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This Isn't North Carolina, Toto: California Boards Should Survive the Dental Board Case

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In February of this year, the United States Supreme Court decided the case of *North Carolina State Board of Dental Examiners v. Federal Trade Commission*, No. 13-354, affirming a lower court decision that the FTC could order the Board to stop sending cease-and-desist letters to non-dentist teeth whiteners and affirming that the Board of Dental Examiners was not immune as a state agency from the FTC's power to enforce the federal antitrust laws against it. The Court found that although the Board was a body legislatively created by the State of North Carolina, its actions were not per se immune from federal antitrust scrutiny but must meet the ''two part test set forth in *California Retail Liquor Dealers Assn. v. Midcal Aluminum, Inc.*, 445 U.S. 97 [1980],'' which held that''[a] state law or regulatory scheme cannot be the basis for antitrust immunity unless, first, the State has articulated a clear policy to allow the anticompetitive conduct, and second, the State provides active supervision of [the] anticompetitive conduct'' (quoted in *Dental Examiners* at III.C).

Essentially all states regulate their learned professions and various other occupations, such as, in California, barbers and vehicle repossessors among about 40 other trades. Many or most of such states exercise that control through oversight boards whose membership is numerically dominated by persons licensed in and actually practicing such professions or trades; see, e.g., Cal. Bus. & Prof. Code § § 2001, 2007 (Medical Board: 15 members, of whom 7 ''shall be public members''), 2702 (Board of Registered Nursing: of 9 members, 5 shall be registered nurses with stated qualifications; 4 members ''shall represent the public at large and shall not be licensed under any board * * *''); 4001 (State Board of Pharmacy: of 13 members, ''seven [shall be] competent pharmacists'' with various specific qualifications). Or there may be a nominal majority of one for the public members, as with the Board of Accountancy (§ 5000: of 15 members, ''8 shall be public members who shall not be licensees of the board or registered with the board'') or the Contractors State Licensing Board (§ § 7000.5, 7001, 7002: of 15 members, 8 shall be public members who ''shall not be licentiates of the board''). Various other boards and bureaus have more pronounced majorities of non-professional members. But as we will mention later, the California boards' balance between public members and members from the professions or vocations being regulated is different from others such as North Carolina's, since all professional members are appointed by the Governor and the Legislature, and

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since the ratio between professionals and nonprofessionals is always close where the professionals are in the majority.

The question logically follows: How is your state's regulation of various professions and other licensed occupations affected by the *North Carolina Dental Examiners* case? This article will examine that issue from the California perspective.

I. A little antitrust history.

In 1943, the Supreme Court declared that persons acting under a California law that controlled the marketing of raisins were immune from federal antitrust regulation, ruling that a program which was operated largely through a committee of growers and that significantly limited the amount of raisins that could enter the market ''derived its authority and its efficacy from the legislative command of the state and was not intended to operate or become effective without that command'' (*Parker v. Brown*, 317 U.S. 341, 350). Concluding that the Sherman Act never intended to limit state action, the Court ruled that ''[t]he state in adopting and enforcing the prorate program made no contract or agreement and entered into no conspiracy in restraint of trade or to establish monopoly but, as sovereign, imposed the restraint as an act of government which the Sherman Act did not undertake to prohibit'' (p. 352). This was a case of first impression, and the newly declared immunity of state action from federal law restraining trade has since led to many tests of that basic formula.[1]

We see no need to relate the full history of the state action exemption, which has been tested and examined in many ways in the intervening 72 years. The courts have been faced with a multitude of state action immunity claims, examining that broad premise from many angles. For purposes of this paper, it is sufficient to return to what has become known during its 35 years of life as the *Midcal* formula, which, to repeat, makes state action immunity from otherwise trade-restrictive conduct depend on two premises: that a state has articulated a clear policy to allow the challenged conduct, and that it ''provides active supervision'' to see that the restraint ''will shelter only the particular anticompetitive acts of private parties that, in the judgment of the State, actually further state regulatory policies'' (*Patrick v. Burget* (1988) 486 U.S. 94, 100-01).

The Supreme Court has not explained what is required to establish that there is actual ''active supervision'' by a state, of anticompetitive conduct that may occur under the state's direction. (Antitrust Developments (Seventh) (2012), p. 1277.)

II. How Will the North Carolina Dental Board Decision Fare Under California's Regulation of Professions and Trades?

Like virtually all states, California has a myriad of boards and bureaus that oversee particular professions and trades. The boards are created by statute. Our desk copies of the Business & Professions Code which contain those statutory creations and their authority, as well as other laws such as unfair competition laws, are easily 4 inches thick, containing literally thousands of specific statutes. We will discuss the Medical Board here at times, both because it is among the larger and more active such bodies and because its authority is typical of the many boards that regulate professions and trades in California.

Much of the Medical Board's authority is disciplinary, involving ''the enforcement of the disciplinary and criminal provisions of the Medical Practice Act,'' although it also issues medical licenses and can review ''the quality of medical practice'' by its licensed physicians and approve medical education and continuing education programs (§ 2004). From the perspective of conduct that is arguably anticompetitive, its authority to issue medical licenses obviously limits competition since fewer licensed physicians mean a tighter supply of vendors in the market for medical services (see *Hoover v. Ronwin* (1984) 466 U.S. 558, holding that although the bar examination restricts the supply of lawyers, it is a permitted restraint since the Arizona Supreme Court's supervision of the admissions process makes that process state action). And the Medical Board's other authority, such as its oversight of medical practice, can certainly be employed to restrict aspects of the health care market. Thus the question arises: are the Medical Board's actions in these areas subject to federal trade regulation laws, or are they part of California's government and thus immune from such challenge?

Before the *North Carolina Dental Board* case, the only decision which held an agency of the state itself liable for federal antitrust violations was *Goldfarb v. Virginia State Bar* (1975) 421 U.S. 773, which held that enforcement of a ***local*** bar association's (minimum) fee schedule by the State Bar violated the antitrust laws and was not exempted from federal scrutiny under the state action exemption of *Parker v. Brown*, although the Virginia State Bar was ''a state agency for some limited purposes'' (*Goldfarb*, p. 790). Last updated prior to *North Carolina Dental*, the ABA Antitrust Section's treatise states that ''[t]he status of state executive departments, agencies and special authorities under the state action doctrine is unclear,'' referencing a case where the Supreme Court had stated both that ''the circumstances in which *Parker* immunity was available to state agencies or officials'' was ''most specifically'' defined in *Midcal*, and that where ''the actor is a state agency, it is likely that active state supervision is not required.'' (Antitrust Developments (Seventh), *supra*, p. 1279.) The *North Carolina* case thus is the first case where a formally constituted public state agency was found to have actually violated the federal antitrust laws through its official actions.

State agencies, acting for all that appears under full state authority, often restrict the conduct of parties subject to their jurisdiction, as for instance limiting the conditions under which a physician may prescribe controlled substances to an addict (Cal. Bus. & Prof. Code § 2241). After *North Carolina Dental*, are such agencies subject to federal antitrust scrutiny for whatever they may do in the course of their state-assigned tasks? It would obviously create huge new areas of antitrust exposure, perhaps for the sponsoring state as well, if a

[1] Interestingly, the Supreme Court also ruled last month in *Horne v. U.S. Department of Agriculture* that a New Deal-era law that requires raisin growers to deposit a large percentage of their crop with the Department of Agriculture violates the Fifth Amendment's takings clause, allowing the growers to obtain compensation from the federal government. While not exactly the same, this program is similar to that upheld in *Parker v. Brown*, showing the extent to which the law has changed in this field in 72 years.

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state's seemingly routine exercise of its police powers could be challenged under federal antitrust law as anticompetitive, or if a whole new system of state supervision – presumably by an independent state agency that could not be accused of self-interest as the professional bureaus now are – must be put in place to preserve state action antitrust immunity.

Or, since *Midcal* now determines whether the conduct of such state boards is subject to state action immunity, what standards are the courts likely to employ to make that determination?

III. The California System

As noted above, the statutory base of California's many boards and bureaus may seem to have given those bodies a free hand to enforce restrictions on the commercial activities of the activities — the professions or trades — that they license; and in the healing arts field, a majority of these regulatory bodies' governing boards consists of members of the regulated work force, even though they are named by the Governor or the Legislature and not by their peers. So, where is the ''active supervision'' of the professional boards which, as *North Carolina Dental* has taught us, is now a *sine qua non* for obtaining state action immunity from antitrust challenges? When one looks at the lengthy statutory definitions that provide the structure of the California licensing boards, there is nothing that immediately suggests such supervision; but see section III.B, below. Are California's licensed professions and trades then subject to a new no-holds-barred antitrust scrutiny, so that no one would likely want to serve in such regulatory capacities and our structure for the oversight of professions and trades would disappear or have to be drastically revised?

The courts will surely be asked in time to answer these questions; but we believe that the *North Carolina Dental* directive that to obtain state action or *Parker v. Brown* immunity, the *Midcal* ''active supervision'' must be provided by an element of state government that is not subject to claims of dual function (regulator and market competitor), is already firmly in place in California through the government's extensive oversight of what the boards which oversee licensed professions and trades do.

A. Historical Prophylactic: Public Members

The public member presence on the professional licensing boards and bureaus in the Department of Consumer Affairs (together collectively, the ''Boards'') was instituted by the California Legislature forty years ago, at the behest of the first administration of current Governor Jerry Brown and of the consumer movement of the day. It responded to the classic question, ''*Quis custodiet ipsos custodes*?'' – ''who will guard the guardians themselves?'' The issue was the public interest, validity and accountability of the state actions taken by the Boards. The response to the challenge was, members of the public on the Boards, appointed by the highest officer of the State, the Governor.

The ''healing arts'' Boards (doctors, dentists, nurses, psychologists and the like) and the Board of Accountancy were restructured to be populated with a one-third ratio of public members, the balance of the Boards to have a majority of public members. All Board members at the time were appointed by the Governor (in contrast to the North Carolina process of selection where the state dental association was the appointing power), but in the early 1980's the Legislature granted its respective houses, the Assembly and the Senate, the power to make certain of the public member appointments. This diversity of appointing power broadened the base of political and public accountability for the state actions taken by the Boards as entities of the State of California: both the Governor and the Legislature were appointing the agents of the State, including the guardians of the guardians, the public members.

It had not always been so. Traditionally the Boards had acted more as public extensions of their counterpart professional associations: although their members were not elected by the associations, as in North Carolina, the associations did make their recommendations to the Governor's Office, which were routinely honored. The advent of public members to the Boards occasioned the uncovering of a range of professional-protective practices, some of them startlingly abusive for processes considered ''state action.'' For examples. . .

The new public members on the Dental Board discovered that the supposedly anonymous scoring system for the ''hands-on'' component of the licensing exam was anything but: the candidates were to be identified on the rating sheets exclusively by numbers, the on-site dentist reviewers of the performance of the candidates were to use only the number. But the aggregate scoring sheets for all the candidates had printed across their top a noxious coding construct that read in part, ''V – veteran, C – colored, J – Jap, F – female, NG – nice guy.'' The applicable lettering was then hand-written in the margin next to the candidate's number, along with identification of an out-of-state dental school the candidate had attended. Such was the process used to screen out candidates who might not be that acceptable or who would be coming in to California in competition with the existing dentists.

The new public members on the Board of Accountancy discovered that whereas licensure applicants from the British Commonwealth ''charter'' countries were exempted from taking the qualifying California licensure examination, candidates from other countries were put through the full grinder. In some of the ''charter'' countries only a high school certificate was required to become an accountant, but for other countries, including those that closely emulated the United States' educational system, the candidates, some of whom had already worked professionally as accountants for the then-''Big Eight'' accounting firms in their countries, were required to take the licensing examination and meet other requirements waived for the charter country applicants. This practice was rooted out and the blatant discrimination rectified after intervention by the Department and litigation by some candidates, joined by the Department. Scores of those so discriminated against were admitted by the court's decision to full licensed stature. Despite the alarmist warnings of the professional groups, the State continued to prosper.

The public members also discovered another mechanism used by the Dental Board to handicap out-of-state licensure applicants: the ''gold foil technique.'' This was an outdated technique for making an imprint of a drilled tooth with gold foil as the initial step in the filling-design process. It was still taught by the California dental schools and was a required proficiency on the licensure examination as an exclusionary screening device, long after the technique had been retired in the

rest of the states. There actually existed at the time in California a club dedicated to practicing the gold foil technique as an art form. It was also a technique for discouraging out-of-state applicants, in the interest of protecting the practices of California dentists from competition.

Numerous other profession-cozy and –protecting practices were uncovered by the public members, working with the Internal Auditor and management of the Department, in other boards and bureaus, relating to, *inter alii*, contractors, auto repair shops, structural pest operators, funeral home operators, boxing regulation, and so forth. (Some of their early struggles were even amusing: on one board all of the new public members were women, but all of the professional members were men, who would caucus in the men's room and conduct board discussions and business they didn't want the public members to be part of.)

Such were the early days of California's pioneering ''public member'' construct to safeguard the licensure process of its professional licensing Boards from the ''domination'' by the professions and to ensure that actions taken by the Boards were more pristine ''state actions.''

B. Certain Administrative Mechanisms

California has established a Department of Consumer Affairs within its Business, Consumer Services and Housing Agency, in part specifically to oversee the boards and bureaus. The Department is headed by a Director, who is ''appointed by the Governor and holds office at the Governor's pleasure'' (B&P Code § 151), and thus clearly is subject to ''political accountability,'' one of the earmarks of state action as distinguished from ''a mere façade of state involvement,'' per *North Carolina Dental*.

The Director of Consumer Affairs ''may investigate the work of the several boards in his department'' (§ 153) and not only may employ investigators, inspectors and the like to ''investigate and prosecute all violations of any law, the enforcement of which is charged to the department or to any board, agency or commission in the department'' (§ 155) but also oversees a Division of Investigation which in turn includes a Health Quality Investigation Unit whose charge is ''to investigate violations of law or regulation'' within the health care boards under the Director's jurisdiction (§ 159.5). Thus, the forms and structures for the independent oversight of the member-controlled boards are clearly in place. But obviously, the mere existence of an oversight structure will not satisfy the *Midcal* requirement of active state supervision by non-participating elements.

Two other elements of the California government structure go further in that direction, however. Section 313.1 of the B &P Code establishes an elaborate system for review of any regulations proposed by the boards under the Department's jurisdiction. This section provides:

> (a) Notwithstanding any other provision of the law to the contrary, no rule or regulation, except those relating to examinations and qualifications for licensure, and no fee change proposed or promulgated by any of the boards, commissions, or committees, within the department shall take effect pending compliance with this section.
>
> (b) The director shall be formally notified of and shall be provided a full opportunity to review . . . all of the following [among others]:
>
> (1) All notices of proposed action, any modifications and supplements thereto, and the text of proposed regulations. . . .
>
> (3) Final rulemaking records.''

The Director's review ''shall be a precondition to the filing of any rule or regulation with the Office of Administrative Law,'' about whose role more in a moment, which is without jurisdiction to review ''any rule subject to this section'' until the Director has completed his or her review and ''has not disapproved it'' (§ 313.1(c)(3)). And a board can override the Director's disapproval of any rule or regulation only by the board's unanimous vote (§ 313.1(e)(3)), which of course takes the board's action out of the hands of the ''market participants'' since all boards have at least *some* public members, who are thus in a veto position.

The role of the Office of Administrative Law is also meaningful. While the OAL has no power over the substantive content of any California regulations, it has been tasked by the Legislature with ''the power and duty to review regulations to ensure that they are written in a comprehensible manner, are authorized by statute, and are consistent with other law'' (Gov't Code § 13400(e)); and state agencies are forbidden from ''issu[ing], utiliz[ing], [or] enforc[ing] . . . any guideline, criterion, bulletin, manual, instruction, order, standard of general application, or other rule . . . unless'' it has gone through the OAL filing and review process (§ 11340.5(a)). Thus, while the OAL has no substantive powers of review, its review process is another necessary step before any board can issue even ''guidelines'' or ''criteria'' that might have anticompetitive content which the State had not separately vetted; and it, too, is in a position to call attention to any proposed board action that may appear to go beyond what, per the first *Midcal* standard, the State of California itself had ''clearly articulated and affirmatively expressed as state policy.'' The OAL's review is thus added to the Director's review as an additional element of the State's ''active supervision.''

Following the passage of the law establishing the OAL, the Department of Consumer Affairs, collaborating with the Boards and Bureaus, conducted a zero-based review of all regulations that had been promulgated over the years, with salutary effect. By this time the public members were at full statutory strength and the composition and culture of the professional members had changed considerably with replacement appointments, by the public processes, not courtesy of professional association election. Ironically, the OAL balked at adopting internal procedural regulations for itself, which prompted the publication, in the maiden edition of a new regulatory law reporter that survives to this day, founded by certain erstwhile public members, of an article entitled, ''*Quis Custodiet Ipsos Custodes*?''

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