How the U.S. Supreme Court Empowered Political Accountability and Economic Growth in Arkansas

By Dan Greenberg *9/2/15*

In February of 2015, the Supreme Court of the United States issued a decision in the matter of *North Carolina State Board of Dental Examiners v. Federal Trade Commission*,[1] which will have profound effects on the operations of state boards and commissions in the years ahead. **The end result of this decision is that, if boards and commissions exercise rulemaking or quasi-legislative authority, in some circumstances they are no longer immune from liability under federal antitrust law.** This means that if such boards and commissions continue to issue or enforce anti-competitive regulations, those actions could generate notable liability exposure both for individuals and government bodies. These damages could possibly include treble damages or even criminal penalties. **If the state of Arkansas wishes to avoid such liability, its lawmakers should make substantial structural changes in our state boards and commissions: these changes could also trigger substantial job creation and economic growth.**

Background

This case, which for the sake of brevity I'll refer to as *Dental Examiners,* involved a dental regulatory board – composed largely of practicing dentists – that successfully locked providers out of the market who were offering teeth-whitening services. The dental board contended that the teeth-whitening providers were illegally practicing dentistry. Some might believe that non-dentist teeth whiteners were endangering the public, and some might believe that the dental board was protecting a lucrative dental service cartel. It seems fair to say that the Supreme Court was more sympathetic to the latter view.

How This Case Affects Arkansas

Dental Examiners has a much larger scope than just the North Carolina Board of Dental Examiners: the decision applies to state regulatory bodies generally. **The case suggests that many boards and commissions will need to be restructured or firewalled in order to escape antitrust liability.**

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It is reasonable to read *Dental Examiners* as creating new antitrust liability for boards and commissions, but only if those boards and commissions are structured in such a way that special interests might come to control them. This is a phenomenon known to economists and political scientists as "regulatory capture."[2] The *Dental Examiners* case identifies the structure of a regulatory board in North Carolina as fitting into this category. In this case, North Carolina law required that six of the eight state dental board members had to be licensed dentists engaged in the active practice of dentistry.

The core of the Supreme Court's concern is based on "the risk that active market participants [e.g., professionals placed on boards that regulate their own business] will pursue private interests in restraining trade" – or, to put it another way, "the structural risk of market participants' confusing their own interests with the State's policy goals."[3]

It is likely that Arkansas could avoid *Dental Examiners* liability in two ways. It could either **restructure** boards and commissions so that their members are not self-interested. For instance, states could remove some or all practicing professionals from service on their own profession's boards. Or the state could **firewall** those boards and commissions in a way that adds an element of sovereign accountability. This could happen by requiring legislative or gubernatorial review of regulations. Because of the opinion's emphasis on the structural aspect of preventing special interests from capturing regulatory bodies, the second alternative ("firewalling") is probably superior.

***Dental Examiners* also suggests that state legislatures have powers to create anti-competitive policies in ways that boards and commissions do not.** The anti-competitive conduct of a state which is acting in its sovereign capacity is immune from interference by antitrust law. But if a state delegates its sovereign regulatory power to a board or commission, that sovereign immunity could vanish unless two conditions are met:

- *First,* the measure passed by the board/commission must be "clearly articulated and affirmatively expressed as state policy,"[4] or at least must be consistent with it.
- *Second,* the policy must be "actively supervised by the State."[5] To put it another way, from now on the state must take responsibility for a system of anticompetitive regulations by endorsement through its court or legislature.

Policymakers who want state government to encourage competition should therefore view *Dental Examiners* not simply as a nuisance that will create more difficulties, but as an opportunity. For instance, the state legislature could expressly lay down the policy by statute (or by means of state Supreme Court interpretation), and by requiring state officials to "exercise power to review particular anticompetitive acts of private parties and disapprove those that fail to accord with state policy."[6]

***Dental Examiners* specifies an impermissible structure, but it is less forthcoming about what constitutes permissible structures of regulatory boards and commissions. This means policymakers have some degree of freedom to respond to the opinion with a reform plan; nonetheless, that reform needs to be substantive, not simply cosmetic.** The best way to respond to *Dental Examiners* is only partially determined by the law. Any legislative response will be, in part, a policy decision. However, superficial reforms that do not significantly affect anti-competitive/quasi-monopolistic regulatory action by boards and commissions will leave Arkansas open to significant legal uncertainty. The way to avoid such legal uncertainty is to enact measures that will restrict the kind of anti-competitive conduct that originally created the grounds for *Dental Examiners.* It is likely that if Arkansas only does the bare minimum to comply with *Dental Examiners'* "active supervision" requirement, it will run a significant risk of continued liability.

If, for instance, the Federal Trade Commission targets Arkansas for anti-competitive action under this decision, the state is unlikely to prevail if it argues that the state merely employs someone who monitors regulations. **Instead**, **Arkansas would be better served by enacting some kind of structural safeguard against anti-competitive regulations.**

Recommendations for Action

If policymakers want a more competitive and productive economic system, then *Dental Examiners* provides an excellent opportunity for change. Arkansas lawmakers could respond to *Dental Examiners* in the following way:

Create an Office of Regulatory Affairs ("ORA"), with the mission of reviewing board and commission regulations so as to protect Arkansas taxpayers from antitrust liability. This office could presumably be composed entirely of one person. This office, or officer, could report directly to the Governor. In fact, establishing this office could be as simple as adding one person to the Governor's

staff. While the office could be situated in many possible places in state government, the requirement of active supervision suggests that the ORA should be inside the executive branch of state government. An alternative possibility would be to house the ORA in the Attorney General's office.

Require the ORA to encourage competition inside each industry through its supervision. Unless this step is taken, the ORA will be reviewing regulation without a clear idea of what it is looking for. Articulating a pro-competition ORA policy in state law would assure the exercise of public supervisory authority to prevent anti-competitive behavior. Furthermore, such legislation should list specific factors for the ORA to consider, such as the impact of regulations on consumer choice, product and service innovation, and job creation in the state. More generally, the ORA should be guided by the standards of active supervision that our nation's highest court has laid down.[7] Ideally, such legislation would provide a scale of most to least restrictive regulation, so as to encourage lawmakers and regulators to establish only the least burdensome regulation necessary to protect consumers from actual (not hypothetical) harm.

Require the ORA to review rules created by boards and commissions on a regular basis, and to recommend changes to the legislature which would repeal or reduce inappropriate regulatory burdens. Lawmakers should consider allowing the ORA to take into account the extent to which other states regulate the industry in question, the extent to which alternatives to licensure (such as certification) would serve the same safety or consumer protection interest, and the extent to which the predicted harms that justify regulation are real. This approach falls in line with a recent White House Council of Economic Advisors report which examines licensure. It recommends certain best practices for states. One such recommendation is that "in such cases where public health and safety concerns are mild, consider using alternative systems that are less restrictive than licensing, such as voluntary State certification … or registration…" It also recommends that states "make sure that the substantive requirements of licensing (e.g., education and experience requirements) are closely tied to public health and safety concerns."[8]

In line with these recommendations, legislators may wish to require the ORA to determine whether certain conduct is outside the scope of regulatory bodies, or to produce a plan for the legislature to the effect that some boards and commissions be consolidated or eliminated.

Give the ORA power to disapprove regulations from boards and commissions that might reduce competition and/or create antitrust liability. When

boards and commissions issue regulations, they should go through some kind of review process that requires affirmative approval by the ORA. Similarly, ORA should in some circumstances have similar disapproval power over already-existing regulations from boards and commissions.[9]

Although this disapproval power may be controversial to some observers, something like it appears mandated by a paragraph near the end of the *Dental Examiners'* decision, which lays out some "requirements of active supervision":

> 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, see Patrick, 486 U. S., at 102–103; the supervisor must have the power to veto or modify particular decisions to ensure they accord with state policy, see ibid.; and the "mere potential for state supervision is not an adequate substitute for a decision by the State," Ticor, supra, at 638. 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.[10]

While *Dental Examiners'* scope is limited to boards and commissions, policymakers are not. Legislators who want to encourage regulatory reform more generally should consider whether regulations that are issued by executive departments in state government (for instance, the Department of Health) should come under ORA review.

Arkansas already has an existing gubernatorial review process of board/commission rulemaking, but its scope and force is unclear. Legislators should consider the above recommendations for replacing or modifying that existing process. It is worth emphasizing that just having a regulatory review process does not do much to shield against *Dental Examiners* liability. Instead, Arkansas needs a regulatory review process that expressly highlights and scrutinizes anti-competitive practices and provides a practical avenue to eliminate them.

Colorado's Example

Colorado established a one-person office in 2003 called the Office of Regulatory Reform and Economic Competitiveness. It has many praiseworthy elements that can inform Arkansas policymakers. For instance, in Colorado all regulatory agencies must submit proposed new rules or amendments to an online database that is open to the public. This online system allows citizens to receive "Regulatory Alert" emails whenever new rules or amendments are considered. Interested parties are able to send comments to the office on those proposals by email. The office can also require that a state agency submit a cost-benefit analysis that described the impact of a proposed new rule or amendment. Importantly, Colorado allows this regulatory review office to disapprove regulations.

Obama Administration Endorses Licensure Reform

Policymakers across the political spectrum are endorsing licensure reform. Perhaps the most prominent example comes from the Obama Administration. As mentioned above, the White House Council of Economic Advisors (CEA) recently issued a report that noted the sharp increase in occupational licensing over the past few decades.

This report pointed out the problems with this uptick in licensing:

> ...the current licensing regime in the United States also creates substantial costs, and often the requirements for obtaining a license are not in sync with the skills needed for the job. There is evidence that licensing requirements raise the price of goods and services, restrict employment opportunities, and make it more difficult for workers to take their skills across State lines.[11]

It goes on to discuss how lawmakers who enact these licensing rules do not take into consideration the full range of effects, or look at alternatives such as certification that may impose a far lighter burden on those seeking to work. The CEA then calls on lawmakers to create a regulatory system that "protects public health and welfare while promoting economic growth, innovation, competition, and job creation."[12] Establishing an ORA in Arkansas would advance this goal.

Deregulation Creates Jobs and Economic Growth

In testimony earlier this year to the House State Agencies Committee, Dr. David Mitchell, a professor of economics at the University of Central Arkansas, explained the burden that excessive regulation places on Arkansas's economy. According to Mitchell, Arkansas policymakers have burdened our economy far more than surrounding states through occupational regulation, making our state one of the five worst (out of 50) when we compare the burdens of occupational licensure across the country. We place the second-highest burdens of experience and education in the country on licensed occupations; for instance, on average to obtain a professional license one needs more than twice as much education and experience in Arkansas as in Texas. Mitchell estimated that if Arkansas had reduced the number of low-wage jobs requiring a license to equal that of Missouri, it would cut Arkansas's black poverty rate by 15.6% (from 34.1% of the population to 28.8%), bringing over 22,000 black Arkansans out of poverty; if Arkansas had reduced education and experience licensure requirements for low-wage jobs to those of Mississippi's, (from 689 days to 155 days), prices would have fallen in Arkansas by 5%, which of course would significantly raise the purchasing power of the poor; if Arkansas had reduced the number of low-wage jobs that require a license to correspond with the requirements of Missouri (from 52 occupations to 31 occupations), then Arkansas could have created more than 8,000 new jobs. These figures suggest that, compared to surrounding states, the Arkansas economy is relatively overregulated in a manner that blocks job creation and economic growth – and that creating a government institution that reduces the barriers that government has previously created should lead to a future of growth and prosperity for Arkansas.

Conclusion

Although *Dental Examiners* arguably creates a new set of burdens for state government regulators, it also presents an opportunity for state lawmakers. A reasonable structural response to this decision might provide an avenue for a significant increase in free-market competition in the state. That, in turn, would lead to increased consumer welfare and economic growth. Arkansas should take advantage of this opportunity to pursue regulatory reform, rather than becoming a laggard state that is targeted by the Federal Trade Commission in a future lawsuit.

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[1] *North Carolina State Bd. of Dental Examiners v. FTC*, 574 U.S. ____ (2015).
[2] See generally, e.g., Daniel Carpenter and David Moss (eds.), *Preventing Regulatory Capture: Special Interest Influence and How to Limit It* (2013).
[3] *Dental Examiners.*
[4] Ibid.
[5] Ibid.
[6] Ibid.
[7] See, e.g., *FTC v. Ticor Title Ins. Co.*, 504 U.S. 621, 634–635 (1992) (stating the purpose of active supervision is to determine "whether the State has played a substantial role in determining the specifics of the . . . policy" and that the policy was "established as a product of deliberate state intervention, not simply by agreement among private parties"). See also *Hallie v. Eau Claire*, 471 U.S. 34, 47 (1985) ("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 governmental interests of the state.") and *Goldfarb v. Va. State Bar*, 421 U.S. 773, 791–792 (1975) (denying immunity to a state agency that "joined in what is essentially a private anticompetitive activity" for "the benefit of its members"). See also *Patrick v. Burget*, 486 U.S. 94, 101 (1988) ("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."). See also *Dental Examiners* (holding active supervision "require[s] the State to review and approve interstitial policies made by the entity claiming immunity" to provide "realistic assurance that a private party's anticompetitive conduct promotes state policy . . . .") (quoting *Patrick*, 486 U.S. at 101).
[8] "Occupational Licensing: A Framework for Policymakers," White House Council of Economic Advisors, July 28, 2015.
https://www.scribd.com/doc/272814969/CEA-report-on-occupational-licensing?secret_password=piRg7qvS7TeQVHAmSiNX
[9] To state the obvious: there are many instances of regulation that are important and necessary, and under this paper's proposed recommendations, it is quite simple for state government to protect regulation from anything like an ORA disapproval if that is the desired result. All that would be necessary in such a situation would be to write the regulation into state law.
[10] *Dental Examiners.*
[11] "Occupational Licensing," p. 3.
[12] Id, p. 5.