The Commission Strikes Back: The FTC Task Force Report on the State Action Doctrine

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Under principles of federalism and state sovereignty, courts have long held that local governments and certain private actors are exempt from the antitrust laws when the state itself has made a policy decision to displace competition and authorize conduct that would otherwise violate the antitrust laws. This "state action" doctrine had its genesis in the 1943 Supreme Court decision, Parker v. Brown, 317 U.S. 141 (1943). It has been applied in recent years to shield from the antitrust laws conduct such as exclusive contracts for local services such as cable television or airport taxi services, denials of zoning permits, hospital acquisitions of competitors, and to uphold rules of a state accountancy board rule barring CPAs from selling securities.

One of the current enforcement priorities of the FTC is to examine various antitrust immunities and exemptions, including the state action doctrine. The purpose is to determine whether such exemptions are being applied by courts in a manner consistent with competition policy generally. In September of 2003, the FTC's Task Force on State Action issued its Report ("Report") and concluded that in many instances the courts have applied the doctrine too broadly. The Report makes a series of specific recommendations as to how the state action doctrine should be properly applied, and the steps the FTC will take, such as filing amicus briefs, and legislate intervention, to return the doctrine to its proper scope.

While the Report comes with the usual admonition that it represents only the views of the Task Force itself (all FTC staffers), the Commission did authorize its issuance by a 5-0 vote. There is little doubt that one can expect the Commission to pursue actions consistent with the Task Force recommendations, and in some cases it already has. see, eg, Indiana Movers, FTC Docket No. C-4077. The focus of the Report, however, is on what the authors think the law should be, not what it is, as some courts have already rejected positions taken by in the Report.

By way of background, while the state itself (i.e., legislature, Supreme Court, etc.) is protected by the state action doctrine, local government entities are not unless they act pursuant to a state policy which "clearly articulates" a policy to displace competition. California Retail Liquor Dealers Association v. Midcal Aluminum, Inc., 445 U.S. 97 (1980). In addition, for private actors, the state must also "actively supervise" their conduct. Town of Hallie v. City of Eau Claire, 471 U.S. 34 (1985) (active supervision required for private parties but not local government entities). One recommendation of the Report is that various "hybrid" government entities, such as hospital boards or state accountancy boards, should be treated as private parties subject to the active supervision requirement.

Many courts have held that such hybrid entities are to be treated government entities not subject to the active supervision requirement. See, e.g., Earle v. State Board of Certified Public Accountants, 139 F. 3d. 1033, 1042 (5th Cir. 1998). The Report concedes this is appropriate in some cases, but notes that the examination of the

public/private distinction by courts is "not as rigorous as it might be." The Report recommends that there be a more rigorous analysis of structure, membership, decision-making apparatus and openness to the public of such quasi-government entities before concluding no active supervision is required. Where the decision-making personnel of the company is composed largely of private parties who may compete with each other, such as lawyers and accountants, the Report suggests that the entity be treated as a private party despite its public status.

A related recommendation in the Report is that, where local government entity itself is a market participant -- engages in commercial activities like those offered by private entities -- the court should impose an active supervision requirement even though Town of Hallie specifically exempted public entities from such a requirement. Most courts have rejected the market participant exception, but the issue usually arises in the context of whether there is any such exception to the state action doctrine at all, not whether the active supervision requirement should be imposed. See Antitrust Law Development (5th Ed.), p. 1222. Those courts rejecting the market participant exception do so on the basis that most local government "proprietary" functions also have a public purpose and to create a market participant exception would largely eliminate the state action immunity for local governments entirely. In Town of Hallie itself, for example, the municipality was engaged in the sewage treatment business and would itself have been a market participant.

That gets us to the active supervision itself. The Report notes that the courts have provided little guidance in this area. In its 1992 Ticor decision, dealing with whether the filing of collectively determined insurance rates were immune from price fixing claims under the state action doctrine, the Supreme Court held there was no immunity for private parties from such price fixing claims due to the failure to meet the active supervision requirement. FTC v. Ticor Title Insurance Co., 504 U.S. 621 (1992). While noting that state regulators must play a "substantial role" for active supervision to be present, the Ticor court provided little specific guidance as to what is required for active supervision, and suggested that it may vary based upon the gravity of the offense describing the alleged price fixing there as "pernicious" conduct that is per se illegal. Lower courts have not filled this void.

The Report's proposal to fill this vacuum, however, may be an example of where the cure may be worse than the disease. It proposes a rather wooden three-part test already adopted in the Indiana Movers case – there must be an adequate factual record, a decision on the merits, and a specific assessment of how the private action comports with substantive standards established by the legislature. When viewed in the context of daily decisions by water districts and airport authorities, however, this is an onerous set of standards that may not be practical or workable. Moreover, the Report appears to apply the same standard to rule of reason conduct as to conduct which is per se illegal, although there are some oblique references to a "tiered approach" in some cases. A more relaxed standard, implicitly suggested by Ticor, should suffice for rule of reason conduct such as exclusive contracts or vertical restraints.

The Report is likewise critical of existing law with respect to the clear articulation requirement. The Report emphasizes that, as originally developed in Parker and its progeny, clear articulation required that the state intended to displace competition in the area in which the anticompetitive conduct by local government occurs, usually in the form of a statute passed by the legislature. In Town of Hallie, however, the court held that the anticompetitive conduct at issue there -- a refusal to supply sewage treatment services to unannexed areas -- was protected by the state action doctrine even though not expressly authorized by the legislature. Stating that the statute was not "neutral" as to competition, the court held that the anticompetitive conduct was the

"foreseeable result" of the statute since it did empower the city to refuse to serve unannexed areas. The "foreseeable" standard was reiterated by the Supreme Court in City of Columbia v. Omni Outdoor Advertising, 499 U.S. 365 (1991) where it held that it was foreseeable that authority given a city to regulate land use and buildings would result in zoning restrictions on billboard advertising.

In recent years, a number of courts have used this "foreseeability" test to conclude that a general grant of authority to a local government entity to act in a specific area, such as providing taxi service at airports or to own and operate hospitals, is sufficient to meet the clear articulation standard. The Report criticizes these decisions, and describes them as "conflating" a general authorization of conduct with a specific intent to displace competition. It recommends a return to the principle that the authorizing statute must also evince an intent to displace competition with respect to the particular conduct at issue, a recommendation does have some judicial support. See generally Surgical Care Center of Hammond v. Hospital Service District No. 1, 171 F.3d 231 (5th Cir. 1999).

In dealing with the clear articulation issue, or any other issue for that matter, the Report does not address the Local Government Antitrust Act. 15 USC § 34-36. The LGAA was passed in response to the City of Boulder decision which denied immunity on the basis that a general authorization statute did not articulate a state policy to displace competition with respect to the award of cable television franchises. Community Communications Co. v. City of Boulder, 455 U.S. 40 (1982). Although the LGAA bars only damages claims against local governments, not those for injunctive relief, it appears to apply even if there is no legislation which clearly articulates a policy to displace competition.

Another section of the Report is its recommendation that courts consider "spillover" effects on citizens of other states in determining whether the alleged conduct is protected by the state action doctrine. Citing the original Parker decision as an example, the Report notes that in the affected market there (production and sale of raisins), the benefits of the higher prices were concentrated in the state enacting the law displacing competition but the costs spilled overwhelmingly into other states. When such "spillover" effects are present, argues the Report, courts should consider this in their state action analysis, presumably to limit its application.

The Report concedes that this spillover effect has been largely ignored by the courts, and is founded mainly on various scholarly articles. Given the fact that virtually every industry and market today is an interstate one, this spillover concept is really an attack on the principles of federalism and state sovereignty which form the basis for the state action doctrine in the first place. One also wonders how a court would formulate a spillover rule (e. g., how much must go out of state before you lose state action protection?) and the evidentiary hearings that would be necessary to determine whether such a rule should apply in specific cases.

For those lawyers dealing with state action immunity issues, the Report provides guidance concerning existing law and the enforcement intentions of the Commission. Given the current status of the law and the existence of substantial protectionist sentiment where "local control" is an issue, as exemplified by the LGAA, the Commission has an uphill battle.

Practice Areas

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