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State action immunity: a wavering defense

William C. Lavery and Ashley Eickhof examine the topic of state action immunity: still a viable and potentially powerful affirmative defense, but one that is falling into increasing disfavor

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STATE ACTION IMMUNITY: A WAVERING DEFENSE

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The Department of Justice ("DOJ") and Federal Trade Commission ("FTC") have had a long-running campaign to narrow the scope of the state action doctrine (including policy statements, a State Action Task Force, a number of amicus briefs, and enforcement actions dating back as far as at least the early 2000s), and while the doctrine unquestionably continues to offer a viable and potentially powerful defense to certain state and quasi-state entities for conduct that may be otherwise deemed anticompetitive, its scope has been narrowed considerably in recent years (and courts that may have once been lax in its application now tend to apply it more judiciously). There are also a number of signs that suggest we can expect continued or even increased enforcement – including statements by federal antitrust enforcers themselves and a number of court decisions applying recent Supreme Court precedent narrowing the scope of the state action doctrine. This article briefly addresses some of these signals, and posits that we can expect increased enforcement and potentially an even further narrowing of the state action doctrine as a viable defense in the future. It also offers some suggestions on how state-affiliated entities can avoid falling into obvious traps and becoming the target of enforcement for behavior that may otherwise be a perfectly legitimate exercise of sovereign power.

I. Background of the state action doctrine and its increased narrowing by the courts

In general, the "state action doctrine," also referred to as "*Parker* immunity," confers immunity from the federal antitrust laws for "anticompetitive conduct by the States when acting in their sovereign capacity."[1] This immunity also extends, in some instances, beyond the state itself to municipalities, state boards, agencies and other entities acting at the direction of the state in an official capacity. But the Supreme Court has long held that "*Parker* immunity is not unbounded" and has increasingly narrowed those bounds, recently stating: "given the fundamental national values of free enterprise and economic competition that are embodied in the federal antitrust laws, 'state action immunity is disfavored, much as are repeals by

Parker immunity can also extend beyond the state itself to municipalities, state boards, agencies and other entities

implication'."[2] The Supreme Court has also repeatedly made it clear in recent years – including in both *North Carolina State Bd.* and *Phoebe Putney* – that "state-action immunity is disfavored" because it conflicts with "the fundamental national values of free enterprise and economic competition that are embodied in the federal antitrust laws."[3] As a result, lower courts have tended to apply the doctrine judiciously.

An entity "may not invoke *Parker* immunity unless the actions in question are an exercise of the State's sovereign power," and the affirmative defense typically applies only where (1) the challenged restraint is "one clearly articulated and affirmatively expressed as state policy," and (2) the policy is "actively supervised by the State."[4] But this seemingly simple, two-pronged test disguises a number of traps that can ensnare unwary parties. For example, it is not always obvious when the active supervision prong must be met – the Supreme Court has held that municipalities and other state subdivisions may be entitled to immunity even without active state supervision, but state agencies may not be.[5] However, the line between municipalities, state subdivisions, agencies (whether controlled by market participants or not), and other entities acting pursuant to state authorization is often less than clear. In *North Carolina State Bd.*, for example, the Supreme Court held that entities designated by states as "agencies" are not automatically exempt from the "active supervision" requirement simply because of their designation by the state as an agency – and certainly are not exempt where they are controlled by active market participants.[6] The result has been a tendency to require active supervision in an increasing number of cases.

The Supreme Court and Circuit Courts have also, in recent years, made the "clear articulation" requirement harder to meet, generally holding that broad delegations of state power to state agencies or other quasi-state actors generally will not confer antitrust immunity. Rather, as the Supreme Court explained in *Phoebe Putney*, the state action defense requires evidence that the state "affirmatively contemplated the displacement of competition such that the challenged anticompetitive effects can be attributed to the 'state itself'" – i.e., not only the anticompetitive "conduct" but also the anticompetitive "effect" must have been foreseen by the state itself and clearly articulated in the statute.[7]

Emboldened by recent state action decisions by the courts, federal antitrust agencies have remained active on the enforcement front

Though it predated *Phoebe Putney*, in an opinion authored by then-Judge Gorsuch, the Tenth Circuit's *Kay Electric* decision illustrates the close statutory reading that courts now tend to apply.[8] In *Kay Electric*, the plaintiff alleged that a city in Oklahoma had unlawfully tied the provision of sewage services to the purchase of electricity. The principal issue was whether the city enjoyed state action immunity pursuant to Oklahoma law.[9] Judge Gorsuch found that the city enjoyed no such immunity, and held that the presence of "general enabling statutes conferring on the city the authority to do business" in sewage and electricity was insufficient to trigger immunity.[10] What was needed instead was a specific statute "authoriz[ing] the kind of anticompetitive conduct alleged."[11]

The Tenth Circuit's *Kay Electric* decision illustrates the close statutory reading that courts now tend to apply

If and when the issue comes before the Supreme Court again, Justice Gorsuch seems likely to support an even further narrowing of the "clear articulation" requirement, as outlined in *North Carolina Board* and *Phoebe Putney*, to make clear the exception applies only to anticompetitive conduct expressly written in the statute – not conduct that may be a "foreseeable result" of the statute. Indeed, Justice Gorsuch even seemed to express disappointment with the Supreme Court for not making this clear at the time – some might even say daring them to take the issue up to provide clarity – instead he cited Professors Areeda and Hovenkamp's leading treatise which suggests a more bright-line "clear articulation" standard.[12]

II. Federal antitrust enforcers may view the recent narrowing of the state action doctrine as an opportunity for increased enforcement

Perhaps emboldened by the string of recent state action decisions by the Supreme Court and lower courts,[13] the federal antitrust agencies have remained active on the enforcement front. In its first antitrust action against a state entity since its 2015 victory in *North Carolina State Bd.*,[14] on May 30, 2017 the FTC filed an administrative complaint against the Louisiana Real Estate Appraisers Board ("LREAB") alleging the LREAB, a state agency controlled by licensed real estate appraisers, violated Section 5 of the FTC Act by unreasonably restraining competition for real estate services provided to appraisal management companies ("AMCs"). The FTC objects to an LREAB policy that requires AMCs to pay fees to individual appraisers that equal or exceed median fees listed in surveys commissioned by the LREAB. Though state and federal law requires AMCs to pay appraisers a "customary and reasonable fee" for their services, the FTC appears to

be betting that its Administrative Law Judge will reject the LREAB's state action immunity defense.[15]

In a press release accompanying the FTC's Complaint, Tad Lipsky, the then-Acting Director of the Bureau of Competition, emphasized that "the Commission remains vigilant and will exercise its prescribed authority" to challenge anticompetitive state activity when doing so would be "economically sound and otherwise consistent with the public interest."[16] Similarly, Maureen Ohlhausen, the Acting Chairman of the FTC, has also boasted of the Commission's efforts to "define and confine the anticompetitive effects that flow from state action,"[17] even as she has counseled restraint in other areas of antitrust enforcement. In statements the Acting Chairman has also pointed to the Commission's "victory at the Supreme Court in North Carolina Dental as being particularly notable," and supported the Commission's role in "forc[ing] states wishing to limit competition to clearly articulate that goal and to actively supervise its application by [state actors who are also] market participants."[18]

Recent cases send a clear message: tread carefully and consult antitrust counsel if the conduct potentially violates the law

Indeed, recently, and not long after filing suit against the LREAB, the FTC nearly brought a second challenge against a state board for exceeding the scope of its legislative mandate.[19] In a rarely issued closing letter, the FTC announced that it would not pursue charges against the Texas Medical Board for restricting the practice of telemedicine and telehealth only because the state legislature enacted a law addressing the Commission's competitive concerns. But the FTC warned that where state boards engage in anticompetitive conduct that is "beyond the scope of state policy and/or supervision," "they are subject to federal antitrust law."[20]

Makan Delrahim, President Trump's nominee to be the United States Assistant Attorney General for the Antitrust Division,[21] has likewise advocated for limiting state action immunity, and recently stated at his confirmation hearing that, "I'm an open book on this issue. In my views on the Antitrust Modernization Commission, if there are immunities from the antitrust laws, I think it should be done by this body [Congress], not impliedly from the courts."

Many entities that found themselves in trouble didn't pay attention, or purposely adopted an overly broad reading of the relevant statutes

In yet another decision that may embolden federal antitrust enforcers and private plaintiffs, on June 12, 2017 – in a case involving the state action doctrine that has been followed closely by antitrust practitioners – the Ninth Circuit in *SolarCity v. Salt River Project Ag. Improvement & Power Dist* held that the collateral order doctrine does not allow defendants to immediately appeal a finding that the defendant lacks immunity from the federal antitrust laws under the state action doctrine.[22] Usually a defendant cannot appeal until a court enters a final decision terminating the case, but the "collateral order doctrine" enables parties to immediately appeal certain non-final decisions that resolve important issues separate from the merits of the case where they would be effectively unreviewable on appeal if the defendant was forced to wait until after the case ended to appeal. Some immunities, such as Eleventh Amendment immunity and qualified immunity, fall into this category and are immediately reviewable. Whether state action immunity orders are immediately appealable has always been a closer question and courts have had mixed views, but after the Ninth Circuit's *SolarCity* decision, the balance has tipped towards denying immediate appeals. The Fourth, Sixth, and Ninth Circuits do not allow immediate appeals of denials of state action immunity, while the Fifth and Eleventh Circuits do allow immediate appeals. This decision was a victory for both antitrust enforcers and private plaintiffs wishing to narrow the state action doctrine, who filed a number of amicus briefs both in this case and others addressing this issue over the years.

III. State-affiliated entities should take particular caution to ensure their conduct complies with the antitrust laws

For state agencies and other quasi-state actors acting at the direction of states, the FTC's action against the LREAB – as well as the action it nearly brought against the Texas Medical Board – should be of more than academic interest. It demonstrates that even under the Trump Administration, the federal antitrust enforcers stand ready to challenge anticompetitive conduct by quasi-state entities that is not clearly sanctioned – and in most cases, supervised – by the state itself. The Ninth Circuit's decision in *SolarCity* should likewise give such agencies and quasi-state actors some pause as it solidified that in the majority of Circuits, state action immunity does not protect defendants from lawsuits altogether (it is only a defense to liability) and, assuming any such cases get past motions to dismiss, such state-affiliated entities may have to go through discovery and potentially trial before re-raising the defense.

For state agencies, boards, utilities, and other entities authorized by the state to exercise control over markets and engage in

activity that would otherwise potentially violate the antitrust laws, recent enforcement activity and state action cases send a clear message: tread carefully and consult antitrust counsel if the conduct potentially violates the antitrust laws absent their status as a state-affiliated entity. Entities may not be able to rely on the vague "foreseeable results" standard and instead should likely base their actions on a stricter reading of the statute, and in many cases – particularly in cases where entities straddle the line between state subdivisions and state instrumentalities – should ensure there is "active supervision" of the conduct itself for anything close to the line. The good news is: most of the time it isn't difficult to meet both prongs of the *Midcal* test if entities plan ahead and ensure their actions are in line with what the statute actually says. The federal agencies – and private plaintiffs – seem to be increasingly eager to pursue claims for violations against entities that do not. ■

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Footnotes

1 *North Carolina State Bd. of Dental Examiners v. FTC*, 135 S. Ct. 1101, 1110 (2015) (citing *Parker v. Brown*, 317 U.S. 341, 350-51 (1943)).

2 *North Carolina State Bd.*, 135 S. Ct. at 1110 (citing *FTC v. Phoebe Putney Health Sys., Inc.*, 568 U.S. 216, 225 (internal quotations omitted).

3 *North Carolina State Bd.*, 135 S. Ct. at 1110 (2015); *Phoebe Putney*, 568 U.S. at 225 (2013).

4 *North Carolina State Bd.*, 135 S. Ct. at 1110; see also *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97 (1980).

5 *Phoebe Putney*, 568 U.S. at 226 ("[U]nlike private parties, [local governmental] entities are not subject to the 'active supervision requirement' because they have less of an incentive to pursue their own self-interest under the guise of implementing state policies.").

6 *North Carolina State Bd.*, 135 S. Ct. at 1115 (holding that "the need for supervision turns not on the formal designation given by States to regulators but on the risk that active market participants will pursue private interests in restraining trade").

7 *Phoebe Putney*, 568 U.S. at 229 (stating that litigants claiming state action immunity must convince courts that the state "fores[aw] and implicitly endorsed the anticompetitive effects as consistent with its policy goals.").

8 *Kay Elec. Co-op. v. City of Newkirk, Okla.*, 647 F.3d 1039 (10th Cir. 2011).

9 *Id.* at 1041.

10 *Id.* See also *id.* at 1045 ("[I]t is well settled that general municipal charters are never enough to trigger [state action] protections.").

11 *Id.* at 1044. See also *Edinboro Coll. Park Apartments v. Edinboro Univ. Found.*, 850 F.3d 567, 580 (3d Cir. 2017) (holding that a defendant "University's conduct complie[d] with a clearly articulated state policy because mandating on-campus residency is a foreseeable consequence of the legislative mandate to provide appropriate student living facilities").

12 *Id.* at 1043.

13 See *id*.

14 *North Carolina State Bd.*, 135 S. Ct. at 1101.

15 Notably, on July 19, 2017, the LREAB filed a motion to stay the FTC action on the grounds that the state legislature intended to change the statute at issue to comply with, among other things, the "active supervision" requirement of the state action doctrine, essentially mooting the issue. The FTC opposed the motion as moot. On August 2, 2017, the FTC's ALJ granted the motion to stay while the state passes new legislation to clearly address oversight of the board's regulations—requirements that will presumably satisfy the "active supervision" prong of *Midcal*.

16 Complaint, In the Matter of Louisiana Real Estate Appraisers Board, FTC Docket No. 9374 (May 30, 2017); Press Release, FTC Challenges Louisiana Real Estate Appraisers Board Regulations that Restrict Competition (May 31, 2017), https://www.ftc.gov/news-events/press-releases/2017/05/ftc-challenges-louisiana-real-estate-appraisal-board-regulations.

17 Speech by Acting Chairman of the Federal Trade Commission Maureen K. Ohlhausen, GCR Live 6th Annual Antitrust Law Leaders Forum, The FTC's Path Ahead 8 (Feb. 3, 2017). *See also* Speech by Acting Chairman of the Federal Trade Commission Maureen K. Ohlhausen, The Heritage Foundation, Antitrust Policy for a New Administration 1–2 (Jan. 24, 2017) (noting that she has "championed efforts to reign in possible abuses of government processes, as when a state fails to supervise regulatory boards comprised of active market participants").

18 Antitrust Policy for a New Administration, January 24, 2017, The Heritage Foundation.

19 Statement of the Federal Trade Commission On Commission Vote to Close Investigation of Texas Medical Board's Conduct (June 21, 2017).

20 *Id.*

21 On June 8, 2017, the Senate Judiciary Committee overwhelmingly approved Makan Delrahim's nomination by a vote of 19-1. The nomination will now go before the full Senate and is expected to eventually be approved.

22 *SolarCity v. Salt River Project Ag. Improvement & Power Dist.*, No. 15-17302, 2017 WL 2508992 (Slip Opinion, 9th Cir. June 12, 2017).