Securities Law: Case Notes

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I. INTRODUCTION

A. An Important Confrontation: The Justice Department and the SEC

The question of the extent to which the securities industry, and particularly the stock exchanges, should be subject to the rules of competition as enforced under the antitrust laws is one of the most critical problems confronting the industry today.¹ The Justice Department and the Securities Exchange Commission (SEC), traditionally opposed in their views on the issue, have played increasingly important roles in the controversy in recent years. Through amicus curiae participation in private antitrust actions involving the securities industry, the two agencies have not only sharpened the divergence of opinion but have lent considerable effort and expertise to the dispute. Conflicting positions taken by the federal courts of appeals have also been instrumental in leading to a showdown in the United States Supreme Court.

The vehicle for this larger battle is Gordon v. New York Stock Exchange,² a case focusing primarily on the stock exchanges' minimum fixed commission rates. Despite the narrow focus of the factual issue in Gordon, the Supreme Court's resolution of the controversy is likely to have a significant impact on other exchange activities and other industries policed by regulatory agencies.

In Gordon, plaintiff brought a private antitrust action on behalf of himself and a class of small investors against the New York Stock Exchange (NYSE), the American Stock Exchange, and two representative member firms.³ He alleged that the exchanges' fixed minimum commission rate structure constituted a system of price discrimination and price-fixing in violation of the Robinson-Patman Act⁴ and the Sherman Act.⁵ In effect, the action constituted a broad-based

² 498 F.2d 1303 (2d Cir. 1974).
³ Merrill Lynch, Pierce, Fenner & Smith and Bache & Company, Inc.
⁵ Id. §§ 1, 2.
antitrust attack upon practices of the securities industry. Plaintiff sought injunctive relief, treble damages of $1.5 billion, plus interest, attorneys' fees of $10 million, and other costs and disbursements. The district court, granting defendants' motion for summary judgment and dismissing the complaint, declared that the minimum commission rate structure was not within the jurisdiction of an antitrust court because § 19(b) of the Securities Exchange Act of 1934 displaced judicial oversight with review power vested in the Securities Exchange Commission. The court also found that implied exemption from the Sherman Act is necessary if the SEC is to continue to perform its statutory function with respect to both rate-fixing and more generally, making the Exchange Act's scheme of regulation work in the manner intended by Congress. Affirming, the United States Court of Appeals for the Second Circuit held that the practice of fixing commission rates pursuant to § 19(b)(9) of the Exchange Act is immune from antitrust scrutiny.

Unless the exchanges' commission rate activities enjoy immunity from the antitrust laws, it would appear that such activities constitute per se antitrust violations. The commission rate structure clearly constitutes price-fixing, a per se violation of the Sherman Act unless an exemption is available. Because of this, the problem confronting the court of appeals in Gordon was not whether the alleged practices were anticompetitive, but whether the antitrust laws were applicable to the exchanges' practices.

B. The Self-Regulatory Scheme

Since the Buttonwood Tree Agreement of 1792, which created the original cartel of securities dealers, NYSE members have operated under an agreement binding all members to give preference to one another and to charge non-members a minimum rate for their services. Similarly, under the present NYSE Constitution, members must charge all non-members a minimum commission rate for services involving securities transactions. Thus, the anticompetitive

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7 Because plaintiff's complaint was dismissed on the merits, the district court did not consider his motion for a class action determination. Gordon's Robinson-Patman claim was dismissed because the court did not find the securities to be "commodities" within the meaning of the Act.
9 498 F.2d 1303 (2d Cir. 1974).
12 NYSE Constitution, art. XV, § 1, found in NYSE Guide ¶ 1701 (1972).
practices complained of in *Gordon* are an institutionalized part of the operation of the securities industry.

The 1934 Act provides no express exemption from the antitrust laws for the stock exchanges. Section 19(b) does provide that the SEC is authorized to alter or supplement exchange rules in regard to the “fixing of reasonable rates of commission” if the SEC determines “that such changes are necessary or appropriate for the protection of investors or to insure fair dealings in securities.” Nonetheless, the Act makes the exchanges the principal promulgators and enforcers of rules governing the conduct of their members. The Act does require all exchanges, brokers, and dealers to register with the SEC. Once an exchange is registered, however, the Act authorizes it to adopt any rules “not inconsistent with this chapter and the rules and regulations thereunder.” This is the core of the self-regulatory feature of the securities laws. Thus, the role of the SEC has been primarily supervisory, not involving any active participation in the rule-making process. However, as the language of § 19(b) indicates, the SEC has more power over exchanges than it traditionally has exercised.

II. PREVIOUS CONFRONTATIONS

A. *Silver v. New York Stock Exchange*

The relationship of the securities regulatory scheme to the antitrust laws was first explored in *Silver v. New York Stock Exchange.* As *Gordon* correctly pointed out, “[a]ny analysis of the interrelation of the antitrust laws and the system of supervised exchange self-regulation . . . must begin with *Silver.*” In that case, a broker-dealer who was not a member of the NYSE sought treble damages for injuries to his business caused by the severing of his telephone connections with a number of member firms. The exchange action was not preceded by notice or an opportunity for a hearing or explanation. Plaintiff alleged violation of the Sherman Act, claiming that the action by the members of the NYSE constituted a collective refusal to deal (group boycott). The Supreme Court agreed, refusing to view the Securities Exchange Act of 1934 as a blanket antitrust exemption for the NYSE.

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16 Id. § 78f(c) (1970).
17 Recent developments in the SEC’s supervision of the rate structure suggest that the “passivity” on the part of the SEC has been abandoned. See text accompanying notes 59-60 infra.
19 498 F.2d at 1305.
In attempting to reconcile the conflict between the antitrust laws and the 1934 Act, the Court stressed that any repeal of the antitrust laws must be by implication since the 1934 Act contains no explicit exemption. Because repeal by implication is generally disfavored, the Supreme Court emphasized that "[r]epeal is to be regarded as implied only if necessary to make the Securities Exchange Act work, and even then only to the minimum extent necessary. This is the guiding principal to reconciliation of the two statutes."18

In applying this test to Silver's claims, the Court distinguished between the rules of the exchange and particular instances of their enforcement. The NYSE had argued that because the 1934 Act authorized the Commission to review and alter NYSE rules, judicial scrutiny of NYSE rulemaking would conflict with SEC jurisdiction. Although the Court intimated that there may be some validity to the NYSE argument when the exercise of antitrust jurisdiction might render ineffective the supervised self-regulatory scheme of the 1934 Act, this precise question was left unresolved by Silver.19 Instead, the Court determined that the NYSE had applied, rather than formulated, a rule, and that the SEC lacked jurisdiction to consider the individual applications of NYSE rules. If judicial scrutiny were not allowed, the Court reasoned, the antitrust function would not be performed at all in regard to the application of NYSE rules. Thus the principal question presented by Gordon—whether the availability of SEC review of exchange rulemaking will immunize these exchange activities from the antitrust laws—was left untouched by Silver.

B. Earlier Lower Court Decisions

In Kaplan v. Lehman Bros.,20 the activity complained of was not the manner in which a particular rule had been applied, but the existence of the rule itself. Kaplan was a shareholder's derivative suit and representative class action alleging that the NYSE's fixed commission rates constituted a price-fixing conspiracy in violation of the Sherman Act. It was the first antitrust action ever instituted against the fixed minimum commission structure—the same system attacked in Gordon. The district court granted judgment to the NYSE and its member firms. The court dismissed the complaint, noting that it had alleged a per se violation of the antitrust laws in contravention of the

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18 373 U.S. at 357.
19 "Should review of exchange self-regulation be provided through a vehicle other than the antitrust laws, a different case as to antitrust exemption would be presented." Id. at 360.
clear dictates of Silver, which made "it plain that action taken by the Exchange and its members, pursuant to its statutory authority to make rules, is not illegal per se under the Sherman Act."21 The district court attempted to distinguish the Silver holding by pointing out that Silver involved only the application of an Exchange rule, while Kaplan concerned an area subject to SEC review under § 19(b) of the 1934 Act. Because Kaplan was thought to be unlike Silver, the court refused to determine whether the challenged rule was necessary to make the Act work, as the Supreme Court had required in Silver.22 Affirming in a brief opinion, the Court of Appeals for the Seventh Circuit apparently agreed with the lower court that the necessity test of Silver need not be applied since the challenged rule was reviewable by the SEC.23

The Kaplan case received considerable criticism, both in the courts and by commentators.24 The Seventh Circuit implicitly retreated from its position in Kaplan in Thill Securities Corp. v. New York Stock Exchange.25 In that case, Thill claimed that the NYSE had violated the antitrust laws by prohibiting its members from sharing commissions with non-member brokers, allegedly constituting a restraint of trade.26 It was also alleged that the NYSE had discriminatorily applied the rule against some non-brokers and not against others. The court reversed a district court decision granting summary judgment for the Exchange and remanded the case for further consideration. The court held that Silver does not preclude the assertion of antitrust jurisdiction over NYSE rules merely because there is a possibility of SEC review. The Seventh Circuit emphasized that Silver allows only the minimum repeal of antitrust laws necessary to make the 1934 Act work.

21 250 F. Supp. at 564.
22 The district court also suggested that the danger of discriminatory action was far greater in situations like Silver's wire disconnection than in the administration of a fixed commission structure. 250 F. Supp. at 565.
23 In Kaplan, the Court of Appeals for the Seventh Circuit said:
[W]e do not construe the Sherman Act and the exchange act as showing a congressional intention to permit the maintenance of an antitrust prosecution of the exchange . . . based upon its action relating to the rates of commission to be charged by its members. Obviously, the fixing of commissions is one method of regulating commission rates. 371 F.2d at 411.
24 In a strenuous dissent to the Court's denial of certiorari in Kaplan, Chief Justice Warren referred to the Seventh Circuit's action as a "blunderbuss approach [falling] far short of the close analysis and delicate weighing process mandated by this Court's opinion in Silver." 389 U.S. at 957. See also Baxter, Johnson, supra note 1.
26 This is the NYSE's "anti-rebate" rule. NYSE Constitution, art. XV, § 1, supra note 12.

1975] CASE NOTES 149
It is important to note, for purposes of contrasting Thill with Gordon, that Thill found that SEC review of NYSE rules, as provided for in § 19(b) of the 1934 Act, does not in itself require automatic abstention by an antitrust court. The case clearly indicates, even though it directly concerned the anti-rebate rule, that minimum commissions are not totally immune from antitrust scrutiny. The rate structure is to be subject, at least in the Seventh Circuit, to the Silver necessity test.

III. RECENT CONFLICT OF OPINION: THRESHOLD IMMUNITY

A. The Vehicle for Decision. Gordon v. New York Stock Exchange

The Second Circuit court of appeals has adopted a view much different from that of the Seventh Circuit. Noting the Supreme Court's acknowledgement in Silver that if there were SEC jurisdiction to review a challenged rule, a "different case" might arise concerning antitrust exemption, the Second Circuit viewed Gordon as that different case. Distinguishing Silver on the ground that there was no possibility of SEC review of the disconnection of the telephone wires, the court felt that assertion of judicial oversight in Silver did not result in inconsistencies in the system of administrative regulation. In regard to the practice challenged by Gordon—the fixed commission rate structure—the court stressed that the availability of SEC review under § 19(b) of the 1934 Act removed the system from judicial antitrust scrutiny.

Perhaps not confident that reliance on Silver alone would adequately support its findings, the court of appeals opined that both the language and the history of the 1934 Act, together with the sound policy behind supervised exchange self-regulation, mandate the conclusion that Congress intended to exempt from the antitrust laws the exchange practice of fixing commission rates.27

In its analysis of § 19(b) of the 1934 Act, the Second Circuit seemed impressed by the fact that "the fixing of reasonable rates of commission" was listed among the items with respect to which the SEC was authorized by Congress to "alter or supplement" exchange rules. In fact, Thill was partly distinguished by the court because the anti-rebate rule challenged in the Seventh Circuit case was not specified in § 19(b). In Gordon, the court of appeals concluded that Congress considered the fixing of commissions to be essential to meeting the goals of supervised self-regulation which are to insure fair dealing and

27 498 F. 2d at 1305, 1306.
to protect investors.\textsuperscript{28} Emphasizing the SEC’s role in determining what changes are necessary to achieve the goals of the 1934 Act,\textsuperscript{29} the court of appeals decided that the core of exchange self-regulation necessary to make the 1934 Act work, as discussed in \textit{Silver}, must refer to the twelve practices specified in § 19(b), including the fixing of reasonable rates of commission.\textsuperscript{30}

In a brief review of the legislative history of the 1934 Act, the Second Circuit suggested that because the Act, which explicitly provides for the “fixing of reasonable rates of commission,” was passed \textit{after} the Supreme Court decision in \textit{United States v. Trenton Potteries Co.},\textsuperscript{31} Congress intended to permit the SEC to participate in the fixing of commission rates.\textsuperscript{32} Based on this, the court concluded that: (1) Congress viewed the commission rate structure as essential to the aims of the 1934 Act; and (2) Congress viewed the SEC as the proper body to assume the central role in assuring the fulfillment of the goals of the Act including review and control of the commission rate structure.\textsuperscript{33} The \textit{Gordon} court also based its decision on what it perceived

\textsuperscript{28} Id. at 1306.

\textsuperscript{29} Finally, and most importantly for this jurisdictional dispute between an antitrust court and the SEC, Congress vested in the Commission the power to determine whether changes are “necessary” in the exchanges’ rate-fixing practices to assure fulfillment the goals of the Act. Accordingly, Congress defined in § 19(b) those matters fundamental to achieving “the aims of the Securities change Act,” \textit{Silver v. New York Stock Exchange}, 373 U.S. at 361, and accorded the SEC the authority to make whatever changes respecting those matters are “necessary or appropriate” (19(b)) to effectuate those aims.

498 F. 2d at 1306.

\textsuperscript{30} The twelve items are listed in 15 U.S.C. § 78s (b) (1970):

(1) safeguards in respect of the financial responsibility of members and adequate provision against the evasion of financial responsibility through the use of corporate forms or special partnerships; (2) the limitation or prohibition of the registration or trading in any security within a specified period after the issuance or primary distribution thereof; (3) the listing or striking from listing of any security; (4) hours of trading; (5) the manner, method, and place of soliciting business; (6) NYSE fictitious or numbered accounts; (7) the time and method of making settlements, payments, and deliveries and of closing accounts; (8) the reporting of transactions on the exchange and upon tickers maintained by or with the consent of the exchange, including the method of reporting short sales, stopped sales, sales of securities of issuers in default, bankruptcy or receivership, and sales involving other special circumstances; (9) the fixing of reasonable rates of commission, interest, listing, and other charges; (10) minimum units of trading; (11) odd-lot purchases and sales; (12) minimum deposits on margin accounts; . . . [emphasis added].

\textsuperscript{31} 273 U.S. 392 (1927). The Supreme Court held that price-fixing was a per se violation of the Sherman Act.

\textsuperscript{32} The Second Circuit also looked to congressional hearings to support this finding, adding that “[the hearings] make plain the congressional awareness that this provision ‘would permit the Commission to fix rates.’” 498 F.2d at 1307 (citations omitted).

\textsuperscript{33} Id. The Court’s implication that an agency’s “central role” in a particular area is
as the "danger . . . that courts and the SEC would subject exchanges to repetitive or conflicting standards." Reviewing at length the SEC's role in the regulation of commission rates since 1963 (the year in which Silver was decided), the court emphasized that "the process of administrative review in the first instance is far superior to judicial review."

In a thinly-veiled rejection of the Seventh Circuit's rationale in Thill, the court made a half-hearted attempt to distinguish the case. However, the court clearly recognized that it was taking a contrary position on the issue. In its discussion of Thill, the Second Circuit stated that "it would be difficult to maintain that the effect of the anti-rebate rule . . . is in any significant respect different from the practice of commission rate-fixing."

B. The Seventh Circuit: Frederickson v. Merrill Lynch, Pierce, Fenner & Smith

The contrast in the positions taken by the two circuits is sharpened by a recent opinion of the United States District Court for the Northern District of Illinois. In Frederickson v. Merrill Lynch, Pierce, Fenner & Smith, the minimum commission rate structure was attacked in a suit very similar to Gordon. In a memorandum opinion, the district court denied the defendant's motion to dismiss the complaint. The defendant's alternative motion to stay all proceedings pending assertion of the SEC's alleged primary jurisdiction was also denied. The court held that the 1934 Act does not provide the commission rate structure with a complete exemption from the antitrust laws, and that the SEC does not have exclusive jurisdiction to pass on the legality of the fixed commissions. The decision clearly and explicitly rejected the reasoning of Gordon. It disagreed with the Gordon court's application of Silver as well as the court's analysis of the legislative intent behind the 1934 Act. The Frederickson court concluded that because there was no immunity from antitrust laws, the Silver "necessity" test must be applied to the commission rate structure.

synonymous with immunity from antitrust laws is not well-founded. The Second Circuit's reasoning is soundly criticized in Frederickson v. Merrill Lynch, Pierce, Fenner & Smith, 5 TRADE REG. REP. (1974-1 Trade Cas.) ¶ 75,227 (N.D. Ill. 1974), discussed in text accompanying note 38 infra.
IV. THE PRIMARY JURISDICTION ISSUE

A. Different Approaches of Two Federal Circuits

The diversity in the conclusions reached by the two circuits stems partially from different interpretations and applications of the administrative law involved in the problem. For example, the Second Circuit in Gordon anchored its decision squarely on the notion of immunity from the antitrust laws, finding exclusive jurisdiction resting in the SEC. It expressly disclaimed any reliance on the doctrine of primary jurisdiction. In a footnote, the court said:

we do not intend to imply that withdrawal of antitrust jurisdiction is based on the SEC's "primary" jurisdiction over the practices challenged by Gordon. . . . As our earlier discussion of the language and history of the 1934 Act indicates, we are of the view that Congress intended to exempt commission rate-fixing from the operation of the antitrust laws, and consequently deprived the courts of even "secondary" jurisdiction to entertain Sherman Act claims like that which Gordon asserts.

Typically, the doctrine of primary jurisdiction means that the agency makes an initial decision, although not necessarily a final one. It is invoked when the court determines that either of two situations exists: (1) the question to be decided falls within the special expertise of the administrative agency because of the agency's familiarity with the industry, or (2) the question to be decided has been delegated to the agency as an essential part of a pervasive regulatory scheme that requires consistent administration. The two factors are clearly related, and arguably, both are present in Gordon. The Second Circuit in Gordon, however, did not confine its decision to a finding that the stock exchange should get the advantage of an initial SEC determination. Instead, the Second Circuit ruled that an SEC-reviewed activity is per se exempt from antitrust scrutiny outside the regulatory agency's review procedures. Such a decision transcends the tradi-
tional application of the primary jurisdiction concept; it suggests the existence of a much higher level of "immunity."

The Seventh Circuit, on the other hand, has not been uniform in its application of the doctrine of primary jurisdiction. In Thill, the question was considered in a concurring opinion by Chief Judge Swygert. The issue of primary jurisdiction was said to "[lie] at the heart of the proper resolution of conflicting antitrust and securities law considerations."44 Yet, the judge declined to resolve the question, recommending instead that the district court consider the issue on remand. He noted that the Supreme Court had not reached the issue of primary jurisdiction in Silver.45

Apparently relying on the concurring opinion in Thill, the district court in Fredrickson directly addressed the primary jurisdiction problem. The court found that the attack on the commission rate structure was the "type of dispute which is appropriate for the invocation of the doctrine of primary jurisdiction."46 However, the court concluded that the doctrine was not applicable in the case before it because of the regulation of the rate structure by the SEC. The court apparently felt that the SEC could not or would not exercise objective judgment in regard to the challenge of a practice which the SEC had sanctioned.47 Thus even initial determination by the SEC was denied.

These different views of the meaning and application of the doctrine of primary jurisdiction are responsible for some of the antagonism between the SEC and the Justice Department, and for much of the confusion over the identity of the exact nature of the problem in Gordon. It is submitted that the doctrine of primary jurisdiction

Administrative Procedure Act, or under the provisions of the 1934 Act itself. 498 F.2d at 1311.
The applicable sections of the A.P.A. are: "A person suffering legal wrong because of agency action . . . is entitled to judicial review thereof." 5 U.S.C. § 702 (1970). "[F]inal agency action for which there is no other adequate remedy in a court [is] subject to judicial review." 5 U.S.C. § 704 (1970). 15 U.S.C. § 78y (1970) provides for review in the court of appeals for "[a]ny person aggrieved by an order issued by [the SEC] in a proceeding under this chapter to which such person is a party." Section 78y also provides that SEC findings of fact shall be conclusive, if supported by substantial evidence.

433 F.2d at 276.

44 In Silver, the question of primary jurisdiction was "obviated" by the fact that the SEC had no statutory authorization to "review particular instances of enforcement of exchange rules." 373 U.S. at 357.

At least one commentator has suggested that, in so holding, the Court purposefully and erroneously avoided the question of primary jurisdiction. See Baxter, note 1 supra.

45 5 TRADE REG. REP. ¶ 75,227 at 97,534 (emphasis added).

46 "If I were to remand this case to the SEC, I would be requiring the plaintiffs to seek from the regulators an admission of their failure to properly regulate." Id. at 97,534. The district court judge was reflecting the sentiments of Justice Douglas' dissenting opinion in Ricci v. Chicago Mercantile Exch., 409 U.S. 289, 308 (1973), discussed in text accompanying notes 54-55 infra.
should receive a much closer analysis in the ultimate resolution of any antitrust attack on practices subject to SEC review. The question remains whether the Supreme Court will invoke the doctrine in situations where the SEC has approved the exchange rule under attack. The Court will have the opportunity to pass on that question since Gordon’s petition for review of the Second Circuit decision has been granted.48

B. Ricci v. Chicago Mercantile Exchange

An analysis of the Supreme Court’s decision in Ricci v. Chicago Merchantile Exchange49 is necessary to determine how the Court might handle the primary jurisdiction question in Gordon. Ricci is one of the more recent cases in a long line of Supreme Court decisions dealing with the primary jurisdiction problem in antitrust suits involving regulated industries.50 In Ricci, the plaintiff charged the Chicago Mercantile Exchange with conspiracy to restrain trade, alleging that his membership in the exchange was transferred in violation of exchange rules, the Commodity Exchange Act,51 and the Sherman Act. The Supreme Court held that the antitrust proceedings should be stayed until the Commodity Exchange Commission could pass on the validity of the exchange’s conduct under the Commodity Exchange Act. The Supreme Court said:

We make no claim that the Commission has authority to decide either the question of immunity as such or that any rule of the [Commodity Exchange] takes precedence over antitrust policies. Rather, we simply recognize that Congress has established a specialized agency that would determine either that a membership rule of the Exchange has been violated or that it has been followed. Either judgment would require determination of facts and the interpretation and application of the Act and Exchange rules. And either determination will be of great help to the antitrust court in arriving at the essential accommodation between the antitrust and the regulatory regimes. . . .”52

The Court concluded that the Commission’s resolution of the dispute would allow the antitrust court to “make a more intelligent and sensitive judgment as to whether the antitrust laws will punish what

52 409 U.S. at 307.
an apparently valid rule of the Exchange permits.”

In light of Ricci, there is a serious question of how much discretion is left in the application of the doctrine of primary jurisdiction by a district court judge. The Supreme Court seemed to mandate the application of the doctrine, at least in certain types of situations. The issue in Gordon, although distinguishable from the Ricci problem, also presents questions which merit initial determination by those especially familiar with the customs and practices of the securities industry. A prior SEC adjudication of the dispute could be a material aid in the ultimate decision of whether the 1934 Act forecloses Gordon’s antitrust suit against the minimum commission rate structure.

Admittedly, previous SEC positions on the matter and SEC participation in Gordon on behalf of the stock exchanges seem to suggest what the Commission’s resolution might be. Justice Douglas’ dissenting opinion in Ricci, in which he suggests that it would be an “anomaly” to have the agency make a determination regarding an alleged violation of regulations when it has “shown every indication of sanctioning the alleged violation,” is not precisely in point, but indicates the nature of this particular argument against agency determination. Certainly, futility is good reason for non-application of the doctrine of primary jurisdiction. However, a key question in the ultimate resolution of the conflicting antitrust and securities laws jurisdiction is whether the minimum commission rate structure is necessary to make the Securities Exchange Act of 1934 work. Prior SEC action with respect to the minimum commission rate structure may never have directly involved an assessment of this question. Thus, even though the SEC determinations may be predictable, the Commission is still in the best position to make findings of fact which support or reject the proposition that the minimum commission rate structure is necessary. Presumably, the SEC has been monitoring rules of the exchanges for many years to assure furtherance of the aims of the 1934 Act.

The strongest argument against an initial SEC determination under the doctrine of primary jurisdiction is that the agency does not possess the relevant expertise on the question of whether the minimum commission rates represent the minimum repeal of the antitrust laws necessary—the other key factor under the Silver analysis. However, ascertaining what constitutes “minimum” repeal involves the

53 Id. at 308.
54 See note 47 supra.
55 409 U.S. at 308-309.
evaluation of the effect of alternatives to the present rate structure. That problem arguably requires SEC expertise. In fact, recent changes in the minimum commission system itself are evidence of the SEC’s awareness of the antitrust movement against the rate structure, and indicate that the issue of minimum repeal is under consideration.56

Assuming that the question of invocation of primary jurisdiction is decided affirmatively, the SEC determinations would play an important role in the antitrust court’s adjudication of the Gordon issue. The “home-court advantage” enjoyed by the stock exchange might well determine the final outcome in future cases. Courts traditionally have been somewhat reluctant to upset agency findings. However, at least the “extremes” of allowing the SEC exclusive jurisdiction or of totally disregarding the SEC’s judgment, would be sensibly discarded.

V. IMMUNITY UNDER THE Silver NECESSITY TEST

A. An Opportunity for a Substantive Resolution of the Immunity Question

It is unlikely that the Supreme Court will limit its decision in Gordon to the jurisdictional issue. At this stage of the litigation the SEC itself does not want merely an “initial determination” of the problem, but rather an opportunity to present its views concerning the substantive immunity of exchange activities before the high court. The Commission, effectively a “winner” in the lower court decisions, joined Mr. Gordon in his request for Supreme Court review of the case, and is openly seeking further confrontation over the question of antitrust immunity. Hopefully, the Court will resolve the long-simmering dispute between the SEC and the stock exchanges on one hand, and the Justice Department on the other. Depending on its scope, the decision by the Court could harbor broad implications for other activities within the securities field, and for other regulated industries.

B. The “Necessity” Question

The question of whether some implicit repeal of the antitrust laws is necessary to preserve the viability of the 1934 Act could be the key determination in the Court’s decision. Silver is still the leading case in that area, and the necessity test prescribed in Silver must

56 See text accompanying notes 59-60 infra.
ments. In applying the Silver test, the Court might be forced to measure the impact of the rate structure on the securities industry and the effects on the exchanges should the rate structure be abandoned. It is conceivable that the necessity of the stock exchanges themselves will be considered.\(^5\)

1. The SEC: Dichotomy of Opinion

The SEC will probably continue its enthusiastic support of the fixed commission rates in the *Gordon* case, although the Commission has become increasingly aggressive in its attempts to persuade the exchanges to voluntarily effect a gradual elimination of the fixed commission rates. Essentially, this leaves the SEC fighting a "two-front war," and in a position that might very well diffuse the strength of the Commission's arguments. In the courts, the SEC has been an energetic advocate of the position that the fixed rate structure is vital to the securities industry and necessary to make the 1934 Act work. But in its dealings with the exchanges in recent years, the Commission has been insistent upon exchange action which would eliminate the fixed rates.\(^6\) Even viewing the situation most favorably to the SEC, there is at least a superficial contradiction between these two positions. The Commission will likely respond with the suggestion that although a competitive rate structure is desirable, it can be achieved without spelling disaster for the exchanges only by a gradual withdrawal from the present system. This argument might merit considerable attention in the Supreme Court, particularly in light of the Court's impression of the importance of agency expertise and judgment, as delineated in *Ricci*. The Court's concern with the need for an initial determination by the agency under the doctrine of primary jurisdiction, stemming from the perceived importance of agency determinations of fact, and interpretation and application of the relevant legislation, would probably be the decisive factor. Given the present existence of the fixed rate structure, the Supreme Court could acquiesce in the SEC's position recommending a gradual withdrawal.

2. The Mootness Problem

However, the particular question of "necessity" might be implic-

\(^5\) The Supreme Court, of course, is not likely to address the question of whether the exchanges should fail. But at least one commentator has suggested that the failure of the NYSE is both desirable and "inevitable." See Ratner, *The NYSE's Day of Judgment*, The Wall Street Journal, November 19, 1974 at 22, col. 4.

\(^6\) See text accompanying notes 59-60 infra.
itly predetermined by the time the Court decides the case. The SEC, apparently motivated by the exchanges' "foot-dragging" in regard to instituting negotiated rates, has brought its rulemaking power into play. The Commission has proposed two rules which would strip the exchanges of the power to fix commission rates. One of the rules has already been adopted. In light of this most recent agency action, the SEC will be hard-pressed to argue before the Court in Gordon that the fixed rate structure is "necessary." Indeed, if the Court limits its inquiry to the fixed commission rate structure, and it is in effect rendered moot, the case's impact on the securities industry will be negligible. However, the Court is being urged to settle once and for all the extent of antitrust immunity enjoyed by stock exchanges. Its concern, then, might shift to the extent of the regulatory power vested in the SEC, and perhaps more importantly, the degree to which the SEC has exercised that power.

In setting aside the mootness question, the Court could find that the SEC's recently demonstrated vigor in policing the exchanges' commission rate rules is sufficient indication of the Commission's pervasive review power to cloak the rate structure with immunity, regardless of its status at the time of the decision. This result would be welcomed by the SEC, notwithstanding its current determination to inject competitive practices into the securities industry. Additionally, it would represent a significant setback for the Justice Department. A decision along those lines would essentially answer the question left unanswered by Silver.

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59 On September 19, 1974, the SEC sent letters to all stock exchanges, asking them to completely eliminate fixed commissions by May, 1975. SEC Release No. 34-11019, 39 FED. REG. 35214 (1974).

The New York, American and Boston Stock Exchanges have announced their refusal to comply with this SEC request to complete the implementation of negotiated rates. Up to this point, the exchanges have voluntarily agreed to phase in competitive rates. But they have now balked at eliminating fixed rates on orders between $2,000 and $300,000, which would represent the last step in full withdrawal from the fixed rate structure.

60 The SEC has adopted rule 19b-3, which essentially prohibits any exchange from adopting or retaining any rule that requires its members to charge fixed rates of commissions for transactions executed on or by use of such exchange after May 1, 1975. SEC Release No. 34-11203 (1975).

In the release, the Commission expressed the view that "the free play of competition can provide a level and structure of commission rates which will better serve the interests of the investing public, the securities markets, the securities industry, the national economy and the public interest than any system of price fixing which can reasonably be devised."

Proposed rule 10b-22 would make it unlawful for any broker, dealer, or member of any national securities exchange to directly or indirectly participate in any agreement or arrangement with another broker, dealer, or member of any exchange with respect to the fixing of any amount to be charged to other persons with respect of transactions in securities effected on, or
VI. SUMMARY AND CONCLUSIONS

The recent SEC decision to exercise its rule-making power and to eliminate fixed commission rates is unfortunate in at least one respect: it significantly complicates what would otherwise be an ideal opportunity for the Supreme Court to resolve the immunity question left unanswered in *Silver*. Assuming that the Court does not surrender the chance to tackle the issue of immunity presented in *Gordon* by invoking the primary jurisdiction or mootness doctrines it will be forced to proceed upon two fronts.

A. Threshold Immunity

In *Gordon*, the Second Circuit upheld the exchanges' exemption from the antitrust laws on two theories. First, the court of appeals determined that the review power vested in the SEC under § 19(b) of the 1934 Act provided the exchange rules with per se immunity from antitrust attack. The granting of such threshold immunity undeniably filled in the gap left by *Silver*, but the advisibility of conferring that type of exemption is doubtful. The fact that a rule comes within the scope of review jurisdiction granted by the 1934 Act to the SEC should not suffice to automatically immunize the rule from the antitrust laws. An actual exercise of the review power, even if energetic and ongoing, is not synonymous with the active enforcement of the antitrust laws, or even with the mere consideration of factors relevant to antitrust questions. The SEC, although empowered to conduct antitrust scrutiny as part of its review process, is not required to do so, and there is not much indication that it has done so. It is suggested, in fact, that the current wave of SEC action regarding the fixed rate structure is not part of an SEC concern with antitrust objectives, but instead stems from an SEC desire to contain and minimize the scope and consequences of reform-oriented phenomena such as antitrust lawsuits like Gordon's and the current legislation under consideration by Congress.\(^1\) This does not imply that the SEC is not in favor of enforcement of the antitrust laws, but only that the SEC tends to relegate antitrust considerations to a secondary status,

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\(^{1}\) Both houses of Congress have considered large-scale reform legislation affecting the securities industry. The Senate has already passed its version of the securities legislation. Proponents of H.R. 5050 are experiencing somewhat more difficulty in obtaining passage of the House's omnibus securities bill. Recently, the House Rules Committee has twice refused to clear H.R. 5050 for floor action.

The parallel bills, although varying considerably in approach, represent the same philosophical thrust. They would provide, among other things, for the elimination of fixed commission rates.
due to the agency's concern and intimate connection with the securities industry. Its review activity, therefore, is skewed toward monitoring and promoting the health of the securities industry. Accordingly, antitrust immunity should not be granted on the basis of the mere existence of agency review power.62

B. **Immunity Under the Silver Necessity Test**

The second basis for the immunity afforded the stock exchanges in *Gordon* was the alleged satisfaction of the *Silver* necessity test. The Second Circuit, attempting to apply the test laid down in *Silver*, determined that an implied exemption for the rate structure from the antitrust laws was necessary to make the 1934 Act work. However, since the *Silver* decision did not specify the factors to be considered in making that determination, the *Gordon* court became understandably confused. The Second Circuit, to its credit, logically proceeded to examine the purpose of the 1934 Act in terms of Congressional intent. It essentially failed, however, to discern the policies advanced by the fixed commission rate structure, and the availability and advisability of alternatives to that pricing system. Although *Silver* is silent in this regard, those factors would appear to be indispensable in determining whether the fixed rate structure is necessary to effectuate the purposes of the 1934 Act. Thus, the Second Circuit did not include all of the relevant considerations in its attempts to measure the necessity of the fixed rate structure. Interestingly, the court of appeals acknowledged the SEC action designed to *eliminate* the rate structure, yet made the remarkable observation that "[t]here is little question but that the commission rate structure is the keystone of . . . . the brokerage industry, and a matter of vital importance to individual investors as well."63

This failure to properly apply the *Silver* test weakens the *Gordon* opinion significantly in regard to the necessity question. Moreover, even assuming that the present pricing system does serve a legitimate purpose, it still should not be upheld if there is another pricing system which could accomplish the same objectives without being in violation of the antitrust laws. *Gordon* made virtually no attempt to examine any such alternative. The negotiated rate structure soon to be implemented by the SEC represents that viable alternative. The possibility that the new rules are themselves a response to antitrust pres-

62 Though somewhat parallel, this is not the same futility argument advanced by Justice Douglas in *Ricci*, and by the district court judge in *Fredrickson*. Those arguments concerned the issue of who was to make the first decision regarding the question of necessity.

63 498 F.2d at 1307.
sure is irrelevant, since they evidently are a feasible option. Accordingly, the *Silver* necessity test cannot be satisfied by the present system, and immunity should not be conferred on that basis. The fixed commission rate system should fall under the current antitrust attack.

The Supreme Court could reasonably agree, and in so holding still defer the larger question of threshold immunity to a future determination. Again, that would be unfortunate because the situation in *Gordon*, in the absence of the mootness problem, otherwise presents the very question—the "different case"—that *Silver* refused to resolve. As regulatory agencies continue their somewhat unrestrained growth, the availability of active review of regulated industry activities will continue to conflict with the antitrust objectives of both the Justice Department and private litigants. The absence of a definitive Supreme Court ruling will extend the confusion, uncertainty, and inconsistency created by the divergent views of two potent government agencies, and of at least two federal courts of appeal.

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