Supreme Court Limits State Action Immunity

The state action doctrine immunizes from antitrust scrutiny anticompetitive conduct that constitutes the action of a state itself. However, courts have not always been consistent in applying the state action doctrine to the conduct of local governments (or private parties) who act in accordance with state policy. The Supreme Court granted certiorari this term in FTC v. Phoebe Putney Health System – the Court's first major state action doctrine case in decades – to address whether state action immunity bars a Clayton Act merger challenge to a public hospital authority's acquisition of a private hospital, which was the largest competitor of a hospital operated by the authority. On February 19, 2013, the Supreme Court unanimously held that state action immunity was unavailable because the Georgia state legislature had not "clearly articulated and affirmatively expressed a policy allowing hospital authorities to make acquisitions that substantially lessen competition."1

A. Background

1. State Action Doctrine

In Parker v. Brown,2 the Supreme Court held that the federal antitrust laws do not apply to market restraints imposed by state legislatures. In subsequent cases, courts have held that the immunity applies not only to the acts of the state legislature, but may also extend to the state's highest court and to the executive branch (such as the governor). However, subordinate government entities (such as state agencies) and political subdivisions (such as cities) cannot invoke the state action doctrine through Parker directly, because they are not sovereign states. To avail themselves of state action immunity, subordinate governmental entities must demonstrate that they have acted "pursuant to state policy to displace competition with regulation or monopoly public service."3 In other words, a state may delegate administration of state regulatory schemes to subordinate governmental entities "free of the inhibitions of the federal antitrust laws without at the same time permitting purely parochial interests to disrupt the Nation's free-market goals."4

However, in order to invoke the protections of the state action doctrine, subordinate governmental bodies must show that their action was undertaken pursuant to a "clearly articulated and affirmatively expressed … state policy."5 It is not necessary for the state

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2 317 U.S. 341 (1943).
3 Phoebe Putney, No. 11-1160, slip op. at 7 (internal quotation marks omitted).
legislature to “expressly state in a statute or its legislative history that the legislature intends for the delegated action to have anticompetitive effects.”

Rather, “immunity applies if the anticompetitive effect was the ‘foreseeable result’ of what the State authorized.”

For cities, counties, and municipalities, clear articulation of a state policy to displace competition is the only showing necessary to obtain immunity. While private (non-governmental) entities may also invoke the state action doctrine when they act in accordance with a state regulatory scheme, private parties ordinarily must make an additional showing – they must show not only that their conduct conformed to a clearly articulated and affirmatively expressed state policy, but also that their conduct was “actively supervised by the State.”

2. Hostility to the State Action Doctrine

The FTC has taken a hostile position toward the state action doctrine in recent years, as lower courts have applied state action immunity to an increasing variety of cases. In 2001, the agency created the State Action Task Force to examine and make recommendations regarding the state action doctrine. In 2003, the Task Force issued a report warning that courts’ application of both the clear articulation and the active supervision standards had become too lax, and that “overbroad interpretations of the state action doctrine could potentially impede national competition policy goals.”

The report recommended that the FTC work to encourage the courts to re-affirm, clarify, and strengthen the clear articulation and active supervision standards, and advocate for stringent application of the state action doctrine by the courts.

Similarly, the Antitrust Modernization Commission, created by Congress in 2004 to review U.S. antitrust law to determine whether changes were required, issued a report finding that lower courts in some cases “misinterpreted or misapplied the state action doctrine … in ways inconsistent with Supreme Court rulings” and granted immunity where a state did not intend to authorize anticompetitive conduct.

The Antitrust Modernization Commission recommended that these concerns be resolved through litigation and more precise application of Supreme Court precedents by the lower courts.

B. The FTC’s Case and the Decisions Below

Georgia state law authorizes municipalities to form public hospital authorities to ensure that the public has access to hospital services. To that end, the law grants hospital authorities broad powers to operate, acquire, and lease health services projects. In April 2011, one such hospital authority approved the plan of Phoebe Putney Health System (PPHS) – a private non-profit created by the hospital authority to manage hospitals it had acquired in the area – to acquire the only remaining hospital in the authority’s jurisdiction owned by a third party. Under the plan, the hospital authority would purchase the hospital – then owned by for-profit healthcare giant HCA – and lease it to PPHS for one dollar per year, effectively creating a regional monopoly for hospital services.

The FTC sued to enjoin the acquisition as a violation of Section 7 of the Clayton Act, which outlaws acquisitions that may substantially lessen competition.

The defendants moved to dismiss the case on the grounds that the acquisition was immune from federal antitrust liability under the state action doctrine. The district court found that state action immunity applied to the transaction and dismissed the case. The FTC appealed, and the U.S. Court of Appeals for the Eleventh Circuit affirmed, holding that the state legislature had “clearly articulated” a policy to displace competition for hospital services because “in granting the power to acquire hospitals, the legislature must have anticipated that such acquisitions would produce anticompetitive effects.”

The Eleventh Circuit reasoned that the legislature must have foreseen that granting such broad powers to hospital

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[10] Id. at 3-4.
[12] Id.
authorities under the statute, including the authority to acquire hospitals, was likely to harm competition. The court explained: “It defies imagination to suppose the legislature could have believed that every geographic market in Georgia was so replete with hospitals that authorizing acquisitions by the authorities could have no serious anticompetitive consequences.” The Eleventh Circuit, finding that the hospital authority was a political subdivision subject only to the clear articulation standard, did not address the active supervision prong of the state action doctrine analysis.

C. The Supreme Court’s Opinion
The Supreme Court granted the FTC’s petition for writ of certiorari and, on February 19, 2013, reversed the Eleventh Circuit’s decision, holding that the transaction was not immune from antitrust scrutiny under the state action doctrine because “[w]hen a State’s position is one of mere neutrality respecting the municipal actions challenged as anticompetitive, the State cannot be said to have contemplated those anticompetitive actions.”

The Court essentially reaffirmed its prior state action doctrine holdings, including the “foreseeable result” standard, but clarified that if a regulatory scheme could reasonably be carried out without any anticompetitive effects and the legislature has not expressly authorized the anticompetitive actions at issue, the state action doctrine does not apply.

The Court agreed with the FTC’s narrow interpretation of the foreseeable result standard: if powers delegated under a state statute can be fully exercised without anticompetitive effect, the statute’s grant of authority alone is insufficient to establish “clear articulation” of a state policy to displace competition. The Court reiterated that while the state policy need not be explicitly stated to satisfy the clear articulation standard, the state legislature “must have foreseen and implicitly endorsed the anticompetitive effects as consistent with its policy goals.”

In the holding, the Court took issue with the Eleventh Circuit’s “loose” application of the “foreseeability” test in the Court’s clear articulation test – i.e., that the state action doctrine applies to a subordinate governmental unit if it is “foreseeable” that the subordinate governmental unit will apply its delegated powers in a manner that displaces competition. “[W]hen a State’s position is one of mere neutrality respecting the municipal actions challenged as anticompetitive, the State cannot be said to have contemplated those anticompetitive actions.”

The respondents argued that the broad powers granted under the statute clearly articulated a policy to displace competition in light of the state’s regulatory regime governing hospitals generally, which places significant regulatory burdens and limitations on ownership, expansion, and construction of new hospitals. The Court dismissed this argument, noting that “regulation of an industry, and even the authorization of discrete forms of anticompetitive conduct pursuant to a regulatory structure, does not establish that the state has affirmatively contemplated other forms of anticompetitive conduct that are only tangentially related.”

The Court’s opinion echoes the view of the Antitrust

15 Id.
17 Id. at 10 (internal quotation marks omitted).
18 Id. (internal quotation marks omitted).
19 Id. at 11.
20 Id. at 12.
21 Id. at 17.
Modernization Commission that the clear articulation standard should focus on: "(1) whether the conduct at issue has been authorized by the state, and (2) whether the state has deliberately adopted a policy to displace competition in the manner at issue."

Finally, the Court also rejected the argument that courts should err on the side of finding immunity where there is any doubt about whether the clear articulation test is satisfied. Instead, the Court reiterated the view it expressed in *Ticor Title* that "state-action immunity is disfavored."

Interestingly, the Court never reached the second question presented – whether, even if the state law clearly authorized the hospital authority to displace competition, the purchase-and-lease arrangement in this case would nonetheless violate antitrust law because the hospital authority’s role was reduced to that of a strawman facilitating an unsupervised private anticompetitive transaction. The Court chose instead to use this case as an opportunity to clarify and refine its state action doctrine analysis. In so doing, the Court avoided the often perplexing question of when conduct is “private” in nature and therefore requires “active supervision” by the state in order to be protected by the state action doctrine.

**D. Implications**

The decision marks a significant victory for the FTC in its crusade against the state action doctrine. In reversing the Eleventh Circuit, the Supreme Court clarified the outer boundaries of the clear articulation test and emphasized that state action immunity is disfavored.

Before this case, many lower courts had found immunity by interpreting the clear articulation test broadly, and by taking an expansive view of when anticompetitive conduct by a subordinate state entity is “foreseeable” by the state. The Court’s *Phoebe Putney* decision will almost certainly preclude such expansive interpretations of the scope of the state action doctrine in the future. After *Phoebe Putney*, lower courts will be hard-pressed to conclude that anticompetitive conduct was “foreseeable” by the state in circumstances where the anticompetitive conduct was not “actually contemplated” by the state. As a result, subordinate government entities (and private parties acting pursuant to a government regulatory scheme) will now face a much higher hurdle in obtaining state action immunity.

If you have any questions about any of the topics discussed in this advisory, please contact your Arnold & Porter attorney or the following attorneys:

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24 *FTC v. Phoebe Putney Health Sys.*, No. 11-1160, slip op. 18 (internal quotation marks omitted).