LEGISLATIVE COUNSEL BUREAU

A TRADITION OF TRUSTED LEGAL SERVICE TO THE CALIFORNIA LEGISLATURE

LEGISLATIVE COUNSEL BUREAU
925 L STREET
SACRAMENTO, CALIFORNIA 95814
TELEPHONE (916) 341-8000
FACSIMILE (916) 341-8020
INTERNET WWW.LEGISLATIVECOUNSEL.CA.GOV

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Honorable Jerry Hill
Room 5035, State Capitol

ANTITRUST LIABILITY: STATE-ACTION IMMUNITY - #1509722

Dear Senator Hill:

The Sherman Act[1] prohibits anticompetitive conduct including monopolies and agreements in restraint of trade, but states are immune from Sherman Act liability in certain circumstances. In *North Carolina State Bd. of Dental Examiners v. F.T.C.* (2015) 574 U.S. __ [135 S.Ct. 1101, 1110] (hereafter *North Carolina*), the United States Supreme Court held that the State of North Carolina's dental board, which was controlled by active market participants, was not immune from liability under the Sherman Act with respect to its anticompetitive actions because the board was not actively supervised by the state. You have asked us to describe the effect of this holding on the legal standard used by courts to determine when a state agency or board will be granted immunity from liability under the Sherman Act.

1. The Sherman Act

The Sherman Act prohibits agreements in restraint of trade and monopolies, as provided in sections 1 and 2 of the act. Section 1 of the Sherman Act prohibits contracts, combinations, or conspiracies in restraint of trade or commerce, or, in other words, the anticompetitive conduct of a combination of firms. Section 2 of the Sherman Act prohibits monopolies, attempts to monopolize, and combinations or conspiracies to monopolize, or, in other words, the anticompetitive conduct of either a single firm or a combination of firms. Not every combination in restraint of trade is unlawful under the Sherman Act. (*People v. Santa Clara Val. Bowling Proprietors' Ass'n* (1965) 238 Cal.App.2d 225, 233.) Rather, the act proscribes only those restraints that are unreasonable. (*Ibid.*)

[1] 15 U.S.C. §§ 1-7; hereafter the Sherman Act. All further section references are to title 15 of the United States Code.

2. History of state-action immunity prior to the ruling in *North Carolina*

In order to determine the impact of the *North Carolina* decision on the legal standards for state-action immunity, we must first examine United States Supreme Court jurisprudence applying state-action immunity leading up to *North Carolina*.

In *Parker v. Brown* (1943) 317 U.S. 341, 350-351 (hereafter *Parker*), the Supreme Court first addressed the issue of whether the Sherman Act applies to states and concluded that "nothing in the language of the Sherman Act or in its history ... suggests that its purpose was to restrain a state or its officers or agents from activities directed by its legislature." *Parker* involved a suit that challenged a California statute as violating the Sherman Act. The statute in that case established a program for the marketing of agricultural commodities produced in the state by restricting competition among growers and maintaining prices. (*Id.* at p. 346.) The program restricted the trade of raisins by authorizing the establishment of a commission with the authority to approve a petition of raisin producers for the establishment of a prorate marketing plan for raisins. (*Ibid.*) If the commission approved the program and 65 percent of specified raisin producers approved the program, then the program was instituted. (*Id.* at pp. 346-347.) In concluding that the Sherman Act did not prohibit the California program, the court held that state actions are immune from liability under the Sherman Act. (*Id.* at p. 352.) The court reasoned that the California program constituted state action because of the following:

> "It is the state which has created the machinery for establishing the prorate program. Although the organization of a prorate zone is proposed by producers, and a prorate program, approved by the Commission, must also be approved by referendum of producers, *it is the state, acting through the Commission, which adopts the program* and which enforces it with penal sanctions, *in the execution of a governmental policy.* The prerequisite approval of the program upon referendum by a prescribed number of producers is not the imposition by them of their will upon the minority by force of agreement or combination which the Sherman Act prohibits. The state itself exercises its legislative authority in making the regulation and in prescribing the conditions of its application." (*Ibid.*; emphasis added.)

Although the court held that the California program was entitled to state-action immunity, the court limited the application of state-action immunity by cautioning that "a state does not give immunity to those who violate the Sherman Act by authorizing them to violate it, or by declaring that their action is lawful." (*Id.* at p. 351.)

Thus, the holding in *Parker* established that a state entity is immune from Sherman Act liability where it is executing a governmental policy. Following *Parker*, the United States Supreme Court decided a series of cases that developed the application of state-action immunity by examining the nature and extent of state involvement necessary for an action to be considered state action.

In *Goldfarb v. Virginia State Bar* (1975) 421 U.S. 773, 775 (hereafter *Goldfarb*), the United States Supreme Court determined that a minimum fee schedule for lawyers published

by a county bar association and enforced by the Virginia State Bar violated the Sherman Act. In reaching this conclusion, the court ruled that the anticompetitive activity of establishing a minimum fee schedule was not state action because "it cannot fairly be said that the State of Virginia through its Supreme Court Rules required the anticompetitive activities." (*Id.* at p. 790.) Furthermore, the court stated as follows:

> "The fact that the State Bar is a state agency for some limited purposes does not create an antitrust shield that allows it to foster anticompetitive practices for the benefit of its members. [Citation.] The State Bar, by providing that deviation from County Bar minimum fees may lead to disciplinary action, has voluntarily joined in what is essentially a private anticompetitive activity, and in that posture cannot claim it is beyond the reach of the Sherman Act. [Citation.]" (*Id.* at pp. 791-792; fns. omitted.)

Thus, the holding in *Goldfarb* clarified that actions by a purported state agency are, nevertheless, subject to the prohibitions of the Sherman Act where those actions in essence constitute private anticompetitive activity.

However, in *Bates v. State Bar of Arizona* (1977) 433 U.S. 350, 362-363 (hereafter *Bates*), the United States Supreme Court held that the Arizona Supreme Court's imposition and enforcement of a disciplinary rule that restricted advertising did not violate the Sherman Act because the action qualified as exempt state action under *Parker, supra*. The court reached this conclusion after finding that the "disciplinary rules reflect a clear articulation of the State's policy with regard to professional behavior. Moreover, as the instant case shows, the rules are subject to pointed re-examination by the policymaker the Arizona Supreme Court in enforcement proceedings." (*Bates, supra,* at p. 362.) The court deemed "it significant that the state policy is so clearly and affirmatively expressed and that the State's supervision is so active." (*Ibid.*) Thus, *Bates* clarified that it is relevant to a grant of state-action immunity whether the anticompetitive actions represent a clear articulation of the state's policy and are subject to a pointed re-examination by the state Supreme Court.

In *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.* (1980) 445 U.S. 97, 99 (hereafter *Midcal*), the United States Supreme Court examined a California statute that required all wine producers, wholesalers, and rectifiers to file fair trade contracts or price schedules with the state, and prohibited wine merchants from selling wine to a retailer at a price other than a price set in such an effective price schedule or fair trade contract. Under the statute, California had no direct control over, and did not review the reasonableness of, the prices set by wine dealers. (*Id.* at p. 100.) In determining whether the state's involvement in the above program was sufficient to establish antitrust immunity under *Parker, supra,* the court examined its preceding decisions and held that two standards must be met for state-action immunity to apply: "First, the challenged restraint must be 'one clearly articulated and affirmatively expressed as state policy'; second, the policy must be 'actively supervised' by the State itself." (*Midcal, supra,* at p. 105, citing *City of Lafayette, La. v. Louisiana Power & Light Co.* (1978) 435 U.S. 389, 410 (hereafter *City of Lafayette*).) Ultimately, the court in *Midcal* found that the California program failed to meet the second requirement for state-action immunity because the state "neither establishes prices nor reviews the

reasonableness of the price schedule; nor does it regulate the terms of fair trade contracts. The State does not monitor market conditions or engage in any 'pointed reexamination' of the program. [Fn. omitted.]" (*Midcal, supra,* at pp. 105-106.) In sum, the court in *Midcal* expressly imposed two requirements for state-action immunity to apply: (1) a clearly articulated and affirmatively expressed state policy, and (2) active supervision of that policy by the state.

Subsequently, in *Hoover v. Ronwin* (1984) 466 U.S. 558 (hereafter *Hoover*), the United States Supreme Court examined whether state-action immunity applied to a committee appointed by the Arizona Supreme Court to administer the state bar examination. The court reiterated *Midcal's* two-part test and stated that when "the conduct at issue is in fact that of the state legislature or supreme court, we need not address the issues of 'clear articulation' and 'active supervision.'" (*Hoover, supra,* at p. 569.) However, the court articulated that when the conduct is that of a "nonsovereign state representative," it must be pursuant to a "'clearly articulated and affirmatively expressed state policy' to replace competition with regulation," and the degree of state supervision is also "relevant to the inquiry." (*Ibid.*) Applying these standards, the court held that the actions of the committee were entitled to state-action immunity because the Arizona Supreme Court "retained strict supervisory powers and ultimate full authority over [the committee's] actions." (*Id.* at p. 572.) In the court's view, the Arizona Supreme Court retained sufficient supervision and authority over the committee by specifying the subjects to be tested on the bar exam and the general qualifications required for bar applicants, approving the committee's grading formula, and, most significantly, making the final decision to grant or deny admission to the bar and providing individualized review of bar examinations when requested. (*Id.* at pp. 572-573.) In sum, *Hoover* confirmed that a "nonsovereign state representative" is entitled to state-action immunity when its actions meet *Midcal's* clear articulation requirement and emphasized that the degree of state supervision is also "relevant to the inquiry."

The court in *Town of Hallie v. City of Eau Claire* (1985) 471 U.S. 34, 44-46 (hereafter *Town of Hallie*) addressed the application of the state immunity doctrine with respect to municipalities. Distinguishing municipal actors from state actors, the court applied only the first *Midcal* requirement. Thus, the court held that municipalities are immune from Sherman Act liability when acting pursuant to a clearly articulated and affirmatively expressed state policy to displace competition, but need not show active state supervision to maintain their state-action exemption. (*Town of Hallie, supra,* at pp. 40 & 46.) In deciding to apply only the first *Midcal* requirement, the court distinguished municipalities from both the state and private parties, explaining that municipalities "are not beyond the reach of antitrust laws by virtue of their status because they are not themselves sovereign." (*Town of Hallie, supra,* at p. 38.) In making this distinction, the court emphasized that municipalities differ from private parties because there is a real danger that private parties will act to further their own interests over the interests of the state. The court reasoned that with municipalities there is "little or no danger" of this occurring. (*Id.* at p. 47.) In sum, the ruling in *Town of Hallie* stands for the proposition that, to be entitled to state-action immunity, municipalities need only meet the first *Midcal* requirement of acting pursuant to a clearly articulated and affirmatively expressed state policy to displace competition.

The United States Supreme Court examined whether state-action immunity applied to protect private physicians with respect to their anticompetitive conduct on a hospital's peer-review committee that the hospital was under a statutory obligation to establish and review in *Patrick v. Burget* (1988) 486 U.S. 94, 102 (hereafter *Patrick*). The court determined that both *Midcal* requirements must be satisfied for the anticompetitive actions of private parties to be deemed state action and shielded from antitrust laws. (*Patrick, supra,* at p. 100.) After finding that the actions of the peer review committees did not meet the active supervision prong, the court declined to consider the clear articulation requirement and held that state-action immunity did not apply. (*Ibid.*) In discussing active supervision, the court stated that the requirement "stems from the recognition that '[w]here a private party is engaging in anticompetitive activity, there is a real danger that he is acting to further his own interests, rather than the governmental interests of the State.' [Citation.]" (*Ibid.*) Therefore, the court determined that there was a danger that the private physicians on a hospital peer review committee were furthering their own private interests because the state did not have the ability to review the committee's decisions regarding hospital privileges to determine whether those decisions comported with state regulatory policy and correct abuses. (*Id.* at pp. 101-102.) In other words, according to the court in *Patrick*, both *Midcal* requirements apply to the anticompetitive actions of private parties because of the real danger that private parties will act to further their own interests.

In *City of Columbia v. Omni Outdoor Advertising, Inc.* (1991) 499 U.S. 365, 368-369 (hereafter *City of Columbia*), a private billboard company argued that the city's billboard ordinances were the result of an anticompetitive conspiracy between city officials and a private local billboard company, whereby the city colluded with the local billboard company to pass local ordinances intended to restrict competition from out-of-town companies. The United States Supreme Court rejected the argument that a conspiracy exception exists for *Parker's* state-action exemption "'where politicians or political entities are involved as conspirators' with private actors in the restraint of trade." (*City of Columbia, supra,* at p. 374.) In reaching this conclusion, the court cautioned that "[t]his does not mean, of course, that the States may exempt *private* action from the scope of the Sherman Act; we in no way qualify the well-established principal that 'a state does not give immunity to those who violate the Sherman Act by authorizing them to violate it, or by declaring their action is unlawful.'" (*Id.* at p. 379, citing *Parker, supra,* 317 U.S. at p. 351; emphasis in original.) Additionally, the court stated that "with the possible market participant exception, *any* action that qualifies as state action is '*ipso facto* ... exempt from the operation of the antitrust laws.'" (*Id.* at p. 379, citing *Hoover, supra,* 466 U.S. at p. 568; emphasis in original.) Therefore, in *City of Columbia* the Supreme Court left open a "possible" exception from state-action immunity in instances where the state is acting as a market participant.

Next, the United States Supreme Court in *F.T.C. v. Ticor Title Ins. Co.* (1992) 504 U.S. 621, 632 (hereafter *Ticor*) considered whether the mere existence of a state regulatory program for setting insurance rates, if staffed, funded, and empowered by law, satisfied the active supervision requirement in *Midcal.* The court concluded that the regulatory program did not meet the active supervision requirement because "The mere potential for state supervision is not an adequate substitute for a decision by the State." (*Ticor, supra,* at p. 638.)

The court explained that "[w]here prices or rates are set as an initial matter by private parties, subject only to a veto if the State chooses to exercise it, the party claiming the immunity must show that state officials have undertaken the necessary steps to determine the specifics of the price-fixing or ratesetting scheme." (*Ibid.*)[2] Accordingly, the holding in *Ticor* emphasized that the mere potential for state supervision by itself is not adequate for a finding of active state supervision.

Recently, in *F.T.C. v. Phoebe Putney Health System, Inc.* (2013) 568 U.S. __ [133 S.Ct. 1003] (hereafter *Phoebe Putney*), the United States Supreme Court addressed the question of whether a "substate governmental entity" (*id.* at p. 1010) in the form of a hospital authority created by the state legislature to "exercise public and essential governmental functions" (*id.* at p. 1007) is entitled to state-action immunity for permitting acquisitions that substantially lessened competition.[3] The court granted certiorari to answer two questions: (1) whether the hospital authorities acted pursuant to a clearly articulated and affirmatively expressed state policy to displace competition; and (2) if so, whether state-action immunity was nonetheless inapplicable as a result of the hospital authority's "minimal participation" and "limited supervision" of the hospitals' acquisitions and operations. (*Id.* at p. 1009.) The court answered the first question in the negative finding that "[g]rants of general corporate power that allow substate governmental entities to participate in a competitive marketplace" do not clearly articulate or affirmatively express a state policy to displace competition. (*Id.* at p. 1012.) Because the court concluded that the hospital authorities did not act pursuant to a clearly articulated and affirmatively expressed state policy to displace competition, the court did not reach the second question. (*Id.* at p. 1009.) Accordingly, the United States Supreme Court left open the question of whether *Midcal's* active supervision requirement applies to "substate governmental entities." Additionally, in a footnote, the court declined to answer an amicus curiae question of whether a "market participant" exception to state-action immunity applied because the argument was not raised in the lower courts. (*Phoebe Putney, supra,* at p. 1010, fn. 4.) However, the court recognized that *City of Columbia, supra,* left open the possibility of a market participant exception. (*Phoebe Putney, supra,* at p. 1010.) Therefore, the court in *Phoebe Putney* left open the question of whether a "substate governmental agency" is required to be actively supervised by the state to be entitled to state-action immunity, and recognized that there is a possible market participant exception to state-action immunity.

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[2] In *Ticor,* the potential for state supervision was not enough because the rates became effective unless they were rejected by the state within a set time. Furthermore, the facts of that case revealed that, at most, the rate filings were checked for mathematical accuracy and some were unchecked altogether. (*Ibid.*)

[3] The hospital authorities had the power, among other things, to acquire and operate hospitals and other public health facilities. (*Id.* at p. 1008.)

2.1 Summary of pre-*North Carolina* case law

The United States Supreme Court jurisprudence leading up to *North Carolina, supra,* 135 S.Ct. 1101, set forth varying requirements for state-action immunity that largely depend upon the character of the entity engaging in the anticompetitive conduct. Under the pre-*North Carolina* jurisprudence, the application of state-action immunity depends upon whether the entity engaging in the anticompetitive activity is the state, a municipality, a private party, or an agency delegated authority by the state. A state acting in its sovereign capacity is automatically exempt from the operation of antitrust laws. (See *Parker, supra,* 317 U.S. at p. 352; *Hoover, supra,* 466 U.S. at pp. 567-568.)[4] A municipality is entitled to state-action immunity if it engages in anticompetitive activities pursuant to a clearly articulated and affirmatively expressed state policy to displace competition. (*Town of Hallie, supra,* 471 U.S. at p. 44.) A private party is entitled to state-action immunity only if its anticompetitive conduct meets both the clear articulation and active supervision prongs of the *Midcal* test. (*Patrick, supra,* 486 U.S. at p. 100.) Lastly, the pre-*North Carolina* jurisprudence established that an entity that has been delegated state powers, and thus constitutes a state agency for limited purposes, is not automatically entitled to state-action immunity with regard to its anticompetitive activities. (*Goldfarb, supra,* 421 U.S. at pp. 791-792.) However, that jurisprudence provided less defined standards for determining when such an entity is entitled to state-action immunity.

For instance, in *Hoover,* the United States Supreme Court stated that when the activity is that of a "nonsovereign state representative," such as a committee appointed by a state supreme court, the activity must be conducted pursuant to a clearly articulated state policy to displace competition and the degree of the state's supervision of the activity is also "relevant to the inquiry." (*Hoover, supra,* 466 U.S. at p. 569.) Whereas, in *Phoebe Putney,* the court left open the question of whether *Midcal's* active supervision requirement applies to "substate governmental entities," such as hospital authorities cloaked by the state legislature with governmental authority. (*Phoebe Putney, supra,* 133 S.Ct. at pp. 1009-1010.) Additionally, in *City of Columbia,* the court noted the possibility that a state acting as a market participant rather than a regulator may not be ipso facto exempt under the state-action doctrine, and *Phoebe Putney* also recognized the potential application of the market participant exception to state-action immunity. (*Id.* at p. 1010, fn. 4; *City of Columbia, supra,* 499 U.S. at p. 379.) However, prior to *North Carolina,* no United States Supreme Court case had actually applied a market participant exception to deny state-action immunity to a state agency that engages in anticompetitive conduct.[5]

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[4] "[W]hen a state legislature adopts legislation, its actions constitute those of the State, [citation] and ipso facto are exempt from the operation of the antitrust laws." (*Hoover, supra,* at pp. 567-568.)

[5] In its discussion of states acting as market participants in *City of Columbia,* the United States Supreme Court referenced *Union Pacific Railroad Co. v. United States* (1941) 313 U.S. 450,

(continued...)

Thus, the classification of an entity will guide a court in determining which, if any, of *Midcal's* clear articulation and active supervision requirements must be satisfied to entitle the entity to state-action immunity. In this regard, the pre-*North Carolina* jurisprudence provides guidance concerning what is required to satisfy *Midcal's* clear articulation and active supervision requirements.

Regarding clear articulation, the United States Supreme Court has stated that, although compulsion is often the best evidence, "a state policy that expressly *permits*, but does not compel, anticompetitive conduct may be 'clearly articulated' within the meaning of *Midcal*." (*Southern Motor Carriers Rate Conference, Inc. v. United States* (1985) 471 U.S. 48, 61-62; emphasis in original; hereafter *Southern Motor*.) It is not necessary for the state to explicitly require the anticompetitive activity because it can be presumed that anticompetitive effects logically result from broad authority to regulate. (*Town of Hallie, supra*, 471 U.S. at p. 42.) As long as the state statutes are not neutral[6] and "[contemplate] the kind of action complained of," this is sufficient to satisfy the clear articulation requirement of the state-action test. (*Id.* at p. 44.) Therefore, the clear articulation requirement is satisfied "if suppression of competition is the 'foreseeable result' of what the statute authorizes." (*City of Columbia, supra*, 499 U.S. at p. 373.)[7]

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where the court held Kansas City liable for certain anticompetitive activity that it engaged in in its capacity as an owner and operator of a wholesale produce market. (*City of Columbia, supra*, at p. 375.) However, other than this brief discussion in *City of Columbia*, there has been no further elaboration by the United States Supreme Court concerning the application of the market participant exception.

Prior to *North Carolina*, several federal circuit courts of appeal were split regarding the recognition of a market participant exception. Some federal circuit courts of appeal recognized a market participant exception (see *A.D. Bedell Wholesale Co. v. Philip Morris Inc.* (3rd Cir. 2001) 263 F.3d 239, 265, fn. 55; *VIBO Corp. v. Conway* (6th Cir. 2012) 669 F.3d 675, 687; and *Washington State Electrical Contractors Ass'n. v. Forrest* (9th Cir. 1991) 930 F.2d 736, 737), and some did not (see *SSC Corp. v. Town of Smithtown* (2nd Cir. 1995) 66 F.3d 502, 517; *Limeco v. Division of Lime of Mississippi Dept. of Agriculture & Commerce* (5th Cir. 1985) 778 F.2d 1086, 1087; and *Paragould Cablevision v. City of Paragould* (8th Cir. 1991) 930 F.2d 1310, 1312-1313).

[6] The United States Supreme Court has held that a neutral home rule amendment to a state constitution that provides a municipal government with general authority to govern local affairs does not constitute "clear articulation." (*Community Communications Co. v. Boulder* (1982) 455 U.S. 40, 51-52.)

[7] For example, in *City of Columbia*, the suppression of competition was a foreseeable result of a state statute that authorized municipalities to regulate the use of land and the construction of buildings and other structures within their boundaries. (*Id.* at. pp. 370 & 373.) However, in *Phoebe Putney*, the suppression of competition was not a foreseeable result of a neutral grant of general corporate powers to a substate governmental entity. (*Phoebe Putney, supra*, 133 S. Ct. at pp. 1011-1012.)

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Regarding active supervision, this requirement stems from the recognition that "Where a private party is engaging in the anticompetitive activity, there is a real danger that he is acting to further his own interests, rather than the government interests of the State." (*Town of Hallie, supra,* 471 U.S. at p. 47.) As such, "The active supervision prong of the *Midcal* test requires that state officials have and exercise power to review particular anticompetitive acts of private parties and disapprove those that fail to accord with state policy." (*Patrick, supra,* 486 U.S. at p. 101.) Further, potential state supervision does not constitute active state supervision. (*Ticor, supra,* 504 U.S. at p. 638.)

In sum, the first prong of the *Midcal* test for state-action immunity is met if suppression of competition is the foreseeable result of a state statute. And the second prong of the *Midcal* test for state-action immunity is met if state officials have and exercise power to review anticompetitive decisions and disapprove those that fail to accord with state policy. In other words, the state supervision must be active rather than a mere potential for supervision. However, the *North Carolina* decision described below further elucidated when and how the *Midcal* test would apply with regard to an entity to which the state has delegated regulatory authority.

3. The *North Carolina* decision

The United States Supreme Court in *North Carolina* specifically addressed the issue of whether a state dental board controlled by active market participants that engaged in anticompetitive conduct was entitled to state-action immunity from liability under the Sherman Act. In that case, the entity claiming state-action immunity was the North Carolina State Board of Dental Examiners (SBDE), which was established as "'the agency of the State for the regulation of the practice of dentistry'" whose "principal duty is to create, administer, and enforce a licensing system for dentists." (*North Carolina, supra,* 135 S.Ct. at p. 1107.) The SBDE's duties included the authority to file suit to enjoin the unlawful practice of dentistry and the SBDE was authorized to promulgate rules and regulations governing the practice of dentistry in the state, provided those mandates were not inconsistent with state law and were approved by the North Carolina Rules Review Commission, whose members are appointed by the state legislature. (*Id.* at p. 1108.) The SBDE was comprised of eight members, six of whom were required to be licensed dentists engaged in the active practice of dentistry and to be elected by other licensed dentists in North Carolina through an election conducted by the SBDE. (*Ibid.*)[8] There was no mechanism for the removal of an elected member of the SBDE by a public official, and the SBDE members were required to swear an oath of office and to comply with the state's Administrative Procedure Act and open meeting laws. (*Ibid.*)

(...continued)

[8] The other two SBDE members were a licensed and practicing dental hygienist elected by other licensed hygienists and a "consumer" appointed by the Governor. (*Ibid.*)

The anticompetitive activity at issue in *North Carolina* was the SBDE's issuance of cease-and-desist letters on its official letterhead to nondentist teeth whitening service providers and product manufacturers that directed the recipients to cease "all activity constituting the practice of dentistry." (*North Carolina, supra,* 135 S.Ct. at p. 1108.)[9] At the time, neither North Carolina's statutory definition of the practice of dentistry nor the SBDE's official rules and regulations defined the practice of dentistry as specifically including, or not including, teeth whitening. (*Id.* at p. 1116.)

The court in *North Carolina* held that the SBDE was a nonsovereign actor controlled by active market participants, and as such "enjoys *Parker* immunity only if it satisfies two requirements: 'first that the "challenged restraint ... be one clearly articulated and affirmatively expressed as state policy," and second that the "policy ... be actively supervised by the State."' [Citations.]" (*North Carolina, supra,* 135 S.Ct. at p. 1110.) The court and the parties assumed that the clear articulation requirement was satisfied, but the court concluded that "the Board did not receive active supervision by the State when it interpreted the Act as addressing teeth whitening and when it enforced that policy by issuing cease-and-desist letters to nondentist teeth whiteners." (*Ibid.*)

The court explained that automatic state-action immunity does not apply when the state "delegates control over a market to a *non-sovereign actor,*" which is "one whose conduct does not automatically qualify as that of the sovereign State itself," and "[s]tate agencies are not simply by their governmental character sovereign actors for purposes of state-action immunity." (*North Carolina, supra,* 135 S.Ct. at pp. 1110-1111; emphasis added.) According to the court, a limitation on state-action immunity is "most essential when the State seeks to delegate its regulatory power to active market participants." (*Id.* at p. 1111.) Therefore, the court determined that state-action immunity "requires that the anticompetitive conduct of nonsovereign actors, especially those authorized by the State to regulate their own profession, result from procedures that suffice to make it the State's own." (*Ibid.*)

In deciding to apply both *Midcal* requirements, the court acknowledged that *Town of Hallie, supra,* exempted municipalities from the active supervision requirement. (*North Carolina, supra,* 135 S.Ct. at p. 1112.) The court distinguished *Town of Hallie* by explaining that active market participants "ordinarily have none of the features justifying the narrow exception" for municipalities, which are electorally accountable and exercise "a wide range of governmental powers across different economic spheres, substantially reducing the risk that it would pursue private interests while regulating any single field." (*North Carolina, supra,* at pp. 1112-1113.) Having made this distinction, the court concluded that "a state board on which *a controlling number of decisionmakers* are active market participants in the occupation the

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[9] At the time the SBDE issued the cease-and-desist letters, several of its dentist members "earned substantial fees" for performing teeth whitening services. (*Ibid.*)

board regulates must satisfy *Midcal's* active supervision requirement in order to invoke state-action antitrust immunity." (*Id.* at p. 1114; emphasis added.)[10]

In applying the active supervision requirement, the court found no evidence of any decision by the state to initiate or concur with the SBDE's actions against nondentists.[11] Instead, the court found that the SBDE relied upon cease-and-desist letters "rather than any powers at its disposal that would invoke oversight by a *politically accountable official.*" (*Ibid.*; emphasis added.) The court then went on to describe general standards for active supervision, but cautioned that any inquiry regarding active supervision is "flexible and context-dependent." (*Ibid.*) In this regard, the court described the standards for active supervision as follows:

> "Active supervision need not entail day-to-day involvement in an agency's operations or micromanagement of its every decision. Rather, the question is whether the State's review mechanisms provide 'realistic assurance' that a nonsovereign actor's anticompetitive conduct 'promotes state policy, rather than merely the party's individual interests.' [Citations.] [¶] The Court has identified only a few constant requirements of active supervision: The supervisor must review the substance of the anticompetitive decision, not merely the procedures followed to produce it [citation]; the supervisor must have the power to veto or modify particular decisions to ensure they accord with state policy [citation]; and the 'mere potential for state supervision is not an adequate substitute for a decision by the State' [citation]. Further, the state supervisor may not itself be an active market participant. In general, however, the adequacy of supervision otherwise will depend on all the circumstances of a case." (*Id.* at pp. 1116-1117.)

In summary, the court found that active supervision is a fact-specific inquiry that requires, at a minimum, review of an anticompetitive decision by a state supervisor who is not an active market participant and who has the power to veto or modify the anticompetitive decision, which requires an actual decision by the state, rather than the mere potential for a decision.

The dissent in *North Carolina* pointed out several ambiguities in the court's opinion and noted that "it is not clear what sort of changes are needed to satisfy the test that the Court now adopts." (*North Carolina, supra,* 135 S.Ct. at p. 1123 (dis. opn. of Alito, J.).) For

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[10] Because the case did not present a claim for money damages, the court left open the question of whether under some circumstances state agency officials, including board members, may enjoy immunity from damages liability. However, the court provided that "the States may provide for the defense and indemnification of agency members in the event of litigation." (*Id.* at p. 1115.)

[11] Because the SBDE did not contend that its anticompetitive conduct was actively supervised by the state, there was no evidence to review and the court did not review any specific supervisory systems. (*North Carolina, supra,* 135 S.Ct. at p. 1116.)

example, the dissent questioned at what point active market participants constitute a "controlling number of [the] decisionmakers" of a state agency to invoke the active supervision requirement. (*Ibid.*) The dissent posited whether a controlling number is a majority, or if something less than a majority would suffice, such as where active market participants constitute a powerful voting bloc. (*Ibid.*) The dissent also questioned who constitutes an active market participant by postulating the following:

> "If Board members withdraw from practice during a short term of service but typically return to practice when their terms end, does that mean that they are not active market participants during their period of service?
>
> "What is the scope of the market in which a member may not participate while serving on the board? Must the market be relevant to the particular regulation being challenged or merely to the jurisdiction of the entire agency? Would the result in the present case be different if a majority of the Board members, though practicing dentists, did not provide teeth whitening services? What if they were orthodontists, periodontists, and the like? And how much participation makes a person 'active' in the market?" (*Ibid.*)

Ultimately, the dissent conceded that "The answers to these questions are not obvious, but the States must predict the answers in order to make informed choices about how to constitute their agencies." (*Ibid.*)

4. Legal standards for grant of state-action immunity

Based on the foregoing, it is our opinion that a court would apply the following legal standards to a claim for state-action immunity from the Sherman Act in light of the United States Supreme Court's decision in *North Carolina*.

4.1 State acting as sovereign

Actions of the state acting as sovereign, such as legislation or decisions of the state supreme court acting legislatively, *ipso facto* are exempt from the Sherman Act. (*North Carolina, supra*, 135 S.Ct. at p. 1110.)

4.2 Municipalities

Municipalities are entitled to state-action immunity if their anticompetitive conduct is pursuant to a clearly articulated and affirmatively expressed state policy to displace competition. (*City of Lafayette, supra*, 435 U.S. at pp. 410 & 413; *Town of Hallie, supra*, 471 U.S. at p. 44.)

4.3 Private parties

Private parties delegated authority by the state are entitled to state-action immunity only if their anticompetitive conduct is pursuant to a clearly articulated and affirmatively expressed state policy to displace competition, and the policy is actively supervised by the State. (*Patrick, supra*, 486 U.S. at p. 100.)

4.4 State agencies not controlled by active market participants

Although *North Carolina* did not specifically address state agencies not controlled by active market participants, the court did state that "State agencies are not simply by their governmental character sovereign actors for purposes of state-action immunity." (*North Carolina, supra,* 135 S.Ct. at p. 1111.) As such, the anticompetitive actions of a state agency are not automatically entitled to state-action immunity, unless they result from procedures that suffice to make it the state's own action. (*Ibid.*) Whether those procedures include both of *Midcal's* clear articulation and active supervision requirements was not specifically addressed by the court in *North Carolina*; however, the court reiterated that only the first requirement applies to municipalities because they are electorally accountable and there is minimal risk of municipal officers pursuing private, nonpublic aims. (*North Carolina, supra,* 135 S.Ct. at pp. 1112-1113.) Therefore, it is our opinion that, like municipalities, state agencies not controlled by active market participants are entitled to state-action immunity if their anticompetitive actions satisfy only *Midcal's* clear articulation requirement, as long as their actions pose minimal risk of furthering private interests over those of the state.

4.5 State agencies controlled by active market participants

A state agency or board on which "a controlling number of decisionmakers are active market participants" in the occupation that the state agency regulates is entitled to state-action immunity if it acts pursuant to a clearly articulated and affirmatively expressed state policy to displace competition, and is actively supervised by the state. (*North Carolina, supra,* 135 S.Ct. at p. 1114.) It is not clear what "a controlling number of decisionmakers" entails, but in our view, the more likely it is that the members will be able to control decisions of the agency or board, the more likely it is that a court will find them to constitute a "controlling number." For instance, a majority of the voting members would almost certainly be considered a controlling number, but a court could consider an influential voting bloc to also constitute a controlling number. (*Id.* at p. 1123.) Likewise, it is unclear what it means to be an "active market participant." (*Ibid.*) At the very least we think an active market participant would include a person currently licensed and practicing in the field being regulated by the state agency or board because of the greater likelihood that such a person will be influenced by private, rather than public, interests. Ultimately, we think a court would make such a determination on a contextual basis using a spectrum analysis. For example, at one end of the spectrum would be a person with no connection to the industry being regulated, and at the other end of the spectrum would be a person currently practicing in the precise industry being regulated. In our view, the closer a person's ties are to the industry being regulated, the greater the likelihood that the person will act pursuant to private rather than public interests, and the more likely a court would be to consider them an active market participant.

4.6 Clear articulation

A state policy to displace competition is clearly articulated when the displacement of competition is "the inherent, logical, or ordinary result of the exercise of authority delegated by the state legislature. In that scenario, the State must have foreseen and implicitly

endorsed the anticompetitive effects as consistent with its policy goals. [Citation.]" (*North Carolina, supra,* 135 S.Ct. at p. 1112.) Although "compulsion is often the best evidence that the State has a clearly articulated and affirmatively expressed policy to displace competition," it is not required. (*Southern Motor, supra,* 471 U.S. at p. 62.) As long as the state statute providing authorization is not neutral and "contemplate[s] the kind of action complained of," in our view, a court would find it sufficient to satisfy the clear articulation requirement of the state-action test. (*Town of Hallie, supra,* 471 U.S. at pp. 43-44.)

4.7 Active state supervision

Any inquiry regarding active state supervision is "flexible and context-dependent" and should focus on whether the state's "review mechanisms provide 'realistic assurance' that a nonsovereign actor's anticompetitive conduct 'promotes state policy, rather than merely the party's individual interests.' [Citations.]" (*North Carolina, supra,* 135 S.Ct. at p. 1116.) As such, we think a court would analyze the presence of active supervision on a spectrum such that the more the state supervision assures the promotion of state over private interests, the more likely a court would be to find sufficient active supervision for purposes of state-action immunity. However, it is our opinion that a court would require, at a minimum, that the three criteria specified in *North Carolina* be satisfied for a finding of active supervision: (1) the anticompetitive decision is reviewed by a state supervisor;[12] (2) the state supervisor has the actual power, rather than the mere potential, to veto or modify an anticompetitive decision; and (3) the state supervisor is not an active market participant. (*Id.* at pp. 1116-1117.)

5. Conclusion

Ultimately, the United States Supreme Court has a "settled policy of giving concrete meaning to the general language of the Sherman Act by a process of case-by-case adjudication of specific controversies." (*Cantor v. Detroit Edison Co.* (1976) 428 U.S. 579, 603; hereafter *Cantor.*)[13] Therefore, we cannot affirmatively provide every instance in which a

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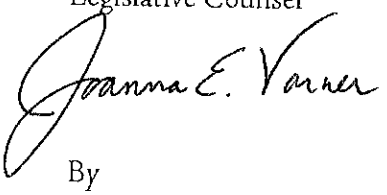
[12] In finding no evidence of active supervision, the court noted that SBDE's anticompetitive actions did not invoke oversight by a "politically accountable official." (*Ibid.*) Therefore, one could argue that the state supervisor should be politically accountable; however, the minimum requirements articulated by the court for active supervision do not specify this requirement. Accordingly, although perhaps not required, supervision by a politically accountable official may influence a court to view the state's supervision on the side of the spectrum that favors a grant of state-action immunity.

[13] In *Cantor,* the court rejected the application of "a simple rule than can easily be applied in any case in which a state regulatory agency approves a proposal and orders a regulated company to comply with it." (*Ibid.*)

court would grant state-action immunity. However, it is our opinion that, in light of the decision in *North Carolina State Board of Dental Examiners v. Federal Trade Commission* (2015) 574 U.S. __ [135 S.Ct. 1101], a court would use the legal standards described above to decide whether to grant state-action immunity from Sherman Act liability.

Very truly yours,

Diane F. Boyer-Vine
Legislative Counsel



By
Joanna E. Varner
Deputy Legislative Counsel

JEV:sjk