No. 20-55735

IN THE
United States Court of Appeals for the Ninth Circuit

JEFFREY SULITZER, et al.,
Plaintiffs-Appellants,

v.

JOSEPH TIPPINS, et al.,
Defendants-Appellees.

On Appeal from the
United States District Court for the Central District of California
No. 2:19-cv-08902 (Honorable George H. Wu)

BRIEF OF THE UNITED STATES OF AMERICA AS AMICUS CURIAE IN SUPPORT OF NEITHER PARTY

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STATEMENT OF INTEREST

The United States Department of Justice enforces the federal antitrust laws and has a strong interest in their correct application. We are concerned that the district court adopted an erroneous legal framework when analyzing whether plaintiffs adequately stated a claim under Section 1 of the Sherman Act, 15 U.S.C. § 1.

The district court appears to have held that conduct falling within the authority of a state regulatory board cannot constitute unreasonable concerted action under Section 1 as a matter of law. Such a holding is incorrect. Agreements by board members can constitute concerted action under Section 1 even though they are within the board members' regulatory authority, and in some circumstances, such agreements can be anticompetitive and unreasonable. While these agreements may be exempt from antitrust liability under the state-action doctrine of *Parker v. Brown*, 317 U.S. 341 (1943), that is a disfavored defense with stringent requirements that defendants must prove.

The government has previously filed amicus briefs emphasizing the importance of separately analyzing the existence of concerted action

under Section 1 and the reasonableness of the concerted action. *See, e.g.*, *Visa, Inc. v. Osborn & Visa, Inc. v. Stomous*, Nos. 15-961, 15-962 (S. Ct. Oct. 2016) (U.S. Visa Am. Br.), *at* https://www.justice.gov/atr/case-document/file/905436/download; *Robertson v. Sea Pines Real Estate*, Nos. 11-1538-41 (4th Cir. Aug. 29, 2011), *at* https://www.justice.gov/atr/case-document/brief-united-states-amicus-curiae-support-plaintiffs-appellees. The government has also previously filed amicus briefs emphasizing the limited nature of the state-action defense. *See, e.g., Ellis v. Salt River Project*, Nos. 20-15301, 20-15476 (9th Cir. July 8, 2020), *at* https://www.justice.gov/atr/case-document/file/1292891/download; *D. Blaine Leeds & SmileDirectClub, LLC v. Jackson, et al.*, No. 19-11502 (11th Cir. Sept. 25, 2019), *at* https://www.justice.gov/atr/case-document/file/1205101/download; *Chamber of Commerce v. City of Seattle*, No. 17-35640 (9th Cir. Nov. 3. 2017), *at* https://www.justice.gov/atr/case-document/file/1009051/download; *Teladoc, Inc. v. Tex. Med. Bd.*, No. 16-50017 (5th Cir. Sept. 9, 2016), *at* https://www.justice.gov/atr/file/890846/download.

If the district court's apparent misreading of the antitrust laws is not corrected by this Court, it could have far-reaching anticompetitive consequences on American businesses and consumers. "[A]cross the United States, licensing boards are largely dominated by active members of their respective industries." *FTC Staff Guidance on Active Supervision of State Regulatory Boards Controlled by Market Participants* (Oct. 13, 2015) (FTC State Regulatory Board Guidance) at 1 (internal quotation marks omitted), *at* https://www.ftc.gov/system/files/attachments/competition-policy-guidance/active_supervision_of_state_boards.pdf. The Supreme Court has emphasized that such "active market participants cannot be allowed to regulate their own markets free from antitrust accountability" due to the significant risk that they might engage in "self-dealing" to promote their private interests. *N.C. State Bd. of Dental Exam'rs v. FTC*, 574 U.S. 494, 505, 507, 510 (2015) (*NC Dental*).

We file this brief under Federal Rule of Appellate Procedure 29(a).

STATEMENT OF ISSUES PRESENTED

1. Whether agreements by board members of the Dental Board of California can constitute concerted action under Section 1 of the

Sherman Act even though they fall within the board members' regulatory authority?

2. Whether such agreements can be anticompetitive, and thus unreasonable under Section 1?

3. Whether limiting antitrust liability for restraints that are "consistent with the Dental Board's regulatory purpose" would *de facto* create a novel exemption for state regulatory boards that is substantively and procedurally inconsistent with the rigorous limitations on the state-action defense set forth in *NC Dental*?

STATEMENT

The Dental Board of California (Dental Board) is a state agency that regulates the practice of dentistry in California; the majority of its members are practicing dentists. *See* First Amended Complaint (FAC) (ER112), at ¶ 59 (ER129).[1] SmileDirect Club LLC (SmileDirect) and certain affiliated California dentists (collectively, Plaintiffs) offer clear aligners via tele-dentistry that compete with traditional orthodontic services in California. FAC at ¶¶ 4-5 (ER115-16). Plaintiffs allege that, following a complaint by an orthodontic trade association, the members

[1] The facts herein come from the FAC.

of the Dental Board, its executive director, and an investigator unlawfully agreed to target Plaintiffs with an intrusive investigation that suppressed the competitive threat posed by Plaintiffs' clear aligners in violation of Section 1 of the Sherman Act. *Id.* at ¶¶ 6, 105 (ER116, ER145). This case involves the sufficiency of those allegations to state a claim under Section 1.

1. Section 1 of the Sherman Act, 15 U.S.C. § 1, prohibits contracts, combinations, or conspiracies (i.e., concerted actions) that unreasonably restrain trade (i.e., are anticompetitive). Courts assess separately whether (i) concerted action exists and (ii) the concerted action is anticompetitive. *See Am. Needle, Inc. v. NFL*, 560 U.S. 183, 186 (2010).

In *Parker v. Brown*, 317 U.S. 341, 350-52 (1943), the Supreme Court recognized a limited exemption from antitrust liability for "state action" to protect the deliberate policy choices of sovereign states to displace competition with regulation. This exemption is "disfavored," however, given its tension with "the fundamental national values of free enterprise and economic competition that are embodied in the federal antitrust laws." *FTC v. Phoebe Putney Health Sys., Inc.*, 568 U.S. 216, 225 (2013). Courts therefore interpret the state-action defense

"narrowly, as a broad interpretation of the doctrine may inadvertently extend immunity to anticompetitive activity which the states did not intend to sanction." *Shames v. Cal. Travel & Tourism Comm'n*, 626 F.3d 1079, 1084 (9th Cir. 2010) (quotation marks omitted).

Actions of a state regulatory board dominated by marketplace participants qualify for the state-action exemption only if two stringent criteria are met: the board is (1) acting pursuant to a clearly articulated state policy and (2) that policy is actively supervised by the state. *NC Dental*, 574 U.S. at 504. Defendants bear the burden for establishing state action. *Id.*

2. Clear aligners are an allegedly superior teeth-straightening alternative to traditional wire braces. SmileDirect created an innovative "tele-dentistry" system for providing clear aligners. Customers begin by getting a digital scan of their mouths at a SmileDirect office or using an at-home mouth impression kit, which are each developed into detailed images by a lab. SmileDirect then connects an affiliated dentist licensed in California with the customer over its online portal. This process allows SmileDirect to send clear aligners to customers without an in-person dental examination,

resulting in significant cost savings and greater customer convenience and access. FAC ¶¶ 2-4, 34-50 (ER115-16, ER122-27).

Plaintiffs allege that, following a complaint by the American Association of Orthodontists, "a powerful and well-funded trade association representing traditional orthodontists," the Dental Board members "engaged in, directed, authorized, acquiesced in and ratified a campaign of harassment and intimidation against" Plaintiffs as part of a multi-year Board investigation. *Id.* at ¶¶ 63-64, 100 (ER130-31, ER142). "In response to this competitive threat" posed by Plaintiffs' offerings, Defendants agreed to "an aggressive, anti-competitive campaign" against Plaintiffs, including "coordinated statewide raids; false statements; misconduct in front of consumers; and a retaliatory accusation filed in response to the lawsuit." *Id.* at ¶ 6 (ER116). The purpose of the conspiracy was "to protect the economic interests of the traditional orthodontia market—including the practices of many of the Board Members—rather than the public's health, welfare or safety." *Id.*

As support for their allegations, Plaintiffs point to a series of simultaneous, unannounced investigative raids on multiple SmileDirect facilities throughout California. During these, Dental Board

investigators "frightened and intimidated" store employees with their "aggressive behavior [and made] unreasonable demands for information and documents," and likewise "harassed and intimidated" customers allegedly for the purpose of creating "disruption[] and public spectacle." *Id.* at ¶¶ 73, 76 (ER133-34). On another occasion, an investigator (having received an email from the Executive Director) entered a SmileDirect service center, and displayed an "investigator badge" in a manner that made customers think he was with the police, yelled at employees, and leveled broad accusations of misconduct in front of customers. *Id.* at ¶ 81 (ER135-36).

Plaintiffs allege that it was not reasonable to believe that this misconduct was due to independent action by the investigators. The Dental Board has "full power over investigators" under California law, and the investigation and harassment spanned multiple years. *Id.* at ¶¶ 67-82, 100 (ER131-36, 142) (quotation marks omitted). Further, Plaintiffs sent letters to the board members complaining about the investigators, and requested a meeting, but the board members refused and "instead retained litigation counsel." *Id.* at ¶¶ 84, 87, 101 (ER137-38, ER142-43). Plaintiffs allege that the extensive and coordinated

nature of the statewide raids makes it reasonable to infer that the investigators informed the executive director and board members "before" the raids happened. *Id.* at ¶ 75 (ER134). These Defendants "at very least did nothing to stop" the raids. *Id.* Even if Defendants did not have prior knowledge, they "ratified" this conduct by allowing it to continue. *Id.* at ¶ 63 (ER130).

Defendants moved to dismiss the Section 1 claim under the state-action doctrine and for failure to state a claim. The district court rejected Defendants' argument that the state-action doctrine applied, reasoning that the Dental Board was controlled by active market participants and that Defendants failed to establish that the State actively supervised the challenged conduct. ER424-30. The court nonetheless held that Plaintiffs failed to state a Section 1 claim. ER432. The court held that Plaintiffs "may have pled enough to suggest an agreement by way of a theory of the Board's ratification" of the investigation, but this was insufficient because it was "simply an agreement to undertake their delegated authority as members of the Board, not an agreement intending to restrict or restrain competition." *Id*.

Plaintiffs amended their complaint to add allegations that various board members viewed SmileDirect and its affiliated dentists as a competitive threat. FAC ¶¶ 61-62, 102-103 (ER130, ER143-45). Defendants again moved to dismiss. Plaintiffs opposed, noting in part that there is no requirement that defendants must specifically agree with the intention of destroying competition. *See* ER60 (*citing Paladin Assoc., Inc. v. Mont. Power Co.*, 328 F.3d 1145, 1153-54 (9th Cir. 2003) ("[T]he district court reached this erroneous conclusion by improperly grafting an additional requirement—specific intent to destroy competition—onto the element of [plaintiff's] prima facie case requiring that the defendants acted in concert.")).

The district court again dismissed the complaint for failure to state a claim with a somewhat different rationale:

> [A]ny "agreement" [Plaintiffs] believe they have demonstrated—or can, with the ability to conduct discovery, demonstrate—is an agreement consistent with the Dental Board's regulatory purpose, not an agreement to—for instance—withhold x-rays from insurers, set fees, or prohibit competitive bidding, as were the situations in the Supreme Court decisions they cite. That certain defendants authorized the investigation into Plaintiffs, and others (or all of them) ratified it, by allowing it to continue, is to be expected of a regulatory body given the authority to investigate those regulated. *See, e.g.*, *In re Musical Instruments & Equip. Antitrust Litig.*, 798 F.3d 1186, 1193-94 (9th Cir. 2015) ("'Allegations of facts that could just as easily suggest rational, legal business behavior by the

> defendants as they could suggest an illegal conspiracy' are insufficient to plead a § 1 violation.") (quoting *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 557 (2007), and *Kendall v. Visa U.S.A., Inc.*, 518 F.3d 1042, 1049 (9th Cir. 2008)).

ER18. The court further noted that:

> What Plaintiffs otherwise have is motive (as to at least some of the defendants), *see* FAC ¶¶ 60-62, opportunity and what they believe are other "plus factors," *see id.* ¶¶ 102-03. *See id.* at 1195 ("[A]llegations of parallel conduct – though recast as common motive – [are] insufficient to plead a § 1 violation."). But, again, the Court believes that these factors would exist any time a state regulatory board that consists, at least in part, of market-participants, engages in an investigation of other market-participants. Unless every single time such an investigation commences the courts should expect a Sherman Act challenge, a plaintiff needs to do something more to push across the plausibility line a case for an agreement prohibited by federal antitrust laws. *See, e.g.*, *Name.Space, Inc. v. Internet Corp. for Assigned Names & Numbers*, 795 F.3d 1124, 1129-30 (9th Cir. 2015).

ER18-19.

ARGUMENT

The district court's ruling that Plaintiffs did not adequately allege an "agreement prohibited by federal antitrust laws" because "any 'agreement'" to implement the challenged conduct is "consistent with the Dental Board's regulatory purpose" and falls within the board members' "authority to investigate those regulated," ER18-19, is ambiguous. Among other possibilities, it could be read as holding either

that (1) there cannot be concerted action among Dental Board members when they act within their regulatory authority or (2) conduct within the Board's regulatory authority cannot be anticompetitive. Each of these propositions would be an incorrect application of antitrust law: Dental Board members can engage in concerted action under Section 1 even when their actions fall within the Board's regulatory authority, and in some circumstances that concerted action can be anticompetitive. An interpretation of the law that conditions a determination of concerted action or of an unreasonable trade restraint on a finding that the board acted beyond its authority could radically circumscribe the scope of Section 1.

While regulatory authority for the challenged action is relevant to whether it qualifies as "state action" under *Parker*, that is a "disfavored" defense with stringent requirements, for which the burden is on defendants. By requiring Plaintiffs to plead—and later prove—that the alleged conduct was beyond the Dental Board members' regulatory authority, the ruling below could be read to create a *de facto* exemption for state regulatory boards controlled by active market participants that is fundamentally inconsistent—both substantively

and procedurally—with *NC Dental*. This Court should make clear that such a novel exemption would be improper because it could result in the very situation the Supreme Court cautioned "cannot be allowed"—active market participants regulating their own industry "free from antitrust accountability." *NC Dental*, 574 U.S. at 505.

I. Anticompetitive Agreements Can Violate Section 1 Even Though They Fall Within Dental Board Members' Regulatory Authority

A. An agreement among members of the Dental Board can constitute concerted action even when their actions are within their regulatory authority

"The question whether an arrangement is a contract, combination, or conspiracy is different from and antecedent to the question whether it unreasonably restrains trade." *Am. Needle, Inc.*, 560 U.S. at 186. To constitute concerted action under Section 1 an arrangement must be (1) an agreement (2) between two or more entities capable of engaging in concerted action. *Id.* at 189-90. The concerted-action requirement plays an important gatekeeping role. "In § 1 Congress 'treated concerted behavior more strictly than unilateral behavior' . . . because unlike independent action, '[c]oncerted activity inherently is fraught with anticompetitive risk' insofar as it 'deprives the marketplace of

independent centers of decisionmaking that competition assumes and demands.'" *Id.* at 190 (quoting *Copperweld Corp. v. Indep. Tube Corp.*, 467 U.S. 752, 768-69 (1984)).

Applying these principles, the Supreme Court has repeatedly held concerted action exists when market participants regulate their industries. These decisions have commonly involved market participants regulating their industries through professional associations. *See, e.g.*, *FTC. v. Ind. Fed. of Dentists*, 476 U.S. 447, 459 (1986) ("[The Federation's] policy takes the form of a horizontal agreement among the participating dentists."); *Ariz. v. Maricopa Cnty. Med. Soc'y*, 457 U.S. 332, 347-51, 357 (1982) (doctors in an association setting price levels reached "a price fixing agreement"); *Nat'l Soc'y of Prof'l Eng'rs v. United States*, 435 U.S. 679, 692 (1978) (*Professional Engineers*) (ethical canon promulgated by a professional organization constituted "an agreement among competitors"). Likewise, in *California Dental Association v. FTC*, this Court found that the Association's challenged policies limiting member advertisements constituted an agreement under Section 1. 128 F.3d 720, 729 (9th Cir. 1997). While the Supreme Court remanded this Court's decision for

further analysis on the policies' competitive impact, it did not question the conclusion that the policies were concerted action. *See Cal. Dental Ass'n v. FTC*, 526 U.S. 756, 769-70 (1999); *see also id.* at 782 (Breyer, J. concurring in part and dissenting in part) (referring to the policies as an "agreement").

The Supreme Court has further made clear that the same principles apply when state regulatory boards controlled by market participants regulate their industries. As *NC Dental* explained, "[t]he similarities between agencies controlled by active market participants and private trade associations are not eliminated simply because the former are given a formal designation by the State, vested with a measure of government power, and required to follow some procedural rules." 574 U.S. at 511. In both situations, the competitive issues are created by "a group of active market participants [] decid[ing] who can participate in its market, and on what terms," and their agreements are subject to antitrust scrutiny under Section 1. *Id.*

Such concerted action often has come in the form of adopted rules or policies. *See* p. 14, *supra* (citing examples); Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* (Areeda & Hovenkamp) ¶ 1477 (4th

ed. Aug. 2019) (In *Professional Engineers*, the "court never asked whether the society as an entity had conspired with anyone," as it "seemed obvious to the parties that the rule was a contract, combination, or conspiracy among the members."). Concerted action is not limited to formal rules, however, but also includes other types of agreements by members or board members. For instance, in *NC Dental*, the Fourth Circuit held that board members engaged in concerted action when agreeing to send cease and desist letters to non-dentist competitors. *N.C. State Bd. of Dental Exam'rs v. FTC*, 717 F.3d 359, 372 (4th Cir. 2013), *aff'd on other grounds*, 574 US. 494 (2015); *cf. Robertson v. Sea Pines Real Estate Cos., Inc.*, 679 F.3d 278, 285-86 (4th Cir. 2012) (holding that concerted action existed even though "defendants passed the MLS by-laws in their capacity as MLS board members").

The district court acknowledged that its decision to dismiss Plaintiffs' Section 1 claim "may be seen as inconsistent, in certain respects, with the Fourth Circuit's decision in *North Carolina State Board of Dental Examiners v. F.T.C.*" The district court indicated, however, that this potential divergence was not troubling because

"Plaintiffs have not demonstrated that the Ninth Circuit" would follow the Fourth Circuit's decision. ER19. Nonetheless, the Fourth Circuit's reasoning in *NC Dental* is consistent with this Court's decision in *California Dental*. Thus, there is no reason to depart from it here, especially in light of the Supreme Court's acknowledgement that state regulatory boards controlled by active market participants pose the same sort of competitive concerns as other types of professional organizations. *See* p. 15, *supra*.

When dismissing the original complaint, the district court indicated that Plaintiffs adequately alleged an agreement by the Dental Board members "by way of a theory of the Board's ratification" of the investigation, ER432, but appeared to reverse course when dismissing the amended complaint. Citing *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 553 (2007), and post-*Twombly* precedent from this Court, the district court appeared to rule that there were insufficient allegations of concerted action because "any 'agreement' . . . is an agreement consistent with the Dental Board's regulatory purpose." ER18; pp. 10-11, *supra*. "That certain defendants authorized the investigation into Plaintiffs, and others (or all of them) ratified it, by allowing it to

continue, is to be expected of a regulatory body given the authority to investigate those regulated." *Id.*

To the extent the district court held that the board members did not reach an agreement under Section 1 because they acted consistently with their regulatory authority, this represents a misapplication of *Twombly*. *Twombly* does not suggest that there cannot be concerted action when the challenged conduct falls within board members' regulatory authority. Rather, *Twombly* holds that conclusory allegations of concerted action are inadequate and that the plaintiff must allege sufficient facts to render the existence of concerted action plausible. 550 U.S. at 556-57. Thus, for instance, "when allegations of parallel conduct are set out in order to make a § 1 claim, they must be placed in a context that raises a suggestion of a preceding agreement, not merely parallel conduct that could just as well be independent action." *Id.* at 557.[2] Allegations fail to "plausibly suggest[]" an agreement if they are "merely consistent with" the existence of an

[2] When plaintiffs allege that parallel behavior is the result of an undisclosed agreement, courts often look for the existence of certain so-called "plus-factors" suggesting that the inference of an agreement is plausible. *See infra* Part II.

agreement. *Id.* That is completely different from the district court's apparent reliance on *Twombly* to hold that allegations of concerted action are inadequate to satisfy that element if the alleged agreement is "consistent" with an ultimately lawful agreement. This misreading of *Twombly* erroneously conflates the subsidiary question of whether concerted action exists with the ultimate question of a violation of Section 1. *Am. Needle*, 560 U.S. at 203 (holding that even concerted actions that are "likely" pro-competitive are still concerted actions).

Indeed, such a misreading of *Twombly* would not only be inconsistent with the Supreme Court and Ninth Circuit precedent discussed above, but also would undermine the purpose of Section 1. *Gregory v. Fort Bridger Rendezvous Ass'n*, 448 F.3d 1195 (10th Cir. 2006), is instructive. *Gregory* held that members of a trade association engaged in concerted action under Section 1 when they mutually agreed to criteria that excluded a competitor from a trade show. *Id.* at 1202. The court rejected the argument that the existence of concerted action depended on whether the association's members acted within the scope of their authority, explaining that a reading of the law "exempt[ing] associations of horizontal competitors from liability under the antitrust

laws so long as its board members are acting within the scope of their authority and with the intention to benefit the association as a whole. . . would eviscerate the protections of the Sherman Act because it would permit, for example, horizontal competitors to form associations in which all competitors agree to sell their product at the same supracompetitive price." *Id.*; *see also Goldfarb v. Va. State Bar*, 421 U.S. 773, 791 (1975) (holding the Virginia State Bar violated Section 1 by using ethical opinions to fix prices, even though the Bar had the authority to issue ethical opinions).

Of course, simply because Dental Board members are capable of conspiring under Section 1 does not mean that they always act concertedly. *See N.C. State Bd.*, 717 F.3d at 372 ("[C]oncluding that the Board has the capacity to conspire does not mean, however, that every action taken by the Board satisfies the contract, combination, or conspiracy requirement of section one." (internal quotation marks omitted)). For a claim to satisfy the concerted-action element of Section 1, "the proper question is whether there was any concerted decision" to act in the manner challenged as anticompetitive. Areeda &

Hovenkamp, *supra*, at ¶ 1477.[3] If not, then plaintiffs' Section 1 claim will fail because there was no agreement as a matter of fact—not because defendants acted within their regulatory authority.

B. Concerted actions can be anticompetitive and thus unreasonable even when within the Dental Board's regulatory authority

Adequately alleging concerted action is necessary but not sufficient to plead a Section 1 violation. Plaintiffs must also allege that the concerted action harmed competition and was therefore unreasonable. *See generally Brantley v. NBC Universal, Inc.*, 675 F.3d 1192, 1197 (9th Cir. 2012). To the extent that the district court held that an agreement by the Dental Board on a matter within its regulatory authority cannot be anticompetitive as a matter of law, that holding would be erroneous.

"Restraints can be unreasonable in one of two ways." *Ohio v. Am. Express Co.*, 138 S. Ct. 2274, 2283 (2018). "A small group of restraints are unreasonable per se because they always or almost always tend to

[3] In some circumstances, that concerted action could come in the form of a prior delegation of authority to an agent of a state regulatory board. *Cf. Am. Needle,* 560 U.S. at 204 (holding that "decisions by [joint licensing agent] regarding the teams' separately owned intellectual property constitute concerted action" by the teams).

restrict competition and decrease output." *Id.* at 2283-84. "Restraints that are not unreasonable per se are judged under the 'rule of reason,'" which involves a "fact-specific assessment" of "the restraint's actual effect on competition." *Id.* at 2284. The fact finder considers "the facts peculiar to the business to which the restraint is applied; its condition before and after the restraint was imposed; the nature of the restraint and its effect, actual or probable" along with the "history of the restraint, the evil believed to exist, the reason for adopting the particular remedy, [and] the purpose or end sought to be attained." *Bd. of Trade v. United States*, 246 U.S. 231, 238 (1918). "[D]epending upon the concerted activity in question, the Rule of Reason may not require a detailed analysis; it 'can sometimes be applied in the twinkling of an eye.'" *Am. Needle,* 560 U.S. at 203 (citation omitted).

Under these standards, many alleged concerted actions by board members would likely be reasonable: they neither fall into the category of restraints that always or almost always have anticompetitive effects and thus are per se unlawful (such as price-fixing and market-allocation), nor do they have an appreciable anticompetitive effect such that they would violate the rule of reason. *See* FTC State Regulatory

Board Guidance at 6 (citing certain licensure requirements as examples of restraints not deemed anticompetitive); *cf. American Needle*, 560 U.S. at 202-03 ("[T]hat NFL teams share an interest in making the entire league successful and profitable . . . provides a perfectly sensible justification for making a host of collective decisions," even though they qualify as "concerted activity under the Sherman Act.").

There are, however, situations in which concerted action by board members can be anticompetitive and unreasonable even though the action is within the board's regulatory authority. "[T]he Supreme Court has . . . made pellucid [] that anticompetitive acts are not immune from § 1 because they are performed by a professional organization." *N.C. State Bd.*, 717 F.3d at 375 (*citing Indiana Fed. of Dentists*, 476 U.S. at 459-60; and *Maricopa Cnty. Med. Soc'y*, 457 U.S. at 347-51); Areeda & Hovenkamp, *supra*, at ¶ 1477 (regulatory organizations "act[] unlawfully when [their] essential functions, necessary incidents, or inherent spillovers on [their] members' behavior in their markets are unduly anticompetitive and without adequate redeeming virtues"). The same is true for state regulatory boards, which can be quite "similar to private trade associations." *NC Dental*, 574 U.S. at 511; *see also id.* at

505; *Goldfarb*, 421 U.S. at 791-92 ("The State Bar . . . 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.").

Contrary to the district court's suggestion, *see* ER18, these rulings did not rest on a determination that the challenged anticompetitive acts were beyond the board members' regulatory authority. As the Supreme Court noted, "ethical standards may blend with private anticompetitive motives in a way difficult even for market participants to discern." *NC Dental*, 574 U.S. at 505. Thus, "prohibitions against anticompetitive self-regulation by active market participants are an axiom of federal antitrust policy." *Id.*; *see also* FTC State Regulatory Board Guidance at 5 ("Antitrust issues may arise where an unsupervised board takes actions that restrict market entry or restrain rivalry.").

Goldfarb v. Virginia State Bar, 421 U.S. 773 (1975), is illustrative. Analyzing the anticompetitive effects of a state bar ethical rule that limited price competition, the Supreme Court noted that the bar at issue "is a state agency for some limited purposes" and "apparently *has been granted the power* to issue ethical opinions." *Id.* at 791 (emphasis added). Yet that did not prevent its ethical rules fixing prices from

violating Section 1. Its state agency status "does not create an antitrust shield that allows it to foster anticompetitive practices for the benefit of its members." *Id.*; *see also Allied Tube & Conduit Corp. v. Indian Head*, 486 U.S. 492, 509 (1989) (analyzing a private trade association and concluding that "[t]he antitrust validity of these efforts is not established, without more, by petitioner's literal compliance with the rules of the Association").

C. The state-action exemption is disfavored, limited in scope, and does not apply to actions merely consistent with regulatory authority

While the presence of regulatory authority does not prevent concerted action from being anticompetitive and unreasonable, it is relevant to whether that conduct might nonetheless be protected "state action" under *Parker v. Brown*, 317 U.S. 341 (1953). Under *Parker*, the Sherman Act does not apply to "market restraints [imposed by the State] as an act of government." *Phoebe Putney*, 568 U.S. at 224 (quotation marks omitted). "If the replacing of entirely free competition with some form of regulation or restraint was not authorized or approved by the State then the rationale of *Parker* is inapposite." *Hoover v. Ronwin*, 466 U.S. 558, 568 (1984).

Ex ante state authorization of challenged conduct is not enough to establish state action, however. Given the importance of "the fundamental national values of free enterprise and economic competition that are embodied in the federal antitrust laws," the state-action defense is "disfavored" and narrowly construed. *See* p. 5, *supra*. Accordingly, non-sovereign actors, such as a state regulatory board "controlled by active market participants," can invoke the state-action exemption only if they demonstrate both (1) that the alleged anticompetitive conduct was taken pursuant to a "clearly articulated and affirmatively expressed . . . state policy" to displace competition, and (2) that the conduct was "actively supervised by the State itself." *NC Dental*, 574 U.S. at 504 (citations omitted). It is defendants' burden to demonstrate that they meet its exacting requirements. *NC Dental*, 574 U.S. at 511. State authorization by itself does not satisfy either the clear-articulation or active-supervision requirement.

In particular, the existence of authorization for the challenged conduct does nothing to show it has been actively supervised by the State. As *NC Dental* explained, the active-supervision requirement is important to show that "an anticompetitive policy is indeed the policy of

a State." 574 U.S. at 507. The clear-articulation requirement "rarely will achieve that goal by itself," because "a policy may satisfy this test yet still be defined at so high a level of generality as to leave open critical questions about how and to what extent the market should be regulated." *Id.* Thus "[e]ntities purporting to act under state authority might diverge from the State's considered definition of the public good," and the "resulting asymmetry between a state policy and its implementation can invite private self-dealing." *Id.* The active-supervision requirement "seeks to avoid this harm by requiring the State to review and approve interstitial policies made by the entity claiming immunity." *Id.* Looking for authorization alone would render the active-supervision requirement superfluous, in direct contravention of *NC Dental*.[4]

[4] State authorization of the challenged conduct does not itself satisfy the clear-articulation requirement either. This requirement is met "if the anticompetitive effect was the 'foreseeable result' of what the State authorized." *Phoebe Putney*, 568 U.S. at 226-27. "Once we determine that there is express state authorization, we then turn to the concept of foreseeability, which 'is to be used in deciding the reach of antitrust immunity that stems from" the authorization. *Chamber of Commerce of the United States v. City of Seattle*, 890 F.3d 769, 783 (9th Cir. 2018). Thus, even authorized conduct will remain subject to the antitrust laws if the anticompetitive consequence is not a foreseeable consequence of

Here, the district court rejected the application of the state-action doctrine. *See* p. 9, *supra*. It then, however, essentially undid that determination through its ruling that Plaintiffs failed to state a Section 1 claim because Defendants' conduct was "consistent with the [] Board's regulatory purpose" and within its authority. *See* ER18. This was improper both substantively and procedurally. It was substantively wrong because effectively expanding the state-action exemption in this manner would allow regulatory boards to escape antitrust liability under a far less "exacting" standard than is required. *Chamber of Commerce of the United States v. City of Seattle*, 890 F.3d 769, 781 (9th Cir. 2018). Additionally, it was procedurally wrong because it erroneously shifted the relevant burden: Defendants have the burden to prove that the Board's conduct is protected state action, but instead the court required Plaintiffs to prove that the challenged conduct was beyond the Board's regulatory authority (which is not a proper limitation on Section 1 liability).

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its authorization. *Cf. Goldfarb*, 421 U.S. at 790 (holding that State Bar's authority to issue ethical rules did not exempt rule fixing prices from Section 1).

The district court indicated that limiting Section 1 in this manner was necessary to prevent excessive antitrust litigation. *See* ER19 (expressing concern that "every single time such an investigation commences the courts should expect a Sherman Act challenge"). This view disregards the Supreme Court's exhortation in *NC Dental* that state regulatory boards controlled by active market participants remain subject to Section 1 scrutiny. "Limits on state-action immunity are most essential when the State seeks to delegate its regulatory power to active market participants." 574 U.S. at 505. "State agencies controlled by active market participants, who possess singularly strong private interests, pose the very risk of self-dealing" that the limits on the state-action defense protect against. *Id.* at 510.

Courts already possess ample means for curtailing unmeritorious Section 1 claims without needing to create a novel exemption for state regulatory boards. To avoid dismissal, plaintiffs must plausibly allege both that an agreement exists and that it is unreasonable. Moreover, depending on the challenged conduct, the Rule of Reason can sometimes be applied quickly, even on a motion to dismiss. *See* p. 22, *supra*.

II. This Court Should Vacate and Remand to the District Court To Perform the Correct Sequential Analysis of Concerted Action and Unreasonableness

Because the district court erred by dismissing the claim on the basis that the board has regulatory authority to undertake investigations, this Court should vacate the decision below and remand to the district court to conduct the proper sequential analysis of concerted action and anticompetitive effect. We take no position on the merits of Plaintiffs' Section 1 claim but offer the following guidance on those inquiries.[5]

A. Concerted action

The district court should first determine whether Plaintiffs have adequately alleged an agreement among the Defendants to act in the manner challenged as anticompetitive. *See* Part I.A, *supra*.

Concerted action may be adequately alleged—and later proved—either through direct or indirect evidence. *See Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 764 (1984). Direct evidence of agreement

[5] As the district court denied the motion to dismiss on the basis of the state action doctrine, *see* ER424-30, and that ruling has not been appealed, this brief does not provide additional guidance on that subject.

among board members may include such acts as votes or organization rules. *See N.C. State Bd.*, 717 F.3d at 373 ("The FTC found both direct and circumstantial evidence to support a finding of concerted action. . . . [T]he FTC concluded that 'on several occasions, the Board discussed teeth whitening services provided by non-dentists and then voted to take action to restrict these services.'") (alterations omitted); *Robertson v. Sea Pines Real Estate Cos.*, 679 F.3d 278, 289 (4th Cir. 2012) (holding that concerted action was sufficiently alleged based "on allegations that the MLS board members conspired in the form of the MLS rules, the very passage of which establishes that the defendants convened and came to an agreement").

A plaintiff also can rely on indirect or circumstantial evidence of an agreement. To allege an agreement from circumstantial evidence, a plaintiff must allege "enough factual matter (taken as true) to suggest [plausibly] that an agreement was made. . . . [This requirement] does not impose a probability requirement at the pleading stage; it simply calls for enough fact to raise a reasonable expectation that discovery will reveal evidence of illegal agreement." *Twombly*, 550 U.S. at 556. To infer conspiracy from circumstantial evidence, this Court frequently

looks for the existence of parallel conduct and certain so-called "plus factors" to render the inference of an agreement plausible. *See In re Musical Instruments & Equip. Antitrust Litig.*, 798 F.3d 1186, 1194 & n.7 (9th Cir. 2015).[6] Examples of plus factors include: common motive to conspire, action against self-interest, government investigation, participation in trade associations, and parallel pricing. *Id.*; *see also In re Citric Acid Litig.*, 191 F.3d 1090, 1102 (9th Cir. 1999); William E. Kovacic et al., *Plus Factors and Agreement in Antitrust Law*, 110 Mich. L. Rev. 393 (2011) (discussing the probative value of different types of plus factors). Allegations of plus factors are examined individually and cumulatively. *Musical Instruments*, 798 F.3d at 1194.

[6] This Court has also stated that, to infer the existence of an agreement, the complaint should contain sufficient factual allegations to "answer the basic questions: who, did what, to whom (or with whom), where, and when?" *Kendall v. Visa U.S.A., Inc.*, 518 F.3d 1042, 1048 (9th Cir. 2008). *Kendall* has been criticized for wrongly imposing a heightened pleading standard. *See In re Delta Dental Antitrust Litig.*, 2020 WL 5296996, at *7 n.3 (N.D. Ill. Sept. 4, 2020). Similarly, in *Frost v. LG Electronics*, 801 F. App'x 496 (9th Cir. 2020), both the concurring and dissenting judges questioned *Kendall's* consistency with *Twombly*. In any event, adequate allegations of circumstantial evidence of agreement are unnecessary when a plaintiff adequately alleges an agreement based on direct evidence. *See Robertson*, 679 F.3d at 289; *see also* U.S. Visa Am. Br., at 13-17 & n.4 (distinguishing *Kendall* on this basis).

In this matter, Plaintiffs are not simply challenging the investigation itself. Rather, they are alleging that it was part of a broader, secret conspiracy among the board members to restrain Plaintiffs' ability to compete in California—which the board members either reached before the investigation began or afterward by ratifying the investigators' conduct. *See* FAC ¶¶ 102-03 (ER143-45); *see also* ER56-59. As support for this alleged conspiracy, Plaintiffs relied on several "plus factors," specifically the opportunities to conspire, the highly regulated nature of the field, the lengthy timeframe of the investigation, and government enforcement activity in this sector.[7] *See* FAC ¶ 102 (ER143-44); ER58-59; pp. 10-11, *supra*.

The district court observed "that these [plus] factors would exist any time a state regulatory board that consists, at least in part, of market-participants, engages in an investigation of other market-

[7] Plaintiffs alleged that the "FTC and DOJ have filed amicus briefs supporting [Smile Direct's] challenges to conduct in other states similar alleged in the complaint." FAC ¶ 102 (ER144). These amicus briefs were about the proper contours of the state-action doctrine and did not address the merits of any Section 1 claims against state regulatory boards.

participants." ER19. It did not, however, conduct a full plus-factor analysis (as Plaintiffs urged) or otherwise determine whether or not there were adequate allegations of concerted action under the correct legal standard.[8] The case should be remanded to the district court to do so in the first instance.

B. Reasonableness

If the district court determines that Plaintiffs adequately alleged concerted action, then it must then decide whether Plaintiffs adequately alleged that the restraint is anticompetitive—and thus unreasonable. The district court never evaluated whether Plaintiffs' allegations sufficed to allege harm to competition because of its mistaken view that the board acting within its regulatory authority was dispositive.

A "section one claimant may not merely recite the bare legal conclusion that competition has been restrained unreasonably," *Les Shockley Racing, Inc. v. National Hot Rod Ass'n*, 884 F.2d 504, 508 (9th Cir. 1988), but instead must allege sufficient facts to render a Section 1

[8] As noted above, there are numerous ways for a plaintiff to prove concerted action, including direct evidence of agreement. *See* pp. 30-31, *supra*. The discussion here focuses on the plus-factor arguments that were raised below.

violation "plausible," *Musical Instruments*, 798 F.3d at 1193. In particular, "section one claimants must plead and prove a reduction of competition in the market in general and not mere injury to their own positions as competitors in the market." *Les Shockley*, 884 F.2d at 508. In some circumstances, however, injury to a competitor can form the basis of harm to competition, for example "when the relevant market is both narrow and discrete and the market participants are few." *Id.* at 508-09. Thus, in *Oltz v. Saint Peter's Community Hospital*, this Court held that the evidence supported a finding that the exclusion of a single provider from a market "had actual detrimental effects on competition," as "[s]ome patients and surgeons who preferred the services of Oltz were hindered from obtaining them" and "the price of anesthesia services and the incomes of the M.D. anesthesiologists rose dramatically because of the challenged restraint." 861 F.2d 1440, 1448 (9th Cir. 1988).

The scope of the alleged agreement is relevant, because that delineates what must be found unreasonable. For instance, an agreement by Board members to prevent a competitor with an allegedly disruptive new business model for providing certain teeth straightening

services from effectively competing in California may be more likely to have anticompetitive effects than an agreement to conduct other types of investigations. In *NC Dental*, for example, the Fourth Circuit noted that "[i]t is not difficult to understand that forcing low-cost teeth-whitening providers from the market has a tendency to increase a consumer's price for that service," and thus be anticompetitive. 717 F.3d at 374.

CONCLUSION

The Court should hold that board members can engage in unreasonable concerted action even when the challenged conduct falls within the board's regulatory authority, and vacate and remand so that the district court can perform the correct analysis of the Section 1 claim.

Respectfully submitted.

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