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Supreme Court Preserves States' Power to Protect Consumers But in the Process Blurs Federal Preemption Analysis

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The Supreme Court once again showed that, when it comes to the antitrust laws, the consumer is king. In *Oneok, Inc. v. Learjet*, the Court was asked to decide where state antitrust laws end and federal regulation begins. The constitution's Supremacy Clause establishes federal law as the supreme law of the land. But the Court gave states wide berth to protect their citizens from anticompetitive conduct, even in industries subject to heavy federal regulation governing the very conduct at issue.

Though *Oneok* focused on a specific regulated industry – natural gas – it involves fact patterns seen in many industries. In dynamic commodity markets like natural gas, price discovery – or the process of determining a fair price in long-term contracts involving products subject to significant swings in supply and demand – can be difficult for both buyers and sellers. To solve this problem, contracting parties might reference public index prices, which are often set on regulated exchanges or other regulated public fora. Firms that participate in setting these index prices may sometimes try to manipulate them to gain an advantage in unrelated transactions. Many antitrust cases involve such fact patterns and raise many questions, like antitrust injury, proximate cause and standing. But there is another threshold question: whether the antitrust laws even apply if the government regulates the index-setting process.

For a 10-year period starting around 1992, the Supreme Court consistently ruled for the defense in antitrust cases, significantly narrowing the types of conduct deemed anticompetitive. But along with a narrowed scope and renewed confidence in the lower courts' ability to distinguish between procompetitive and anticompetitive conduct through an economics-based approach, the Court is now more confident than ever in allowing the antitrust laws to regain their mantle as the "Magna Carta" of the free enterprise system. In the last few years, the pendulum has swung decidedly in favor of plaintiffs, with the Court taking particular interest in narrowing traditional immunities and exemptions that had limited the reach of the antitrust laws.

In its last two antitrust immunity cases, the Supreme Court focused on *who* may enact regulations that free parties from the constraints of the antitrust laws. But in *Oneok*, the Court took on the more difficult question of whether federally regulated conduct can be challenged under *state* antitrust laws if it also affects an unregulated market. Mixing heady constitutional questions and complex issues of legislative intent versus effect, the surprise 7-2 decision held that state antitrust laws must be given full force and effect.

The Supreme Court described the natural gas market as divided into three increasingly blurred segments: (i) extraction and production from the ground; (ii) wholesale distribution through interstate pipelines; and (iii) retail sales to end-users. Only the second of these is subject to federal regulation by the Federal Energy Regulatory Commission (FERC). But the regulatory regime within this sphere is so extensive that "Congress [has] occupied the *field* of matters *relating to* wholesale sales and transportation of natural gas in interstate commerce."

Beginning in the early 1990s, the FERC recognized that, when it comes to setting prices, competition beats regulation, and "adopted an approach that relied on the competitive marketplace, rather than classical regulatory rate-setting, as the main mechanism for keeping wholesale natural-gas rates at a reasonable level." Characterizing the "free-market system for setting" prices as "less than perfect," the Court noted that pipelines, distributors and customers turned to "privately published indices to determine appropriate prices" for both the regulated wholesale and unregulated retail natural gas markets. In 2003, the FERC found that traders had engaged in "efforts to manipulate" the indices by reporting false information, which benefited those traders in both markets.

Congress responded by granting the FERC the authority to prevent "any manipulative or deceptive device" affecting wholesale natural gas sales, and the FERC consequently enacted a Code of Conduct directly regulating the submission of information to the privately published indices.

Private suits also followed the FERC's findings. Large retail natural gas buyers sued under state antitrust laws to recover for overcharges caused by the manipulation of the indices. The district court granted summary judgment to the regulated pipelines, ruling the state antitrust laws were preempted under the Supremacy Clause because the alleged practices directly affected the *regulated* wholesale market, not just the unregulated retail market. The Ninth Circuit reversed, and in a 7-2 decision by Justice Breyer, the Supreme Court affirmed.

The Court recognized that "letting these actions proceed will permit state antitrust courts to reach conclusions about … conduct that differ from those that the FERC might reach or has already reached." While this was a "forceful" reason for preemption, the Court could "not accept the argument" absent an actual conflict, which the defendants could not assert because index manipulation would be condemned by both federal regulation and state law.

As the Court framed it, the application of state antitrust law turns on how far the FERC's "*field* preemption" authority extends outside the wholesale natural gas market. No one doubted the FERC's ability to prohibit the index manipulation at issue. But that did not resolve the question in the Court's eyes, because the authority to regulate is not necessarily the same as the *exclusive* authority to regulate. The conduct at issue did not *directly* involve the wholesale sale of natural gas; it merely *affected* the price of such sales. But "no one could claim," the Court said, that the FERC's "regulation of … physical activity for purposes of wholesale rates forecloses every other form of state regulation that *affects* those rates." Thus, conduct that affects *both* retail and wholesale markets may be subject to the dual regulatory requirements of both state and federal sovereigns. In such cases, the "proper test for purposes of preemption" is simply whether the state law is "aimed directly" at the regulated market. Because the state antitrust laws are "broadly applicable … to all businesses in the marketplace" writ large, the Court held that they were not preempted by FERC regulation.

Justice Scalia, in dissent, argued that this case is not as clear-cut as the majority suggests. As he noted, the "Court does not identify a single case – not one – in which [it has] sustained state regulation of behavior already regulated by the Commission." Accusing the majority of a "make-it-up-as-you-go-along" approach, Justice Scalia noted that the Court's decision "smudges" the traditional line that states may not use their antitrust laws to regulate practices already regulated by federal regulatory agencies, like the FERC.

Where the new dividing lines will be drawn remains to be seen and many questions remain. Perhaps the most important of these is whether *Oneok* has any application to the preemptive effect of federal regulation on *federal* antitrust laws, under the related doctrine of "implied repeal." Consider, for example, Justice Breyer's earlier decision in *Credit Suisse Securities LCC v. Billing*. There, the Court held that the federal securities laws impliedly repealed federal antitrust laws because – even absent an *actual* conflict – the SEC's role in regulating the conduct at issue rendered application of the antitrust laws "plainly repugnant" to the federal regulatory scheme.

In *Billing*, Justice Breyer relied on the same types of arguments Justice Scalia highlighted in his *Oneok* dissent. He noted, for example, that the "law grants the SEC authority to supervise all of the activities here in question" and that the SEC has "exercised that authority." Justice Breyer also noted there was a *potential* for conflicting standards if "antitrust plaintiffs [could] bring lawsuits in dozens of different courts with different nonexpert juries." Although not mentioning *Billing*, Justice Scalia noted that each of those facts applies equally to the circumstances in *Oneok*.

As this suggests, there may be some merit to Justice Scalia's concerns that *Oneok* "smudges" the lines. Exactly how *Oneok* will be reconciled with other preemption and implied repeal cases is an open question. Courts may make fine distinctions among different federal regulatory schemes, distinguish between state and federal antitrust laws, or scrutinize how close the challenged conduct lies to the heart of the regulated market.

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In practical terms, what does *Oneok* mean? At a minimum, it provides plaintiffs with new ammunition to challenge federally regulated conduct. This, in turn, puts greater pressure on firms which operate in these industries to ensure that they have strong antitrust compliance programs that are tailored carefully to their business. As Justice Scalia, and Justice Breyer before him, noted, judges and juries can come to very different conclusions from federal regulators. As a result, it may no longer be sufficient to claim compliance with industry regulation and agency guidance.

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