities. Yet, as is discussed below, the resolution that has been achieved has come about from a long, difficult process involving both the courts and Congress. Even now the inquiry lacks any definitive Supreme Court case or unequivocal expression of congressional intent to solidify and clarify the results.

B. Judicial Decisions: 1963-1973

As noted earlier, the regulatory scheme in the securities industry was uneven and far from pervasive. It was in the context of this regulatory scheme that three major cases involving the reconciliation of the antitrust laws with securities industry self-regulation were decided in the decade from 1963 to 1973. While the decisions in these cases were inhospitable to self-regulation, they must be considered in their historical context. Their very inhospitality helped create changes in the regulatory structure and in the behavior of the federal regulators, which perhaps created a more hospitable climate for self-regulation now.

1. *Silver*⁷⁶

The vulnerability of securities-industry self-regulation to antitrust challenge was not apparent until the decision in *Silver v. NYSE*,⁷⁷ decided nearly thirty years after the passage of the Exchange Act.⁷⁸ In 1959 Silver, a municipal bond dealer, brought an antitrust action against the NYSE concerning a peremptory Exchange order that required member firms with direct private telephone links to Silver's firm to sever such links. The Exchange provided no reasons for its order, the consequence of which was to exclude Silver from quick access to Exchange members for the purposes of trading and discovering prices and, as Silver alleged, to cause his firm's volume of business to drop precipitously. In addition to treble damages, Silver sought an injunction

76. *Silver v. New York Stock Exch.*, 373 U.S. 341 (1963).

77. *Id.*

78. One antitrust case had been brought in the early 1950s, *United States v. Morgan*, 118 F. Supp. 621 (S.D.N.Y. 1953), but the case was against broker-dealers for the syndicate system under which new issues are brought to market, not against the self-regulatory organization, and specifically not against the NASD under whose regulatory aegis the syndicate system worked.

against the NYSE's enforcement of its order.⁷⁹

As noted, the Exchange's severance order had been issued peremptorily; the Exchange had followed no delineated procedures in issuing the order. Thus, Silver's firm had not been afforded an opportunity to protest the Exchange's action, and whether the firm had been quarantined for justifiable reasons could not be determined from any record made by the Exchange.⁸⁰ In addition, under the Exchange Act as it then existed the SEC had no authority to disapprove the Exchange's conduct, because technically the action was the enforcement of a rule, not the promulgation of a rule.⁸¹ Consequently, the SEC had no power to review the matter to determine whether the Exchange's action was within the scope of its self-regulatory authority, or whether the action was an appropriate self-regulatory response to the alleged problem. Given the clearly anticompetitive consequences of the NYSE's action, the absence of federal regulatory oversight was particularly disturbing since there had been no neutral arbiter to determine whether the NYSE's action was anything more than poorly disguised instigation of a group boycott.

The district court granted the relief requested by Silver.⁸² It reasoned that, at the very least, the NYSE's action went beyond an exercise of its legitimate regulatory control of its members, and therefore could not be immunized from antitrust attack as a legitimate exercise of regulatory responsibility.⁸³ Having made this determination, the district court did not discuss whether the test to be applied to the NYSE's conduct should differ from the traditional tests (per se or rule of reason) applied to ordinary private entities. The court simply found that without the umbrella of the Exchange Act to legitimize the Exchange's conduct, the order and the accompanying compliance with the order by Exchange member firms amounted to a group boycott—a per se violation of the Sherman Act.⁸⁴ On appeal, the Second Circuit reversed, not because it disagreed with the district court about the conduct test to be applied

79. The treble damage claim was brought under §§ 4 & 16 of the Clayton Act, 15 U.S.C. §§ 15 & 26 (1976) (current version of § 4 at 15 U.S.C. § 15 (Supp. V 1980)). *Silver*, 373 U.S. at 345 n.4.

80. Although the Exchange alleged at trial that its actions were prompted by evidence of illegal and unethical conduct by Silver, the Exchange refused to disclose that information without first obtaining from Silver a release from potential libel claims. Since Silver would provide no such release, the Exchange refused to reveal its information. Without that information, the trial judge ruled, the Exchange's record basis for its action amounted to little more than "dubious gossip emanating from unreliable sources." *Silver v. New York Stock Exch.*, 196 F. Supp. 209, 225 (S.D.N.Y. 1961).

81. Until the passage in 1975 of the Securities Act Amendments, the SEC could not directly review actions taken by the Exchange to enforce its rules but could review only the initial rule proposals. The Exchange's order was not a promulgation of a rule; it was the enforcement of a broadly worded rule (dealing with member-firm relations with nonmembers) already promulgated. Some commentators have criticized the idea that there is a genuine distinction between the function of rule approval and the function of rule oversight. See 1 J. AREEDA & P. TURNER, *supra* note 73, ¶ 224, at (the authors called the distinction disingenuous). See also Linden, *supra* note 63, at 190 n.55. Whether the distinction is real or artificial, its significance to *Silver* is that the Supreme Court effectively removed an analysis of the role of the SEC from the decision in the case.

82. *Silver v. New York Stock Exch.*, 196 F. Supp. 209 (S.D.N.Y. 1961).

83. *Id.* at 221-22.

84. *Id.* at 222-24.

(a question that it did not reach), but because it disagreed that the Exchange was vulnerable at all—that is, it differed on the immunity question.⁸⁵ Finding that Exchange regulatory authority did extend to the order in question, the court determined that, on that basis alone, the Exchange was immune from challenge under the antitrust laws.

In reviewing the decisions of the two lower courts, the Supreme Court confronted the immunity and the conduct questions (but not the jurisdictional question, because the SEC had none). As to the immunity question, although the Court concurred with the court of appeals that the questioned order was within the scope of the Exchange's general regulatory authority over member firms, it disagreed that such a finding *ipso facto* conferred immunity on the Exchange.⁸⁶ The Court thus resolved the simplest question concerning immunity from the antitrust laws for federally recognized self-regulatory organizations. Absent an express statutory grant of immunity, such organizations would not be immune from antitrust challenge simply because they were acting within the scope of their regulatory authority. The more difficult question was under what circumstances should immunity be appropriately conferred. Here the Supreme Court constructed a new test: a federally recognized self-regulatory organization would be immune from antitrust challenge to the extent that a grant of immunity was necessary to effectuate the statutory scheme of regulation from which such organization derived its legitimacy. Applied to the securities industry self-regulators, immunity would be conferred to the extent necessary to achieve the objectives of the Exchange Act. The problem with the immunity test articulated in *Silver* was that in applying it, the Court simply concluded that a grant of immunity was not necessary to achieve the purposes of the Exchange Act, without saying why.

An additional problem created by the case was the use of the word "necessity" to create a second test—one to determine whether the Exchange's conduct violated the antitrust laws. In recognition of the Exchange's responsibilities as a regulator, the Supreme Court rejected the district court's simple application of the *per se* rule⁸⁷ to assess the Exchange's conduct. Instead, the Court stated that the appropriate test was whether the conduct in question was necessary for the effectuation of the Exchange Act.⁸⁸ The Court then found that the conduct—which included not only the actual severance order, but also the authoritarian procedures used to promulgate it—was so

85. *Silver v. New York Stock Exch.*, 302 F.2d 714 (2d Cir. 1962).

86. *Silver*, 373 U.S. at 355-56.

87. *Id.* at 349.

88. See Linden, *supra* note 63, at 195. He labels the tests as the "repeal issue" and the "justification issue." As the author of that article observed, and as is described more fully below, one consequence of confounding the term "necessity" was that various interest groups were likely to seize upon the interpretation of *Silver* that best suited their interests. Groups, such as the exchanges, that favored broad protection from antitrust attack were later to advocate application of the necessity test to the immunity question and to argue that any involvement of the SEC in the regulatory process made such immunity necessary. In contrast, those groups suspicious of or hostile to the self-regulatory activities of the exchanges were likely to seize upon the conduct-necessity test and to urge that each challenged action be held up to a factual determination of necessity and be struck down should the action be found to be less than necessary to the regulatory scheme.

flawed that on procedural grounds alone the Exchange's conduct could not be said to have been necessary for the achievement of the aims of the Exchange Act.⁸⁹ Because the Court sidestepped the substantive analysis of the Exchange's conduct by resting its decision on flawed procedures, it gave little guidance about the determinants of the conduct-necessity test.

As noted earlier, the jurisdictional question did not arise in *Silver* because, under the securities laws as they then existed, the Exchange action in question was not subject to SEC review. In a footnote to the case, the Court explicitly reserved judgment on whether, with SEC involvement, "a different case would arise concerning exemption from the operation of laws designed to prevent anticompetitive activity."⁹⁰ The Court did not reveal to which issue the existence of federal agency supervision would relate (*i.e.*, the immunity question, the conduct question, or the jurisdictional question).

2. *Thill Securities v. NYSE*⁹¹

The first major judicial effort to address the substantive issues raised in *Silver* was made by the United States Court of Appeals for the Seventh Circuit in 1970 in *Thill Securities Corp. v. NYSE*.⁹² *Thill Securities* concerned a challenge by an over-the-counter broker-dealer, Thill Securities Corp., to a NYSE rule prohibiting its members from rebating to nonmembers a portion of the commission fees charged for executing nonmember transactions on the Exchange. This anti-rebate rule was a component of the NYSE's overall regimen for fixing commission rates and was designed to prohibit circumvention by indirect means. Unlike the situation in *Silver*, the SEC had power to review the Exchange's rule and to reject it. It had done the former, but not the latter.

This significant difference between *Thill Securities* and *Silver*, the existence in the former of SEC oversight authority, should have weighed in the court's analysis of the immunity question. If the SEC actually had reviewed and approved the rule,⁹³ the important question of the relevance of prior gov-

89. *Silver*, 373 U.S. at 361-64. The Court stated that:

Since it is perfectly clear that the Exchange can offer no justification under the Securities Exchange Act for its collective action in denying petitioners the private wire connections without notice and an opportunity for hearing, and that the Exchange has therefore violated [the antitrust laws], there is no occasion for us to pass upon the sufficiency of the reasons which the Exchange later assigned for its action.

Id. at 365.

90. *Id.* at 358 n.12.

91. *Thill Secs. Corp. v. New York Stock Exch.*, 433 F.2d 264 (7th Cir. 1970), *cert. denied*, 401 U.S. 994 (1971).

92. *Id.* In the interim, the Seventh Circuit, in a very short opinion, upheld the NYSE's minimum commission rate schedule against an antitrust challenge. *Kaplan v. Lehman Bros.*, 371 F.2d 409 (7th Cir.), *cert. denied*, 389 U.S. 954 (1967). The court cited specific statutory authorization for such conduct, and applied the conduct-necessity test established in *Silver*. The Supreme Court denied certiorari over the objections of Chief Justice Warren, who decried the absence of "close analysis and delicate weighing process" in the Seventh Circuit's opinion. *Kaplan*, 389 U.S. at 957 (Warren, J., dissenting).

93. A complicating circumstance in analyzing the securities industry cases of the period between 1970 and 1975 was the rapid transformation of the regulatory scene during those years. The early seventies was a time of extensive congressional exploration of the regulatory structure of the

ernmental approval, which was not present in *Silver*, would have been presented. Indeed, in successfully defending against the antitrust attack in district court, the NYSE had argued that the SEC's review power over the rule did immunize the Exchange from antitrust challenge. In agreeing with the Exchange, the district court cited *Silver*'s footnote twelve⁹⁴ as "intimating" that an allegedly anticompetitive Exchange rule subject to SEC review would be treated differently from a rule, such as that challenged in *Silver*, in which oversight power was lacking. On appeal, the Seventh Circuit flatly rejected this argument: "[W]e find in the teachings of *Silver*, no 'intimation' that the mere possibility of SEC review wraps the conduct of the Exchange in an impenetrable shield of antitrust immunity."⁹⁵ The court stated that even if the NYSE could show actual exercise of SEC review power,⁹⁶ that showing would be largely irrelevant to the immunity question because the SEC's regulatory mandate did not include a consideration of the effect of self-regulatory rules upon competition. The court said that the courts, not the SEC, had the "primary responsibility for enforcing competition as mandated by Congress in antitrust laws."⁹⁷

After thus dealing with the question of immunity, the court reached the question whether the NYSE's conduct violated the antitrust laws. It decided that application of the conduct-necessity test created in *Silver* (*i.e.*, whether the

securities industry. Of course, the SEC was well aware of Congress' interest and altered its own regulatory behavior to respond to congressional criticism about the quality of its oversight of the self-regulatory organizations. To say that the SEC "reviewed" an NYSE rule, therefore, is to say different things depending upon the particular time period at issue. For an indication of how dramatically the SEC's review changed, from passive approval to active involvement, see *Thill Securities Corp. v. New York Stock Exch.*, 473 F. Supp 1364, 1368-70 (E.D. Wis. 1979). The court there catalogued the SEC's involvement with the anti-rebate rule from 1938 to 1972.

94. *Silver*, 373 U.S. at 358 n.12. See *supra* text accompanying note 90.

95. *Thill Securities*, 433 F.2d at 269.

96. The court was not impressed with the SEC's conduct in this respect: "[T]here is no evidence in the record that the SEC is exercising actual and adequate review jurisdiction under the Act." *Thill Securities*, 433 F.2d at 271. As noted *supra* note 93, in the late 1960s when the factual record of the case was made, the vigor of the SEC's oversight was not what it later became.

97. *Id.* at 272. The short shrift given by the court to the significance of the SEC's review to the immunity question function was consistent with the Supreme Court's treatment of other regulatory agencies charged with oversight of industry conduct. At the time *Thill Securities* was decided, the most prominent of these cases was *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321 (1963), decided in the same year as *Silver*. The *Philadelphia Nat'l Bank* case concerned the approval by the Comptroller of the Currency of a merger between two large banks in Philadelphia. The Bank Merger Act as it then existed vested in the Comptroller the authority to approve such mergers and directed him to consider competitive factors before doing so. Because of the Act's provisions the banks argued that his approval immunized the merger from challenge under the antitrust laws. The Court rejected that argument, holding that immunity from the antitrust laws must come either by express legislative grant or, rarely, by implication because of a "plain repugnancy between the antitrust and regulatory provisions." *Philadelphia Nat'l Bank*, 374 U.S. at 350-51 (citation omitted). Since the Court found neither factor present, the Comptroller's approval was no bar to a de novo determination by the courts of whether the merger substantially lessened competition in violation of § 7 of the Clayton Act. *Philadelphia Nat'l Bank* was cited subsequently in cases dealing with securities industry self-regulation for the proposition that the mere prior approval of self-regulatory conduct by the SEC did not immunize the self regulation from de novo judicial determination on antitrust complaint. *Philadelphia Nat'l Bank* did not involve conduct of a self-regulator but of corporations, and the remedy sought was not treble damages, but an injunction. These critical distinctions arguably limit the relevance of that case to antitrust issues concerning government supervised self-regulation.

Exchange's rule was necessary to the Exchange Act) was a question of fact. It therefore remanded the case to the district court to determine whether, as a question of fact, the anti-rebate rule was necessary to make the Exchange Act work.⁹⁸ The Supreme Court denied certiorari.⁹⁹

3. *Ricci v. Chicago Mercantile Exchange*¹⁰⁰

Neither *Silver* nor *Thill Securities* addressed the jurisdictional question—*Silver* because the SEC had none, *Thill Securities* because the issue was not raised.¹⁰¹ The jurisdictional question was paramount, however, in the next major case decided after *Thill Securities*, *Ricci v. Chicago Mercantile Exchange*.¹⁰² In *Ricci*, a case concerning commodity futures,¹⁰³ not securities, the enforcement of an exchange rule regarding financial qualifications for membership in the Chicago Mercantile Exchange (CME) was challenged on grounds that the action violated the Commodity Exchange Act and the anti-trust laws. The district court dismissed the complaint and plaintiff appealed. The Seventh Circuit then reversed and remanded with a directive that the judicial proceedings be stayed pending review by the Commodity Exchange Commission (CEC),¹⁰⁴ predecessor to the present Commodities Futures Trading Commission (CFTC). The majority of the Seventh Circuit panel ruled that the regulatory agency had primary jurisdiction to hear and decide the question whether the Exchange's action violated the Commodity Exchange Act. The majority's language hinted that the Commission also could resolve the antitrust question (*i.e.*, could determine whether the Exchange's action was necessary to make the Act work).

A very divided Supreme Court upheld the Seventh Circuit's decision that the Commission should be given the first opportunity to review the CME's application of the rule.¹⁰⁵ The Court made clear, however, that the function of the Commission's review was limited to those matters for which the CEC presumably had expertise, that is, to finding facts and to deciding whether the CME's conduct had violated the Commodities Exchange Act. The Commission's review would not contribute to the question whether the CME's conduct violated the antitrust laws (*i.e.*, whether the conduct was necessary to the statutory scheme of commodities futures regulation), nor would the existence of

98. *Thill Securities*, 433 F.2d at 273-74.

99. *Thill Securities*, 401 U.S. 994 (1971).

100. 409 U.S. 289 (1973).

101. The concurring opinion in *Thill Securities* did suggest that the district court consider the question of SEC jurisdiction, *Thill Securities*, 433 F.2d at 276 (Swygert, C. J., concurring), but the issue was not central to the discussion of that case and was not mentioned by the majority.

102. 409 U.S. 289 (1973).

103. When *Ricci* was decided, the federal government's regulation of commodity exchanges was even less pervasive than its regulation of securities exchanges. Regulation of commodity exchanges was later revamped by the creation of the Commodity Futures Trading Commission. Pub. L. No. 93-463, 88 Stat. 1389 (1974).

104. 447 F.2d 713 (7th Cir. 1971).

105. *Ricci v. Chicago Mercantile Exch.*, 409 U.S. 289 (1973). A plurality of the Court ruled that the case should be stayed by the district court pending agency review. One Justice concurred; four Justices dissented, and one wrote an additional dissenting opinion.

Commission review authority over the CME immunize the Exchange from a subsequent de novo judicial determination of the antitrust complaint. The CEC's review, however, would simplify the court's task of applying the conduct-necessity test, because if the Commission determined that the CME's conduct violated the Commodity Exchange Act, a court would have little difficulty in deciding whether the CME's conduct was necessary to make the Commodity Exchange Act work. Presumably, violations of a statute cannot be necessary to the statute's working. Conversely, a finding by the Commission that the conduct was consistent with the Act would be useful to the courts in determining the necessity of the conduct to the statutory scheme. The majority agreed with the four dissenters (who would have denied the stay) that regardless of whether the Commission found the challenged self-regulatory conduct to be consistent or inconsistent with the Commodities Exchange Act, the critical antitrust analysis was for the courts, not the Commission.¹⁰⁶ The courts were empowered to determine whether the conduct lawful under the Act was also *necessary* to its effectuation.

The Court reaffirmed *Ricci* several years later in *Chicago Mercantile Exchange v. Deaktor*,¹⁰⁷ which reversed a Seventh Circuit denial of a stay. The Seventh Circuit had construed *Ricci* to require primary agency review only in instances in which self-regulatory conduct that was at least colorably lawful under the Commodity Exchange Act—such as the promulgation or enforcement of a rule—nonetheless appeared to conflict with the antitrust laws.¹⁰⁸ In such instances, at least, the regulatory agency could contribute its legal expertise to the question whether the conduct was appropriate to the organic acts the agency was created to administer. Since the allegation in *Deaktor* was that the exchange had engaged in conduct that was unquestionably unlawful under the Act—manipulation of futures contracts—and that in so doing it also had violated the antitrust laws, the Seventh Circuit saw no need to defer to the Commission. It reasoned that there was no real issue regarding the necessity of the conduct to the Commodity Exchange Act and that the Commission would have nothing to contribute regarding the antitrust question. The Supreme Court nonetheless insisted that the Commission first hear the non-antitrust matter before the federal courts heard the antitrust question. The Court reasoned that, at the very least, the agency would act as a fact finder in the manner of a special master, and could offer its view of whether the conduct was in fact a manipulation.¹⁰⁹

106. Said the Court: "We make no claim that the Commission has authority to decide either the question of immunity as such or that any rule of the Exchange takes precedence over antitrust policies." *Ricci*, 409 U.S. at 307. The dissenters argued that giving the agency the right of first review was simply a waste of time. *Id.* at 308-10.

107. 414 U.S. 113 (1975) (per curiam).

108. *Deaktor v. L.D. Schreiber & Co.*, 479 F.2d 529 (7th Cir. 1973).

109. *Deaktor*, 414 U.S. at 113-15. See also *Schaefer v. First Nat'l Bank of Lincolnwood*, 509 F.2d 1287 (7th Cir. 1975), cert. denied, 425 U.S. 943 (1976). There, the Seventh Circuit, after experiencing two prior reversals from the Supreme Court (*Ricci* and *Deaktor*), barred an antitrust claim against Amex because the claimants had not first petitioned the SEC to review Amex's conduct. Said the court: "Private parties may only bring antitrust claims against an exchange or its members when there is no other vehicle for review." *Id.* at 1300.

The upshot of these cases was that government supervised, statutorily recognized self-regulators were not accorded immunity solely by virtue of their status as government supervised self-regulators. Nor did they gain immunity from having received prior approval of their conduct from the federal regulatory agency that had the statutory responsibility to review their conduct. On the matter of jurisdiction, the role of the federal regulatory agency in adjudicating antitrust challenges to self-regulatory conduct was limited to deciding whether the self-regulator's acts had violated the regulatory statute, and to acting as a fact finder. As will be seen, the Supreme Court seemed paradoxically to insist that the federal agencies be given primary jurisdiction to hear all challenges to self-regulatory conduct, but to have no jurisdiction to resolve the antitrust question. Or to put the matter another way, while the Court recognized the primacy of agency jurisdiction in hearing complaints against the conduct of self-regulatory bodies, they limited the subject matter of such jurisdiction to questions concerning the regulatory statutes, not the antitrust laws. As to the conduct question, the first case, *Silver*, offered a variant of the rule of reason to analyze self-regulatory conduct, but the parameters of such a test were not spelled out in that case, nor in the cases that followed.

These results were inimical to the fostering of encouragement of vigorous government supervised self-regulation. They placed little value on the oversight responsibilities of the federal agency in reviewing and guiding self-regulatory conduct and required self-regulators to justify to a court, not to the regulatory agency, that their regulatory acts with anticompetitive consequences were necessary to the regulatory scheme. As noted earlier, however, the results are understandable if viewed in their historical context. First, as a matter of general history, protection of the policies embodied in the antitrust laws have been identified by the federal courts as in their special domain for nearly a century.¹¹⁰ Federal regulatory agencies have been viewed as inadequate¹¹¹ and sometimes suspect¹¹² keepers of the procompetitive ideal embodied in the antitrust laws. Second, regarding securities regulation in particular, both the actual regulatory scheme and the performance of those acting within it gave much justification for judicial skepticism about the attention being paid to the delicate balancing needed to properly monitor self-regulatory conduct for compatibility with the antitrust ideal.

C. Congressional Action—1970-1975

During the period between the decisions in *Thill Securities* (1970) and

110. See, e.g., *Thill Securities Corp. v. New York Stock Exch.*, 433 F.2d 264, 273 (7th Cir. 1970), cert. denied, 401 U.S. 994 (1971) ("[I]t should be remembered that the courts of the United States have over the years become the repository of antitrust expertise.").

111. See, e.g., *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321, 352 (1963) ("Although the comptroller was required to consider the effect upon competition in passing upon appellees merger application, he was not required to give this factor any particular weight . . .").

112. See, e.g., *Thill Securities*, 433 F.2d at 273 ("[W]e . . . note that the history of United States regulatory agencies in general seems usually to record an ever growing absence of the spirit required for vigorous enforcement of the antitrust laws.").

Ricci (1973), while the courts were struggling to resolve both the jurisdictional and substantive questions concerning securities industry self-regulation and the antitrust laws, the matter was being hotly debated in Congress as well.¹¹³

At the same time, the NYSE had also been prompted to do its own self-examination into the self-regulatory shortcomings that led to the crisis of the late 1960s. The examination took the form of a study directed by William McChesney Martin, Jr. The "Martin Report," which was published by the Board of Governors of the NYSE in August 1971,¹¹⁴ addressed, among other matters, the question of antitrust immunity for self-regulatory organizations. Stating that the "Court decisions . . . [had left] the question of anti-trust exemption for exchanges far from clear,"¹¹⁵ the report recommended that the exchanges be given limited immunity under the antitrust laws, that immunity to be coextensive with the SEC's oversight powers over the exchanges:

[I]t is recommended that the Exchange ask the Congress to enact legislation granting all registered national securities exchanges *certain immunity under the anti-trust laws*. The scope of the immunity granted to the exchanges should be coexistent with the scope of the Securities and Exchange Commission's control of the exchanges under the Exchange Act, so that no action or omission by a registered national securities exchange in performing any of its duties of self-regulation under the Exchange Act *which are subject to review by the Securities and Exchange Commission* could give rise to any claim under the anti-trust laws.¹¹⁶

In the House and Senate hearings that commenced contemporaneously with the publication of the Martin Report, the NYSE's antitrust proposal was sharply debated. The SEC, not surprisingly, favored the recommendation, at least insofar as it recognized the primacy of the SEC's role in reconciling the securities industry regulatory scheme with the antitrust laws.¹¹⁷ Just as predictably, the Antitrust Division of the Justice Department strongly opposed the NYSE's proposal.¹¹⁸ Contending that the necessity test articulated in *Silver* was "a reasonable judicial approach,"¹¹⁹ the Justice Department described

113. See *supra* text accompanying notes 54-57.

114. W. MARTIN, *THE SECURITIES MARKETS: A REPORT WITH RECOMMENDATIONS* (August, 1971). The Martin Report is reprinted as Appendix NN to the *Study of the Securities Industry: Hearings Before the Subcomm. on Commerce and Finance of the House Comm. on Interstate and Foreign Commerce*, 92nd Cong., 1st Sess. 3189 (1971) [hereinafter *House Study Hearings—1971*]. The citations to the report will be to the page numbers of appendix NN of the House Study Hearings.

115. *House Study Hearings—1971*, *supra* note 114, at 3209 (appendix NN).

116. *Id.* (emphasis added).

117. William J. Casey, then Chairman of the SEC, testified as follows: "Accommodation of the general national policy favoring competition with the need for effective regulation of a particularly sensitive segment of the economy—the securities markets—was entrusted by the Congress to the Commission in the Securities Exchange Act of 1934." *Securities Industry Study, Hearing Before the Subcomm. on Securities of the Senate Comm. on Banking, Housing and Urban Affairs*, 92d Cong., 1st Sess. 99 (1971) (testimony of William J. Casey) [hereinafter cited as *Senate Study Hearings—1971*].

118. See Statement of the United States Department of Justice, reprinted in *House Study Hearings—1971*, *supra* note 114, at 3135 (appendix LL).

119. *Id.* at 3155.

the necessity test as relating to the conduct of the self-regulatory organizations. The Department rejected any meaningful role for the SEC in resolving the antitrust issues.¹²⁰

The first legislative round was won by the proponents of the Justice Department views. In the hearings, one influential member of the subcommittee, Congressman Eckhardt, observed that he "would not be willing as a Congressman to submit to the SEC the final determination of what Congress intended to exempt from antitrust action."¹²¹ Following his lead, the report issued by the House at the close of the 1971-72 hearings¹²² rejected the NYSE's immunity proposal and squarely endorsed the conduct-necessity test set down in *Silver*. The SEC's role in the decisional process was relegated to that of amicus.¹²³

The exchanges suggest that any challenge to the validity of exchange rules should be made to the SEC, with the ultimate right to appeal from there to the courts. The Subcommittee believes, however, that the better procedure is for the Federal district court to determine the issue de novo after having invited, and hopefully received, the views of the Securities and Exchange Commission and the Antitrust Division of the Department of Justice.¹²⁴

Among the subcommittee's reasons for rejecting the primacy of the SEC was that the Commission's expertise did not include concern for competitive impacts, and the federal courts' did.¹²⁵ Addressing the vulnerability of self-regulatory organizations to antitrust liability, the subcommittee suggested that such fears were largely unfounded as long as the self-regulator was doing what it was supposed to do—protect the public—and not what it was sometimes in-

120. *Id.* at 3155-56. It argued that the regulatory expertise of the SEC was in the area of customer protection, not economic control. As a harbinger of the more general deregulatory drive now in vogue, the Justice Department used the specific problem of SEC regulatory involvement to make a broadside attack on economic regulation in general:

Transforming the Commission into an economic regulator patterned after the ICC and CAB would not only dramatically change the character of the agency, but, if past experience with economic regulation is any guide, smother whatever innovative impulses reside in the industry under a blanket of administrative delay and complexity.

Id. at 3156. The testimony was sometimes emotional. Morris A. Schapiro, president of a non-NYSE member firm, said that granting the NYSE proposal for antitrust immunity would be a "shocking betrayal of . . . investors." *Id.* at 2987. Sometimes the debate touched on issues of broader significance than simply whether the exchanges should have antitrust immunity. Reflecting a growing national disillusionment with government by regulatory agency, Congressman Eckhardt of Texas, in discussing the SEC's role, observed that he was "becoming more and more . . . inclined less and less to entrust basic questions of policy to a commission." *Id.* at 3113.

121. *Id.* at 3112. His statement was later endorsed by the entire subcommittee in its report. SECURITIES INDUSTRY STUDY, REPORT OF THE SUBCOMM. ON COMMERCE AND FINANCE OF THE HOUSE COMM. ON INTERSTATE AND FOREIGN COMMERCE, H.R. REP. NO. 1519, 92d Cong., 2d Sess. 161 (1972).

122. H.R. REP. NO. 1519, *supra* note 121. The report disclosed that the hearings compiled 4,600 pages of testimony and exhibits and heard 87 witnesses. See *id.* at iii (letter of transmittal from the subcommittee to the full committee, August 23, 1972).

123. *Id.* at 160-61.

124. *Id.* at 156.

125. *Id.* at 163-64.

clined to do—protect the economic self-interest of its members.¹²⁶

The Senate likewise initially flatly rejected granting antitrust immunity to the self-regulatory organizations.¹²⁷ As was true in testimony to the House subcommittee, the Senate subcommittee heard little in support of the immunity proposal and much to the contrary. The Senate committee report, published in early 1973,¹²⁸ contained an extensive discussion of the antitrust problems. The necessity test, as described in the report (which included a discussion of cases from *Silver* to *Thill Securities*), also focused on the conduct of the self-regulator, and not on the question of immunity from antitrust attack. In so doing, the Senate report also flatly rejected any meaningful role for the SEC in addressing antitrust questions, commenting favorably on *Thill Securities* and on *Ricci*, which had been decided one month before the report was issued:

Anti-competitive conduct of self-regulatory bodies is immune from antitrust attack only if the conduct is necessary to make the statutory scheme of regulation work and then only to the minimum extent necessary. This immunity is not increased or broadened in the event that the action in question is subject to SEC review or even if it is in fact approved by the SEC. *The SEC has no power to immunize anti-competitive self-regulatory conduct from the operation of the antitrust laws.*¹²⁹

The Senate subcommittee, like the House's, therefore, squarely rejected the Martin Report recommendation, and like the House endorsed the judicial decisions that placed self-regulatory conduct under de novo judicial scrutiny.

As noted, however, the Senate and House hearings of 1971-72 and the reports written at their conclusion did not address the antitrust questions merely in the abstract. Specific anticompetitive conduct, particularly of the NYSE, was discussed and frequently condemned in testimony before both Houses and in the media.¹³⁰ Because particular allegedly anticompetitive NYSE practices were of so much concern in the congressional hearings, the initial Senate legislation brought forward was directed at such conduct, specifically the NYSE's restrictions on membership and its fixed commission rate structure.¹³¹ A later Senate measure addressed the NYSE's rule banning off-exchange trading of NYSE listed stocks.¹³² The House sought to address all the reform elements

126. *Id.* at 165.

127. SECURITIES INDUSTRY STUDY—1973, *supra* note 15, at 227.

128. SECURITIES INDUSTRY STUDY—1973, *supra* note 15.

129. *Id.* at 227.

130. See, e.g., *Antitrust Aide Sees End of Fixed Rates on Stock Fees, Threatens Court Action*, Wall St. J., November 6, 1972, at 2, col. 3; *Hart Threatens to Call Hearings on Legality of Fixed Broker Fees: Senate Antitrust Unit Head Says Big Board System, With Aid of SEC, Is Stifling Competition*, *id.*, June 2, 1972, at 5, col. 2; *Rep. Moss Assails Curb on Big Board Members Trading Over-Counter . . .*, *id.*, Feb. 25, 1972, at 6, col. 2. See also *House Study Hearings—1971*, *supra* note 114, at 2986-87 (testimony of Morris Schapiro). Schapiro described the NYSE efforts to keep Exchange-listed securities off the electronic over-the-counter trading system known as NASDAQ.

131. Wall St. J., Feb. 20, 1973, at 3, col. 1.

132. See generally Wall St. J., Dec. 12, 1973, at 3, col. 1.

in one bill.¹³³ Other events of 1973¹³⁴ overtook securities legislation, however, and although the Senate actually passed the bills that banned fixed commissions and certain restrictions on membership, the House did not take up the measures in 1973. Likewise in 1974, securities reform legislation failed to come to a vote in the House although again it succeeded in the Senate.¹³⁵

By 1975 much had changed on the regulatory landscape even in the absence of affirmative legislation, perhaps as a result of all the publicity and prodding emanating from the congressional studies. Of importance to the antitrust issues, the SEC, which had been criticized for years for being far too tame a regulator of industry anticompetitive practices, had flexed some regulatory muscle and had ordered, on its own authority, the ending of NYSE fixed commissions by May 1, 1975.¹³⁶ Therefore one of the most, if not *the* most, controversial of the NYSE's anticompetitive regulatory practices had already been abolished by the time Congress, in 1975, once again acted to reform the structure of the securities industry. Perhaps more significantly, in the years spanning the congressional hearings, the SEC assumed generally a far more active role in reviewing the competitive practices of the industry than it had previously assumed.¹³⁷ By 1975, therefore, Congress could actually envision the SEC as having the potential to oversee self-regulatory conduct with a view toward competitive as well as regulatory concerns.

This change was reflected in the Securities Acts Amendments of 1975, signed into law on June 4, 1975.¹³⁸ The legislation, which with minor revisions was the Senate's version of the bill¹³⁹ directed the SEC to take a central role in addressing the competitive needs of the securities industry. As stated by the Senate committee report, "[the bill] is designed to force the Commission to focus with particularity on the competitive implications of each regulatory requirement."¹⁴⁰ The amendments:

would lay the foundation for a new and more competitive market system, vesting in the SEC power to eliminate all unnecessary or inappropriate burdens on competition while at the same time granting to that agency complete and effective powers to pursue the goal to centralized trading of securities in the interest of both efficiency and

133. H.R. 5050, 93d Cong., 2d Sess. (1973).

134. The energy crisis and the growing concern over Watergate were two items of concern that pushed much other legislation aside. *Wall St. J.*, Nov. 14, 1973, at 12, col. 2.

135. The Senate bill was S. 2519, 93d Cong., 2d Sess. (1974). Senator Williams, the sponsor of the Senate legislation, attributed the bill's failure to intense lobbying by the NYSE and the securities industry generally. *Wall. St. J.*, Dec. 6, 1974, at 5, col. 2.

136. The SEC undid the fixing of commissions first by issuing a series of releases declaring its intentions to do so, followed by promulgating of Rule 19b-3. Exchange Act Rel. No. 11203, Jan. 23, 1975.

137. These efforts are recited in the Senate report accompanying the Senate's passage of The Securities Acts Amendments of 1975. S. REP. NO. 29, *supra* note 6. They included in addition to the unfixing of commissions already noted, the development of a composite tape for reporting the trades in listed securities, the assistance in the establishment of a national clearing system, and uniform net capital requirements.

138. Pub. L. No. 94-29, 89 Stat. 97 (codified in scattered sections of 15 U.S.C.).

139. S. 249, 94th Cong., 1st Sess. (1975).

140. S. REP. NO. 29, *supra* note 6, at 14.

investor protection.¹⁴¹

The Act did not outlaw specific anticompetitive practices, placing responsibility to review such practices in the SEC. The Senate report stated:

[R]ather than amending the Exchange Act to eliminate particular, enumerated barriers to competition, the most effective way to foster competition would be to *charge the Commission with an explicit obligation to eliminate all present and future competitive restraints* that cannot be justified by the purposes of Exchange Act. Following this pattern, various sections of [the Senate Bill] would direct the Commission to remove existing burdens on competition and to refrain from imposing, or permitting to be imposed, any new regulatory burden on competition "not necessary or appropriate in furtherance of the purposes" of the Exchange Act.¹⁴²

At the same time, however, the Senate was careful to note that enhancement of competition might not always be the primary concern of the Commission. The task of the Commission was not to justify its approval of self-regulatory actions as being the "least anti-competitive manner of achieving the regulatory objective,"¹⁴³ but rather "to balance, against other regulatory criteria and considerations, the competitive implications of self-regulatory and Commission action"¹⁴⁴

The Senate also spoke to the question of jurisdiction. After stating that the Commission's obligation in reviewing self-regulatory conduct was to "weigh the competitive impact in reaching regulatory conclusions,"¹⁴⁵ the report went on to say:

The manner in which [the SEC] does so is to be subjected to judicial scrutiny upon review in the same fashion as are other Commission determinations, with no *less* deference to the Commission's expertise than is the case with other matters subject to its jurisdiction.¹⁴⁶

141. *Id.* at 2.

142. *Id.* at 13 (emphasis added).

143. *Id.*

144. *Id.* "[T]he Commission's responsibility would be to balance the perceived anti-competitive effects of the regulatory policy or decision at issue against the purposes of the Exchange Act that would be advanced thereby and the costs of doing so." *Id.*

145. *Id.*

146. *Id.* (emphasis added). Emphasizing that the antitrust determination by the courts would occur in the course of a review of an SEC decision, not self-regulatory action, the report again stated, on the next page:

S. 249 is designed to force the Commission to focus with particularity on the competitive implications of each regulatory requirement. For example, in promulgating its own rules under Section 23(a) and in reviewing proposed self-regulatory rules under Section 19(c), the Commission would be required to make specific findings as to the justification for any limitation on, or restraint of, competition that would be involved. On review, such findings, to the extent they are based upon evidentiary facts, would be subject to a searching and careful inquiry by the Court of Appeals to determine whether they are supported by substantial evidence.

Id. at 14.

A most telling indication of the Senate's (and presumably Congress') attitude toward the SEC's role in resolving antitrust questions was that the 1975 Senate report omitted what it had included in the report accompanying the 1974 version of the bill. The 1974 version expressly addressed the immunity question:

In addition to statutorily mandating the SEC to give due regard to competition, the 1975 Act Amendments significantly revised the regulatory relationships between the SEC and the registered securities exchanges, making the SEC's power over such exchanges comparable to its power since 1938 over registered securities associations.¹⁴⁷ The anomalous disparity of regulatory reach was therefore ended, and more importantly, the revisions to the Act equipped the Commission with the power to regulate comprehensively all aspects of self-regulatory conduct. The registered securities exchange's rule proposals, rule changes, and disciplinary actions were subjected for the first time to SEC oversight and review.¹⁴⁸

The new regulatory framework established by the 1975 Act Amendments provided a statutory basis for more sensible solutions to the antitrust-self-regulatory conflict than those that had been offered by the courts in the pre-amendment period. Because, under the new framework, the SEC's oversight authority over virtually all regulatory aspects of self-regulatory conduct was either reaffirmed or established, the development of problems such as that present in *Silver*, in which SEC authority to review a self-regulatory rule enforcement action was lacking, would be unusual.¹⁴⁹ To the extent, then, that

The Committee believes that the standards enunciated by the Supreme Court in *Silver v. New York Stock Exchange* and *Ricci v. Chicago Mercantile Exchange* provide a sound basis for reconciling the two statutory schemes. Indeed, in drafting [the 1974 bill], the Committee assumed that the provisions of the bill would be interpreted in accordance with the basic principle enunciated in *Silver* that no repeal of the antitrust laws with respect to the conduct of self-regulatory organizations would be implied unless such repeal were "necessary to make the Exchange Act work, and even then only to the minimum extent necessary." *Although the bill substantially expands the scope of the SEC's oversight and regulatory powers and specifically directs that agency to take competitive factors into account in exercising those powers, the Committee does not intend thereby to confer general antitrust immunity on the self-regulatory organizations with respect to conduct subject to the SEC's oversight.* In the Committee's view, it is essential that the antitrust courts retain their jurisdiction to make the ultimate accommodation between antitrust principles and the powers and actions of the self-regulatory organizations. The Committee is certain that in doing so, the courts will carefully consider the SEC's views on the relationship between the action or rule at issue and the effectuation of the purposes of the Exchange Act. Such consideration would not, however, in any way affect the courts' ultimate jurisdiction in appropriate cases to make a de novo determination as to whether self-regulatory conduct, irrespective of whether it has been approved or required by the SEC, constitutes an unreasonable restraint on competition which cannot be justified as necessary to protect the achievement of the aims of the Exchange Act.

NATIONAL SECURITIES MARKET SYSTEM ACT OF 1974, REPORT OF THE SENATE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS, S. REP. NO. 865, 93d Cong., 2d Sess. 11 (1974) (emphasis added). The excision of this passage from the 1975 report suggests that Congress, while stopping short of legislatively immunizing self-regulatory conduct from judicial scrutiny, was establishing for antitrust issues the same decisional relationship that existed with regard to the enforcement of the federal securities laws vis-a-vis the exchanges.

147. For a detailed description of the changes wrought by the 1975 Act Amendments, see Note, *SEC Regulation as a Pervasive Regulatory Scheme*, 44 FORDHAM L. REV. 355, 368, 369 (1975). The author of the note points out that the Amendments effectively eliminated the disparity in the SEC's regulatory oversight of the exchanges and the NASD.

148. Securities Acts Amendments of 1975 (amending §§ 6(b)(8), 19(b), 19(e) of the Exchange Act, 15 U.S.C. §§ 78f(b)(8), 78s(b), (c), (e) (1981)).

149. One commentator has noted that the regulatory scheme established by the 1975 Act Amendments still offers opportunities for self-regulatory organizations to engage in unjustified anticompetitive acts under the guise of self-regulation. See Linden, *supra* note 63, at 231. There are, unquestionably, holes in the regulatory scheme. For example, although §§ 19(b)(1)-(3) of the

absence of pervasiveness accounted for the *Thill Securities* decision, the 1975 Act Amendments would require a contrary result. But *Thill Securities*' holding rested on more than absence of pervasiveness of the regulatory scheme. It also emphasized the SEC's lack of expertise to adjudicate antitrust issues. Since the obligation of the SEC to consider effects on competition in conducting its oversight function was made clear in the Amendments and in the legislative reports, the quality of the SEC's review could no longer be lightly dismissed, as it had been in *Thill Securities*, as being irrelevant to antitrust matters. The peculiar results of *Ricci*, in which agencies such as the SEC were to perform little more than a limited, artificially circumscribed function of fact finder and were not to determine the significant legal implications of the facts as found, arguably also would not be justified under the new regimen.

D. Post Amendment Decisions: Gordon v. NYSE; United States v. NASD—June, 1975

To the new statutory scheme created by the 1975 Act Amendments were added two significant Supreme Court decisions, decided barely three weeks after the passage of the Amendments. (The Amendments were passed on June 4, the cases decided on June 26, 1975.) While those decisions obviously could not have been and were not decided on the basis of the new law, they clearly reflected the changes that had taken place in the legislative and administrative climate since the decisions in *Thill Securities* and *Ricci* earlier in the decade. They recognized the significance of the SEC's oversight powers to the question of antitrust immunity and implicitly recognized the jurisdiction of the SEC to make decisions regarding the antitrust question.

1. *Gordon v. NYSE*¹⁵⁰

Gordon involved the NYSE's fixed commission rate schedule, which had been abolished by SEC decree by the time the case was decided. Unlike *Silver*, *Gordon* involved an Exchange action over which the SEC had been given explicit review authority by the original Exchange Act. There was evidence that for some years before the case was heard, the SEC actively had exercised its review authority with regard to such "price fixing." The district court granted the NYSE's motion for summary judgment¹⁵¹ on the question whether the NYSE's schedule violated the antitrust laws, and the court of ap-

Exchange Act, 15 U.S.C. § 78s(b)(1)-(3) (1976 & Supp. V 1981), provide for the filing of self-regulatory rule proposals and changes with the SEC and for SEC approval or disapproval of same, and § 19(d), 15 U.S.C. § 78s(d) (1976 & Supp. V 1981), provides for SEC review of certain self-regulatory actions, including discipline of members, denials of memberships of participation, or "limit[ations on] any person in respect to access to services offered" by the self-regulatory organization, no section specifically provides for SEC review of self-regulatory enforcement of its rules. As a practical matter, however, the scope and involvement of the SEC in self-regulatory matters is such that a risk of substantial self-regulatory activity with any kind of legitimate purpose falling outside the scope of SEC review is small.

150. 422 U.S. 659 (1975).

151. *Gordon v. New York Stock Exch.*, 366 F. Supp. 1261 (S.D.N.Y. 1973).

peals affirmed.¹⁵² The Supreme Court sustained the two lower courts, applying the necessity test of *Silver* to the question of *immunity*, rather than to the question of *conduct*. In so doing, the Court rejected the contention of the Department of Justice, appearing as amicus, that the critical question was whether, as a question of fact, the challenged *conduct* (price fixing) was necessary to the operation of the Exchange Act. Rather, said the Court, the problem was "whether antitrust *immunity*, as a matter of law, must be implied in order to permit the Exchange Act to function as envisioned by Congress."¹⁵³

The Court then indicated the factors relevant to a determination of the immunity question: (1) the existence of explicit SEC authority to review and regulate the exact conduct in question—here the fixing of commissions; (2) the *actual active* exercise of that oversight authority by the SEC; and (3) the expertise of the SEC in balancing competitive and regulatory concerns.¹⁵⁴ Since these factors were present,¹⁵⁵ "permitting courts . . . to conduct their own antitrust proceedings would conflict with the regulatory scheme authorized by Congress" ¹⁵⁶

In *Gordon* the Court declined to rule whether the same result would obtain without an explicit grant to the federal regulator of oversight authority concerning particular type of conduct. Although the *Gordon* Court did not decide whether a pervasive but more general grant of oversight authority to the SEC over NYSE conduct generally (such as was given by the 1975 Act Amendments) would have justified the finding of an implied repeal, the Court did make such a ruling in the companion case, *United States v. NASD*. The Court somewhat disingenuously distinguished *Gordon* from *Thill Securities* (which also at least indirectly had involved the fixing of commissions) by noting that *Thill Securities* was devoid of a clear record concerning the *actual exercise* of oversight authority by the SEC.¹⁵⁷

In his concurrence Justice Douglas made clear that "mere existence of a statutory power of review by the SEC over fixed commission rates [could not] justify immunizing those rates from antitrust challenges."¹⁵⁸ Only the active aggressive exercise of its oversight powers by the SEC allowed him to concur in the opinion.

The concurrence of Justices Stewart and Brennan, however, rested on a completely different basis. Their decision rested on the conduct-necessity test,

152. *Gordon v. New York Stock Exch.*, 498 F.2d 1303 (2d Cir. 1974).

153. *Gordon*, 422 U.S. at 688 (emphasis added.)

154. *Gordon*, 422 U.S. at 689-90.

155. During the time when the *Gordon* price fixing took place, the Exchange Act specifically authorized the SEC "to supervise the Exchanges 'in respect of such matters as . . . the fixing of reasonable rates of commission.'" Section 19(b)(9) of the Exchange Act, 15 U.S.C. § 78s(b)(9) (repealed 1975).

156. *Gordon*, 422 U.S. at 690.

157. *Id.* at 687. That distinction was found to be without substance by the district and appellate court that finally disposed of *Thill Securities* long after *Gordon* was decided. *Thill Securities Corp. v. New York Stock Exch.*, 473 F. Supp. 1364 (E.D. Wis. 1979), *aff'd*, 633 F.2d 65 (7th Cir. 1980). The courts ruled that the SEC's active oversight immunized the NYSE's anti-rebate scheme from antitrust attack.

158. *Gordon*, 422 U.S. at 691-92.

and they did not find that the statutory grant of oversight power to the SEC, even if actively exercised, immunized the NYSE from antitrust attack. Rather, they inferred from the Exchange Act's granting to the SEC of authority to supervise NYSE fixed commissions, that Congress implicitly had authorized the conduct of price fixing. Price fixing therefore did not violate the antitrust laws, because the *conduct* had been found by Congress to be necessary to make the Exchange Act work.¹⁵⁹

2. *United States v. NASD*

*United States v. NASD*¹⁶⁰ went even further than *Gordon*, because the statutory provisions governing *United States v. NASD* provided no explicit grant of oversight authority to the SEC regarding the challenged conduct. Rather, the SEC's oversight powers came from the more general and pervasive grant of authority over all NASD conduct given to the SEC by the Maloney Act. The case principally involved allegations that several mutual funds had engaged in anticompetitive conduct among and between themselves concerning resale agreements. It also contained one charge of antitrust violation against the NASD for encouraging its members to place restrictions on the secondary market for certain mutual fund shares.¹⁶¹ The evidence indicated that the SEC exercised its review and oversight authority over the NASD's action in an ongoing but informal manner. As already noted, the statutory scheme provided for pervasive SEC authority to review NASD conduct. The Court found that the NASD's activities were immunized from antitrust attack by the SEC's statutory supervisory authority.¹⁶² Said the Court: "[T]he investiture of such pervasive supervisory authority in the SEC suggests that Congress intended to lift the ban of the Sherman Act from association activities approved by the SEC."¹⁶³

United States v. NASD was decided by a simple five to four majority with no concurring opinions and no indication that any Justices in the majority disagreed with Justice Powell's reasoning. Justice Stewart's participation in the majority, in light of his views expressed in *Gordon*, is difficult to understand and raises questions about the vitality of the holding in the case. In his concurrence in *Gordon* he found that even the more explicit grant to the SEC

159. *Id.* at 692-93.

160. 422 U.S. 694 (1975).

161. The Department of Justice originally attacked both the NASD's rules and its conduct. Subsequently, it abandoned its attack on the NASD rules, but continued to allege that the NASD's over-all course of conduct violated the Sherman Act. *Id.* at 730-32 & n.43.

162. The authority was found in two statutes: the Investment Company Act of 1940, ch. 686, 54 Stat. 789 (1940) (codified as amended at 15 U.S.C. §§ 80a-1 to -64 (1976 & Supp. V 1981)); and the Maloney Act, ch. 677, 52 Stat. 1070 (1938) (codified as amended at 15 U.S.C. § 78o-3 (1976)).

163. *NASD*, 422 U.S. at 733. One commentator has called the *Gordon* and *NASD* decisions the "nadir of Supreme Court enforcement of antitrust law in the securities industry." Linden, *supra* note 63, at 211. That view is too harsh if assessed in light of the needs of a self-regulatory body to operate effectively under the antitrust laws. As the foregoing discussion discloses, and as Mr. Linden himself recognizes, the *Gordon* and *NASD* decisions are only explainable in their historical contexts and as a function of the combined congressional and judicial effort to find a *modus vivendi* for self-regulation.

of supervisory authority over the NYSE's conduct in that case did not immunize the NYSE from antitrust challenge.

III. THE 1975 ACT AMENDMENTS AS A MODEL FOR ACCOMMODATING THE ANTITRUST AND SELF-REGULATORY POLICIES

Although the decision in *Gordon* and *United States v. NASD* were not, and obviously could not have been, decided on the basis of the 1975 Act Amendments, the rationale for antitrust immunity provided by those cases has melded nicely with the 1975 Amendments to provide a framework for an accommodation of securities industry self-regulation with the antitrust laws. The framework for such accommodation, prescribed by the Supreme Court in *Gordon* and *NASD* and provided by Congress in the 1975 Act Amendments, has certain critical features: First, the framework requires a federal scheme of regulation that officially recognizes and encourages securities industry self-regulatory organizations to establish their own rules of conduct, their own standards, and their own disciplinary mechanisms.¹⁶⁴ Second, the framework must include a federal agency (the SEC) statutorily charged with the responsibility to review the activities of self-regulatory organizations to ensure consistency with the regulatory scheme and to minimize the anticompetitive impacts of self-regulatory conduct.¹⁶⁵ Finally, there must be allowance in the regulatory scheme for judicial review of the decisions of the SEC to assure that its oversight of the self-regulatory organizations is consistent both with the statutes establishing the regulatory scheme and with the antitrust laws. With these features present, the self-regulatory activities can occur in a legal framework that removes the threat of antitrust penalty, and at the same time, provides assurance that unnecessary anticompetitive conduct will be minimized.

A. *The Jurisdictional Question*¹⁶⁶

Neither the amended Exchange Act nor the 1975 cases provide or imply that the courts are not still the ultimate determiners of antitrust violations. The Exchange Act as amended provides no express exemption, and wisely not,

164. A congressional grant of substantial regulatory authority to private organizations without the addition of a federal regulatory overseer would almost certainly violate the constitutional prohibition against the delegation of legislative authority. See *A.L.A. Schechter Poultry Corp. v. United States*, 295 U.S. 495 (1935). Indeed, one arguable consequence of *Schechter* was the redirection of delegated legislative authority to federal agencies with what then became an increasingly cumbersome and insensitive federal bureaucracy. The thesis of this Article is that delegation to the private sector, if done on the securities industry model, would not only avoid the constitutional problems, but would effectively address the antitrust problem as well.

165. Justice Powell's majority opinion in *United States v. NASD*, 422 U.S. 730 (1980), emphasized that the SEC, in overseeing NASD conduct, "repeatedly has indicated that it weighs *competitive concerns* in the exercise of its continued supervisory responsibility." *Id.* at 732.

166. The jurisdictional question only becomes relevant if it is raised by the defendant to the antitrust action, that is, the self-regulatory organization. Thus, for example, in *Taggares Co., Inc. v. New York Mercantile Exch.*, 476 F. Supp. 72 (S.D.N.Y. 1979), the district court heard and dismissed on the merits a claim against the New York Stock Exchange without mentioning the jurisdictional question. Presumably, the Exchange had not moved for a stay pending review by the CFTC, and the court did not consider a stay *sua sponte*.

because the power of judicial rebuke will act as a strong motivating force both to the self-regulators and to the SEC, to give due regard to antitrust concerns.¹⁶⁷ It should be equally clear, however, that as regards certain self-regulatory actions, the antitrust question is to be decided first by the SEC and afforded as much deference by the federal courts as would be any legal question decided by the SEC regarding the organic acts for which it is responsible.

The difficulty in resolving the jurisdictional question arises, in part, from the need to distinguish between various types of self-regulatory conduct. A self-regulatory organization's anticompetitive conduct may include variously the promulgation of a self-regulatory rule (as in *Gordon*), the enforcement of such a rule (as in *Silver*), or the ad hoc undertaking of extra regulatory activities that bear only marginal relationship to the agency's regulatory function. Depending upon which type of conduct is at issue in an antitrust action, the sequence in which the SEC and the federal courts will review the conduct will differ. For example, antitrust challenges to rules promulgated by self-regulatory organizations after prior approval by the SEC need not be referred to the SEC for first review—not because the agency has no jurisdiction, but because it has already exercised it. Under a statutory regimen established by the Exchange Act,¹⁶⁸ the SEC should have examined the propriety of the rule for both regulatory and antitrust purposes by conducting its own conduct-necessity analysis before approving the rule.¹⁶⁹

A different result follows antitrust challenges to a self-regulatory organization's actions taken to enforce its rules. Unlike the case of challenges to rules, in which the SEC has already had the opportunity to make an antitrust determination, challenges to rule enforcement actions generally will involve reviewing self-regulatory conduct *not* previously approved by the SEC. Under the 1975 Amendments, the SEC is afforded the first opportunity to decide whether the enforcement action taken by the self-regulating organization is a proper exercise of its self-regulatory function.¹⁷⁰ The SEC's review will include a "conduct-necessity" analysis, that is, a determination of the effect of the self-regulator's action on competition as well as its appropriateness to the effectuation of the regulatory scheme. Of course, the SEC determinations are subject to judicial review. When a self-regulatory organization undertakes allegedly anticompetitive actions that bear no colorable relationship to any legit-

167. Linden, *supra* note 63, at 236-38.

168. See also *Harding v. American Stock Exch., Inc.*, 527 F.2d 1366 (5th Cir. 1976). The case concerned an Amex rule regarding the delisting of stocks from its exchange and Amex's conduct in actually delisting a stock. The SEC had approved both the rule and Amex's conduct. Consequently, there was no need to bring the antitrust complaint first to the SEC, and the jurisdictional question was not even raised.

169. In *Gordon* the Court seemed to be employing such an analysis—that is recognizing that it was essentially reviewing the SEC's performance—without exactly saying so.

170. *Ricci* concerned conduct to enforce a rule, as did *Silver*. If *Silver* were relitigated today, the appeal of the denial-of-access issue would go directly from the self-regulatory organization to the SEC pursuant to § 19(d) of the Exchange Act as amended in 1975. Following the *Ricci* analysis, a court now deciding *Silver* would conclude that the federal regulatory agency had primary jurisdiction. But *Ricci* limited that jurisdiction to a decision about regulatory, not antitrust, law. See *Ricci*, 409 U.S. at 302. The proposal here is that the jurisdiction not be so limited.

imate regulatory function, there is no reason to refer the matter to the SEC in the first instance. In such cases, no serious concern exists that oversight of the regulatory scheme is being divided between the judiciary and the federal regulator because no matter touching legitimate regulatory conduct is at issue.¹⁷¹

B. The Immunity Question

Neither the 1975 Act Amendments,¹⁷² nor the *Gordon* and *NASD* cases, nor indeed any of the earlier cases, discussed the immunity question in terms of the distinction between immunity from penalty and immunity from judicial review. It is clear that without express statutory language exempting self-regulatory conduct from judicial review, such conduct is not completely shielded from judicial scrutiny on the antitrust issue even if the SEC has pervasive regulatory authority over self-regulatory conduct. Under the present Exchange Act, however, if the conduct complained of is of the sort for which a self-regulator had been statutorily required to seek prior SEC approval, such as for the promulgation of a self-regulatory rule, the seeking and obtaining of such approval should immunize the self-regulator both from *direct* judicial antitrust review of that conduct and from penalty.¹⁷³ If a person aggrieved by the approval of such a rule wishes to take an appeal, the judicial posture in which the case is heard is that of an appeal from an SEC decision, not a *de novo* antitrust complaint against the self-regulator. Using the criteria validated in *Gordon* and *NASD*, and now present in the Exchange Act, this result pertains because there is (1) a pervasive scheme of federal regulation of the self-regulatory organization's activities, including a requirement for SEC review of self-regulatory rule promulgations,¹⁷⁴ (2) a requirement that concern

171. Plaintiffs should not, however, be permitted by clever pleading to destroy agency jurisdiction.

172. In the 1971-1972 Senate hearings there was some discussion of changing the penalty for antitrust violations by self-regulating organizations from treble damages to single damages, *Senate Study Hearings—1971*, *supra* note 117, and the 1973 Senate Report left open the possibility that the problem could be dealt with that way. SECURITIES INDUSTRY STUDY—1973, *supra* note 15. The 1975 Act Amendments did not follow through on that recommendation, and recent efforts to revive the idea have fizzled.

173. Results such as that in *Fredrickson v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 389 F. Supp. 1151 (N.D. Ill. 1974), *vacated and remanded*, 525 F.2d 694 (7th Cir. 1975), in which the district court determined to conduct a *de novo* review of NYSE fixed commissions and to treat the SEC's actions in approving such commissions as of "essential assistance," but not as the action to be reviewed, would be improper.

The term "should" rather than "would" is used because, as noted earlier, the Supreme Court was seriously split on the question whether a general rather than explicit grant of supervisory authority to a federal regulatory agency over the activities of a self-regulatory agency would immunize the self-regulatory agency's actions. *See, e.g.*, *Jacobi v. Bache & Co.*, 520 F.2d 1231 (2d Cir. 1975), *cert. denied*, 423 U.S. 1053 (1976) (no immunity because SEC had declined to rule on the NYSE's conduct).

174. In other cases decided since *Gordon* and *NASD*, the authority under which the SEC acted had been provided explicitly in the original Exchange Act, so the "pervasiveness" issue did not need to be decided. *E.g.*, *Thill Securities Corp. v. NYSE*, 633 F.2d 65 (7th Cir. 1980) (fixed commissions); *Harding v. American Stock Exch.*, 527 F.2d 1366 (5th Cir. 1976) (delisting of stocks); *Shumate & Co. v. NYSE*, 486 F. Supp. 1333 (N.D. Tex. 1980) (off-board trading restrictions). Whether the "pervasive scheme," found to be sufficient by the Court in *NASD* to immunize self-regulatory conduct, would be found sufficient by today's Court cannot be predicted. It is clear that lower courts have not generously translated the holding of the *NASD* case to cases

for competitive impact be included in the SEC's reviewing function, and (3) actual meaningful review by the SEC. The presence of these factors should immunize the self-regulatory conduct from penalty (although not from relief) under the antitrust laws even if a court reviewing the SEC's approval of the rule reverses the SEC's decision. Such immunity, using the *Silver* "immunity necessity test," is necessary to effect the statutory scheme. Without such immunity, the self-regulators have no comfort that their efforts at regulation will not be stymied and perhaps seriously impaired by the draconian penalties visited on their regulatory efforts. In addition, the failure to confer immunity from penalty on self-regulatory rules approved by the SEC demeans the importance of the SEC's regulatory role and impairs the effectiveness of the SEC's stewardship of the regulatory scheme established by the federal securities laws.

As noted, for SEC review to confer immunity on self-regulatory conduct, the review needs to be *active*, and needs to result in a ruling by the SEC that is judicially reviewable.¹⁷⁵ The process of agency approval of self-regulatory rule proposals is contained in the revisions to the Exchange Act.¹⁷⁶ The SEC decision to approve self-regulatory rules is reviewed pursuant to standards set forth in section 25 of the Exchange Act.¹⁷⁷ Section 25 provides that the Commission's factual findings are conclusive if supported by substantial evidence, and that its decision should be overturned only if "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with the law; in excess of statutory jurisdiction, authority, or limitations, or short of statutory right; or without observance of procedures required by law." The critical point is that the court's function in these rule-review instances is to review the decision of

addressing immunity for one regulated entity, the American Telephone and Telegraph Co. They have found no congressional intent to confer immunity on the company for acts regulated by the Federal Communications Commission. *See, e.g.,* *Phonetele, Inc. v. AT&T*, 664 F.2d 716 (9th Cir. 1981); *Northeastern Tel. Co. v. AT&T*, 651 F.2d 76 (2d Cir. 1981), *cert. denied*, 102 S. Ct. 1438 (1982); *Sound, Inc. v. AT&T*, 631 F.2d 1324 (8th Cir. 1980); *Mid-Texas Communications Sys., Inc. v. AT&T*, 615 F.2d 1372 (5th Cir. 1980), *cert. denied sub nom. Woodland Tele. Corp. v. Southwestern Bell Tel. Co.*, 449 U.S. 912 (1980). The AT&T cases simply highlight the need for a clear statement of congressional intent in any legislation to establish self-regulatory organizations.

175. The SEC's shortcomings in this regard were one reason why the Second Circuit refused to immunize from antitrust review a NYSE rule concerning member firm treatment of service charges to customers. *See Jacobi v. Bache & Co.*, 520 F.2d 1231 (2d Cir. 1975), *cert. denied*, 423 U.S. 1053 (1976). The SEC had, in Judge Friendly's language, "consistently attempted to stay out of the controversy." *Id.* at 1237. That case arose before but was decided after passage of the 1975 Amendments. Presumably, under the Amendments the SEC no longer may voluntarily absent itself from such matters.

176. The revisions are found in § 19(b) of the Exchange Act, 15 U.S.C. § 78s(b) (1982). Under § 19(b) the SEC must publish for public comment any proposed rule or rule change of a self-regulatory organization, must allow for public comment, and must, in ordering approval or disapproval of the rule, make findings that the rule is consistent with the requirements of the Exchange Act. While there is no provision in this section for the SEC to consider the effect on competition of proposed self-regulatory rules, as noted earlier, those provisions appear elsewhere in the Exchange Act. 5 U.S.C. § 553(c) (1982) provides for publication by the agency of proposed rules in the Federal Register. Section 553(c) also requires a "concise general statement" of the basis and purpose for any rule adopted by the agency. Provision for the judicial review of agency decisions is found in § 704 and § 706 of the Act, 5 U.S.C. §§ 704, 706 (1982), which provide for the setting aside of final agency action that is arbitrary or capricious or an abuse of discretion.

177. Section 25(b)(4) of the Exchange Act, 15 U.S.C. § 78y(b)(4) (1982).

the SEC to determine whether the SEC's approval of the rule was rationally based, not to decide in a de novo review that the rule as implemented by the self-regulator has violated the antitrust laws.¹⁷⁸

If the allegedly violative conduct has not received prior agency approval, as, for example, a self-regulatory action to enforce a rule, then, in most instances, the SEC will have primary jurisdiction to determine whether such conduct was an appropriate exercise of self-regulatory authority and, therefore, did not violate the antitrust laws. The SEC's findings should be afforded weight by a reviewing court, but the very difficult question is whether SEC approval of the conduct should serve to immunize the self-regulator from antitrust penalty, as should be the case in challenges to rules. Different treatment may be justified because in the case of rule enforcement, the self-regulator would not have relied to its detriment on a prior agency approval; hence subjecting the self-regulatory organization to penalty, should a reviewing court reverse the SEC, would not be as disruptive to the SEC's regulatory authority as would be the case in rule approvals. Moreover, because (as is discussed below) the legal standard under which self-regulatory conduct is to be measured is that of reasonableness, only egregious self-regulatory conduct would be likely to cause either the SEC or the reviewing court to decide that the self-regulator had violated the antitrust laws.

C. The Conduct Question

Finally, one question remains: which test to self-regulatory conduct should the SEC and the courts apply? The conduct-necessity test, first articulated in *Silver*, is apposite. The Court there stated that the self-regulatory organization would be able to avoid antitrust sanction if it could demonstrate the *necessity* of the conduct to the regulatory scheme from which the organization derived its authority. As noted earlier, the Court in *Silver*, in reaching its determination as to necessity, did not reach the substance of the NYSE's action, and at most, that case established only that self-regulatory conduct that denied affected parties elementary due process could not be necessary to a regulatory scheme. Arguably, the "necessity" language of *Silver* should be read to create a reasonableness standard because it is probably impossible to demonstrate the factual necessity of each instance of self-regulatory conduct to a complex regulatory scheme. A modified rule of reason test is a more appropriate label.¹⁷⁹ To pass this test, a self-regulatory organization would have to show

178. Of course the proposed rule would have to be rationally related to the self-regulator's regulatory responsibility. Otherwise, even approval by the SEC should have no immunizing effect. In another context, this "ultra vires" aspect proved fatal to a claim of immunity. In *Cantor v. Detroit Edison Co.*, 428 U.S. 579 (1976), the Michigan Utility Commission's approval of free light bulb distribution by the public utility was determined by the court to be essentially an ultra vires act, according no immunity to the utility.

179. The term "modified rule of reason" is used by Linden, *see* Linden, *supra* note 63, at 191. Judge Friendly of the Second Circuit assumed that a modified rule of reason analysis was what *Silver* called for stating that the criteria for satisfying the rule were whether the self-regulatory rule was *germane* (not *necessary*) to the purposes of the Exchange Act and whether the rule was reasonable. *Jacobi v. Bache & Co.*, 520 F.2d 1231, 1238-39 (2d Cir. 1975), *cert. denied*, 423 U.S.

that the beneficial effects of the conduct to the statutory scheme outweighed the negative effects of the conduct on free competition. As noted earlier, this balancing is to be contrasted with the traditional rule of reason test applied to anticompetitive acts said to be "beneficial." The rule of reason analysis puts *competition* on both sides of the fulcrum, because under the traditional formulation the only benefit judicially recognized is that which furthers competition. Anticompetitive conduct normally will escape sanction only if its short-term anticompetitive effects are outweighed by long-term competitive benefits. The balancing test offered in *Silver* permits values other than competition to weigh in on one side of the scale. These values might include provision of services other than on a cost basis, prevention of improper trading practices, or prevention of fraud.

D. Self-Regulation in Other Industries

The focus of this Article has been on the accommodation between the antitrust laws and self-regulation in the securities industry. Such accommodation might be possible for other industries as well, that is, for industries not presently enjoying a statutory invitation to self-regulate under government agency supervision. The Supreme Court has shown little sympathy to assertions by nonstatutory self-regulators that their conduct should escape antitrust sanction when the purported motives for such conduct are public spirited. For example, in *National Society of Professional Engineers*,¹⁸⁰ the Court flatly rejected the Society's argument that, because its prohibitions against competitive bidding were motivated by a desire to assure high quality construction, its conduct did not violate the antitrust laws. Similarly, in *Maricopa County Medical Society*¹⁸¹ the Medical Society's claim that its maximum price fee schedule was designed to ensure affordable treatment rather than to fix prices, was rejected by the Court as a defense to an antitrust action brought against the society. A major weakness in the arguments made by quasi-self-regulators such as the National Society of Professional Engineers and the Maricopa Medical Society is that their self-regulatory efforts are largely "voluntary,"

1053 (1976). See also *Drayer v. Krasner*, 572 F.2d 348 (2d Cir. 1978) (Friendly, J.). Modifications of the rule of reason to account for values other than competition have enjoyed a tenuous existence in the lower courts for activities conducted by noncommercial groups. See, e.g., *Marjorie Webster Junior College, Inc. v. Middle States Ass'n of Colleges & Secondary Schools, Inc.*, 432 F.2d 650 (D.C. Cir.), cert. denied, 400 U.S. 965 (1970) (no antitrust violation for refusal of educational accrediting institution to accredit plaintiff); *Paralegal Inst., Inc. v. ABA*, 475 F. Supp. 1123 (E.D.N.Y. 1979) (ABA's accreditation program for paralegals is germane to the purpose for which the ABA exists). Since the Supreme Court, in *Goldfarb v. Virginia State Bar*, 421 U.S. 773 (1975), removed any blanket antitrust immunity for professional organizations as such, the rationale for finding an exemption for reasonable restraints has been pinned to a cryptic footnote in that case, *id.* at 788-89 n.17, in which the Court hinted that *some* practices of professional organizations might escape antitrust sanction when a similar practice in an ordinary group would not. While *Marjorie Webster* and the *Paralegal Institute* prevailed pursuant to a "germane to the purpose of the organization" standard, other defendants have not. E.g., *National Soc'y of Professional Eng'rs v. United States*, 435 U.S. 679 (1978); *Boddicker v. Arizona State Dental Ass'n.*, 549 F.2d 626 (9th Cir. 1977).

180. *National Soc'y of Professional Eng'rs v. United States*, 435 U.S. 679 (1978).

181. *Arizona v. Maricopa County Medical Soc'y*, 102 S. Ct. 2466 (1982).

rather than following from an official, comprehensive statutory scheme of regulation. A framework, such as that now present in the securities industry, would legitimize and protect the pro-public purpose efforts of such organizations and, therefore, prevent such conduct from being found a violation of the antitrust laws.¹⁸²

IV. CONCLUSION

The protection from antitrust attack afforded to self-regulatory organizations by their inclusion in a federal regulatory scheme is still far from clear, although, for securities industry self-regulators, the 1975 Act Amendments arguably have provided far more protection than had been available previously. Since *Silver's* announcement that no blanket immunity is available to such organizations and that immunity will be conferred only if necessary to the federal regulatory scheme, the courts have grappled with the "correct" application of the necessity test and the significance of that test to federal agency oversight authority. By its actions in the 1975 Amendments, giving the SEC more comprehensive review and oversight authority over registered securities exchanges and charging the SEC to extirpate unnecessary impediments to competition, Congress arguably decided that the involvement of the SEC in securities industry self-regulatory rulemaking should be almost dispositive of the immunity issue, and that the SEC's role in deciding antitrust questions should be judicially recognized. Given the public benefits derived from enlisting the self-regulatory efforts, the accommodation in the securities industry offers a model and a justification for expanding the use of this regulatory tool to other industries.

182. As regards the sorts of industries that might be amenable to government supervised self-regulation, there exists in the United States an impressive network of private standard-setting bodies that formulate tens of thousands of standards to be employed in industry. See Hamilton, *The Role of Nongovernmental Standards in the Development of Mandatory Federal Standards Affecting Safety or Health*, 56 TEX. L. REV. 1329 (1978). These organizations, which include thousands of members, enjoy no official government recognition, are not regulated or overseen by any federal agency, and as such are quite vulnerable to antitrust challenges to their activities. As the recent Supreme Court decision in *American Soc'y of Mechanical Eng'rs, Inc. v. Hydrolevel Corp.*, 102 S. Ct. 1935 (1982), demonstrates, such challenges are real and are of potentially devastating effect to the workings of such organizations. Some such organizations have escaped liability by demonstrating that their good faith efforts to promote health or safety were neither unreasonable nor exercised in a discriminatory manner. See, e.g., *Eliason Corp. v. National Sanitation Found.*, 614 F.2d 126 (6th Cir. 1980). See generally, Ponsoldt, *supra* note 65. These cases rescue defendants from antitrust liability by using a variant of the rule of reason analysis to condone restrictive conduct. They do not address immunity or jurisdictional questions because there is nothing in these organizations' existence that would provide a pretext for a discussion of these issues. There have been periodic efforts, either stemming from industry or initiated by Congress, to adapt the self-regulatory scheme of the securities industry to other industries, but these efforts have foundered either because they have been politically unfeasible (automotive safety) or because the industries involved have been unreceptive (broadcasting). See Levin, *supra* note 2. Under the Carter administration several industries were encouraged to initiate voluntary efforts at self-regulation. See U.S. REGULATORY COUNCIL, *REGULATORY REFORM HIGHLIGHTS: AN INVENTORY OF INITIATIVES, 1978-1980* 11 (1980). It is perhaps time to renew such efforts.

