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Supreme Court Holds State Regulatory Board Controlled by Active Market Participants Is Not Immune from Antitrust Liability

When a controlling number of decisionmakers serving on a state regulatory board are active participants in the market or profession being regulated, the board must be actively supervised by the state in order to receive state-action immunity from alleged violations of federal antitrust law, the United States Supreme Court held yesterday. *North Carolina State Board of Dental Examiners v. Federal Trade Commission*, No. 13-534 (Feb. 25, 2015) concerned a challenge brought by the FTC to a state dentistry board's efforts to limit competition for teeth whitening services from non-dentists in North Carolina. In a majority opinion authored by Justice Kennedy, the Court agreed with the FTC that although the board was an agency of the state, its regulations were not entitled to state-action immunity because it was controlled by practicing dentists and not actively supervised by the state. Justices Scalia, Thomas and Alito dissented.

Background

The State of North Carolina has declared the practice of dentistry to be a matter of public concern and created the North Carolina State Board of Dental Examiners to act as "the agency of the State for the regulation of the practice of dentistry." N.C. Gen. Stat. Ann. § 90-22(a). Of the Board's eight members, six must be licensed dentists actively practicing within the state. The Board is given broad authority over the state's licensing system for dentists and is empowered to file suits to "perpetually enjoin any person from . . . unlawfully practicing dentistry." *Id.* at § 90-40.1.

In the 1990s, many North Carolina dentists began earning substantial fees for teeth whitening services, including most members of the Board. In the early 2000s, non-dentists began performing the same services, often charging significantly less than dentists. Dentists complained about their newfound competition, and the Board began an investigation into non-dentist teeth whitening. Starting in 2006, the Board issued dozens of cease-and-desist letters to non-dentist providers of teeth whitening services. The letters strongly implied or stated that teeth whitening services constituted dentistry and warned their recipients that the unlicensed practice of dentistry is a crime. As a result of these and other efforts by the Board, non-dentists eventually ceased offering teeth whitening services in North Carolina.

In 2010, the Federal Trade Commission filed an administrative complaint alleging that the Board's actions constituted anticompetitive conduct. Following a hearing on the merits, an FTC administrative law judge determined the Board had unreasonably restrained trade. The FTC ordered the Board to stop sending cease-and-desist letters or similar communications stating that only dentists could provide teeth

whitening services and further ordered the Board to issue notices to all recipients of its earlier cease-and-desist letters advising them of the Board's limited authority and of their rights to seek declaratory relief. The United States Court of Appeals for the Fourth Circuit affirmed the FTC's decision. The Supreme Court granted *certiorari* to determine "whether the [B]oard's actions are protected from Sherman Act regulation under the doctrine of state-action antitrust immunity." (Op. at 1.) It held that they were not.

The Majority Opinion

The Supreme Court has long recognized that subjecting every state law or policy to antitrust analysis in order to determine whether it was anticompetitive "would impose an impermissible burden on the States' power to regulate." (Op. at 5.) Accordingly, in *Parker v. Brown*, 317 U.S. 341 (1943), it held that states are immune from restrictions on anticompetitive conduct when acting in their sovereign capacity.

State-action immunity also may apply to non-sovereign actors, such as private trade associations, but only in limited circumstances. For such actors' conduct to be eligible for state-action immunity, two requirements must be met: the restraint on competition must be (1) "clearly articulated and affirmatively expressed as state policy," and (2) "actively supervised by the State itself." (Op. at 6, 9.) See *Cal. Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97 (1980).

In *Dental Examiners*, both the parties and the Court assumed that the regulation of dentistry in North Carolina satisfied the "clear articulation" requirement and addressed only the "active supervision" requirement. But the Board did not argue that its conduct was actively supervised by the State—indeed, the Court noted that, aside from the Board's own members, "North Carolina officials may well have been unaware that the Board had decided teeth whitening constitutes 'the practice of dentistry' and sought to prohibit those who competed against dentists from participating in the teeth whitening market." (Op. at 17.) Rather, the Board's primary argument was that because it was a state agency itself, it need not be supervised by any other state actors.

In rejecting that argument, the Supreme Court explained that the supervision requirement is animated by concerns regarding the incentives of active market participants who are given power to regulate their own industry, such as members of the Board. Accordingly, *Parker* immunity "demands realistic assurances that a private party's anticompetitive conduct promotes state policy, rather than merely the party's individual interests." (Op. at 10 (quotations omitted).) The Court compared state agencies run by market participants to private trade associations, noting that the similarities between the two "are not eliminated simply because the former are given a formal designation by the State, vested with a measure of government power, and required to follow some procedural rules." (Op. at 14.) In both cases, "the need for supervision is manifest." (*Id.*)

The Court also rejected the argument that refusing to immunize active market participants from antitrust liability would discourage them from serving as members of state regulatory agencies. In doing so, it first

noted that *Dental Examiners* did not present a case for monetary damages, and therefore did not offer an occasion to address whether agency officials might be immune from financial liability. Nor did *Dental Examiners* provide any reason that States could not provide for the defense and/or indemnification of agency members in the event of litigation arising from their public service. Moreover, the Court explained that market participants appointed to regulatory roles could still benefit from *Parker* immunity so long as their states provided active supervision.

Although no specific supervisory scheme was at issue, the Court provided some guidance as to the “requirements of active supervision:” the supervisor (1) “may not itself be an active market participant;” (2) “must review the substance of the anticompetitive decision, not merely the procedures followed to produce it;” (3) “must have the power to veto or modify particular decisions to ensure they accord with state policy;” and (4) must actually exercise supervision, not simply create the “potential for state supervision.” (Op. at 18 (quotations and citations omitted).) The Court emphasized, however, that the adequacy of supervision is a fact-specific assessment which will depend “on all the circumstances of a case.” (*Id.*)

The Court concluded that although federal antitrust laws accommodate federalism concerns, they do not “authorize the States to abandon markets to the unsupervised control of active market participants, whether trade associations or hybrid agencies. If a state wants to rely on active market participants as regulators, it must provide active supervision if state action immunity under *Parker* is to be invoked.” (*Id.*)

The Dissent

Justice Alito authored a dissenting opinion, joined by Justices Scalia and Thomas. The dissent argued that the majority misapplied *Parker* in failing to recognize that state regulatory agencies have long been staffed by market participants and often serve the interests of those they regulate, as was true of the state agency at issue in *Parker* itself. According to the dissent, *Parker* held that antitrust laws “do not apply to state agencies; the [Board] is a state agency; and that is the end of the matter,” even if “the Board is not structured in a way that merits a good-government seal of approval.” (Dissent at 1-2.) In straying from this simple syllogism, the dissent argued that *Dental Examiners*’ new test for distinguishing between private and state actors for purposes of applying *Parker* immunity “is not true to the *Parker* doctrine; . . . diminishes our traditional respect for federalism and state sovereignty; and . . . will be difficult to apply.” (Dissent at 13.)

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Dental Examiners may provide a new means of challenging certain state regulations, depending on the identity and composition of the state actor or agency that creates and enforces them. In response to the Supreme Court’s decision, states may find it necessary or desirable to change the composition of

professional regulatory boards, as Justice Alito’s dissent suggests, or to change the way such boards are administered and overseen. Because the decision does not specifically enumerate the elements of “active supervision,” however, determining whether a state board comprised of active market participants may be subject to antitrust liability will require fact-based and context-specific analysis.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

Andrew C. Finch

212-373-3460

afinch@paulweiss.com

William B. Michael

212-373-3648

wmichael@paulweiss.com

Joseph J. Simons

202-223-7370

jsimons@paulweiss.com

Aidan Synnott

212-373-3213

asynnott@paulweiss.com

Associate Michael Nadler contributed to this client alert.