BRACEWELL

INSIGHTS

Supreme Court Holds State Regulatory Board Not Immune From Antitrust Laws

February 27, 2015

*By: **Daniel E. Hemli** and **Jacqueline R. Java***

On February 25, 2015, the U.S. Supreme Court determined that the North Carolina State Board of Dental Examiners ("Dental Board") is not shielded from federal antitrust law under the doctrine of state-action antitrust immunity. ***North Carolina State Board of Dental Examiners v. Federal Trade Commission***, 574 U.S. __, __ (Feb. 25, 2015) (slip op.). In a 6-3 ruling, the Supreme Court held that a state agency controlled by active market participants must be actively supervised by the State in order to invoke the state-action doctrine, which was first established in *Parker v. Brown*, 317 U.S. 341 (1943). This decision has important implications for state agencies, including state professional boards, and those who participate in or go before those agencies.

Factual and Procedural Background: Under the North Carolina Dental Practice Act ("Act"), the Dental Board is the "agency of the State for the regulation of the practice of dentistry," creating, administering, and enforcing a licensing system for dentists. Six of the Dental Board's eight members must be licensed dentists engaged in the active practice of dentistry.

In the 1990s, North Carolina dentists began offering teeth whitening services. In 2003, nondentists began offering the same services, but undercut dentists by charging lower prices. Dentists complained to the Dental Board about their new competitors, triggering an investigation by the Dental Board. Beginning in 2006, the Dental Board issued cease-and-desist letters on official agency letterhead to nondentist teeth whitening service providers and product manufacturers threatening criminal liability. The Dental Board also persuaded the North Carolina Board of Cosmetic Art Examiners to warn cosmetologists against teeth whitening, and sent letters to mall operators informing them that kiosk teeth whiteners were violating the Act and advising the malls to expel violators. As a result of these actions, many nondentists ceased offering teeth whitening services in North Carolina.

In 2010, the Federal Trade Commission ("FTC") filed an administrative complaint charging the Dental Board with violating the Federal Trade Commission Act, alleging that the Dental Board's concerted action to exclude nondentists constituted an anticompetitive and unfair method of competition. The Dental Board moved to dismiss based on state-action immunity. An Administrative Law Judge denied the motion and the FTC upheld that ruling on appeal. On petition for review, the Court of Appeals for the Fourth Circuit affirmed the FTC in all respects.

Decision of the U.S. Supreme Court: The Supreme Court first recognized that there is a balance between the federal antitrust laws' goal of promoting robust competition on the one hand, and

principles of federalism and State sovereignty on the other hand. For this reason, the Court in *Parker v. Brown* interpreted the antitrust laws to confer immunity on anticompetitive conduct by the States when acting in their sovereign capacity.

The Board argued it was cloaked with that very immunity because its members "were invested by North Carolina with the power of the State." However, the Supreme Court held that a nonsovereign actor controlled by active market participants must satisfy two requirements to be able to claim immunity: (1) the challenged restraint must be clearly articulated and affirmatively expressed as state policy, and (2) that the policy be actively supervised by the State. This two-part test, set forth in *California Retail Liquor Dealers Assn. v. Midcal Aluminum, Inc.* 445 U.S. 97 (1980), ensures that the State must have foreseen and implicitly endorsed the anticompetitive effects as consistent with its policy goals.

Significantly, in reaching this conclusion, the Court noted that "state agencies are not simply by their governmental character sovereign actors for purposes of state-action immunity," and that "[i]mmunity for state agencies, therefore, requires more than a mere façade of state involvement." The Court went on to say that limits on state-action immunity are most essential when the State delegates regulatory power to active market participants, who may act to further their own private interests rather than the governmental interests of the State (so-called "regulatory capture"). Applying this reasoning to state professional boards, the Supreme Court held that "a state board on which a controlling number of decisionmakers are active market participants in the occupation the board regulates must satisfy *Midcal's* active supervision requirement in order to invoke state-action antitrust immunity." Interestingly, the Court found state agencies controlled by market participants to be similar to private trade associations, which are routinely subjected to antitrust scrutiny, and less akin to municipalities, which are excused from *Midcal*'s active supervision rule.

While noting that "active supervision" will depend on the circumstances of the case and need not entail day-to-day involvement in an agency's operations, the Court did advise that active State supervision must include certain requirements: the supervisor must review the substance of the anticompetitive decision (the mere potential for State supervision is not sufficient); the supervisor must have the power to veto or modify specific decisions to ensure they accord with state policy; and the supervisor must not itself be an active market participant.

In the present case, the Dental Board did not claim that the State exercised active, or any, supervision over its conduct regarding nondentist teeth whiteners, and as a result, the Court found no specific supervisory systems to review. The Dental Board relied on cease-and-desist letters instead of any of the powers at its disposal that would have invoked oversight by a politically accountable official. Since the Dental Board failed the "active supervision" element, it was not cloaked with *Parker* immunity.

Dissent by Justice Alito: Justice Alito disagreed with the majority's interpretation of *Parker* and the cases that followed that decision. He read *Parker* more simply, as holding that state-action immunity always applies to state agencies, and therefore, because the Dental Board is a state agency, it should be immune from federal antitrust laws. Justice Alito expressed concern regarding the potential difficulty of applying the majority's analysis, noting that the majority left a number of questions unanswered and that its decision is likely to have "far-reaching effects" on state regulation of professions.

Important Takeaways: With this significant decision strengthening the tenets of antitrust law, state professional boards and other state bodies can no longer simply rely on their formal designation as a state agency to receive antitrust immunity. Rather, if a controlling number of decisionmakers are active market participants in the relevant profession, then some other State actor will need to actively supervise board actions that may have anticompetitive effects, such as conduct seeking to exclude certain competitors from the marketplace. As Justice Alito points out in his dissent, States may find it necessary to change the composition of medical, dental, and other boards to satisfy the majority's holding. Alternatively, States may need to put in place infrastructure and procedures to more actively supervise board decisions.

Additionally, those who participate on, are subject to, or come before state agencies may also experience a change in their subject agency. As pointed out in the opinion, many state agencies that are controlled by market participants function essentially as private trade associations. The activities of those associations may be subject to antitrust scrutiny, as such associations are capable of facilitating a conspiracy of competitors to restrict competition under the federal antitrust laws. Those participating in or impacted by such actions, either within or outside the agency, may either be subject to or have a cause of action for claims of antitrust.