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NINTH CIRCUIT DISMISSES FTC CHALLENGE TO CALIFORNIA DENTAL ASSOCIATION'S RESTRICTIONS ON MEMBER ADVERTISING

The United States Court of Appeals for the Ninth Circuit, on remand from the U.S. Supreme Court, has dismissed the Federal Trade Commission's complaint challenging advertising restrictions imposed by the California Dental Association ("CDA") on its members. *California Dental Ass'n v. FTC*, 2000 WL 1239199 (9th Cir., Sept. 5, 2000). The CDA required that member dentists disclose the exact prices for services mentioned in ads offering discounts, and prohibited members from including unverifiable claims about the quality of their services. The court concluded that the FTC failed to show these restrictions impermissibly restricted competition in the market for dental services, and ordered dismissal of the case.

Factual Background

CDA is part of the American Dental Association ("ADA"), and is comprised of numerous local component societies. Individual dentists in California must be members of a component society to join CDA, and must have CDA membership to join ADA. Roughly 75 percent of licensed dentists in California belong to CDA, though membership is not required for state licensure.

CDA members must comply with the CDA Code of Ethics ("Code"), which, together with separate advertising guidelines and advisory opinions issued by CDA, restricts the types of statements members may make in their ads. The guidelines require that all ads offering discounts state the dollar amount of the nondiscounted fee for each service, as well as either the dollar

amount or percentage of the discount, the length of time the discount is offered, and any terms, conditions, or restrictions on qualifying for the discount. CDA also issued advisory opinions prohibiting members from making unverifiable claims about the quality of their services (*e.g.*, "gentle, quality care", "fast and caring"), or their fees (*e.g.*, "reasonable fees," "lowest prices," "as low as," "and up"). The Code authorized CDA to impose penalties for a violation of these restrictions, ranging from censure to denial of membership or expulsion.

Prior Proceedings

The FTC challenged CDA's advertising restrictions in an administrative complaint filed in July 1993. The case was tried before an FTC Administrative Law Judge ("ALJ"), who ruled in July 1995 that CDA had unreasonably restrained competition in violation of Section 5 of the FTC Act. The ALJ concluded that CDA's advertising restrictions barred members from making representations of "low" or "reasonable" or "affordable" prices, effectively prohibited across-the-board discounts (by requiring dentists to list the nondiscounted price of each service to which the discount applied), and barred forms of price and quality advertising without regard to the truth or falsity of the ads.

The FTC affirmed the ALJ's decision in March 1996. *California Dental Ass'n*, 121 FTC 190 (1996). The FTC ruled that CDA's restrictions on price advertising were unlawful per se, and that its nonprice restrictions were unlawful under an abbreviated or "quick-look" rule of reason analysis. In October 1997, the U.S. Court of Appeals for the Ninth Circuit affirmed the FTC's ruling. *California Dental Ass'n v. FTC*, 128 F.3d 720 (9th Cir. 1997), *aff'd in part, rev'd in part and remanded*, 526 U.S. 756 (1999). The court of appeals held that the FTC erred in applying a per se standard to CDA's restrictions on price advertising, but concluded that both the price and nonprice restrictions were unreasonable under an abbreviated rule of reason analysis.

The Supreme Court, in a May 1999 decision, held that the court of appeals erred in applying an abbreviated rule of reason analysis, because CDA's restrictions do not amount to an obvious restraint on trade, and because there was a lack of direct evidence of actual anticompetitive effects. *California Dental Ass'n v. FTC*, 526 U.S. 756 (1999). The Court also credited CDA's concern that misleading ads could harm competition and consumers, given the disparities in information available to dentists and to patients. The Court remanded the case "for a fuller consideration of the issue," under a less abbreviated (but unspecified) rule of reason analysis.

Summary of Decision on Remand

On remand, the court of appeals engaged in a more extensive rule of reason analysis, focusing on (1) whether CDA intended to harm or restrain competition, (2) whether an actual injury to competition occurred, and (3) whether the restraint was unreasonable as determined by balancing anticompetitive effects against any justifications or procompetitive effects.

The court found the evidence of CDA's intent to be ambiguous and not favoring either party, noting that, although CDA clearly intended to restrict certain types of advertising, it advanced plausible procompetitive reasons for doing so (*i.e.*, to prohibit consumers from being misled). Consistent with its first decision, the court also found that CDA had caused anticompetitive effects, in that it prohibited certain types of potentially competition-enhancing advertising without regard to the ads' truth or falsity.

The court then balanced the procompetitive benefits claimed by CDA, noting the Supreme Court's instruction to consider them with much greater care, and found that these benefits outweighed any competitive harm CDA had caused. The court's analysis is patterned on issues raised by the Supreme Court concerning the scope of CDA's restrictions, and the behavior of consumers in evaluating dentists and their services.

The court agreed with the Supreme Court's observation that, due to an information disparity between dentists and consumers, misleading ads for dental services might be particularly harmful, because dentists can evaluate the cost and quality of services far better than consumers. The court also agreed with CDA that its restrictions were far from a complete ban on advertising, and that these restrictions could reduce the information disparity by providing consumers with more detailed and accurate information. The court concluded that there is a reasonable likelihood that ads falling within CDA's restrictions could mislead consumers, and that preventing such ads is procompetitive. On the other hand, the court found the FTC had not shown that prohibited types of ads benefit consumers, and had not quantified any actual competitive harm caused by CDA. The FTC relied on published studies showing that restrictions on ads had increased the cost of other professional services, but the court rejected this evidence – which primarily concerned a total ban on ads for legal services – as having limited applicability to CDA's partial restriction on ads for dental services.

The FTC requested that the case be remanded so additional empirical evidence and expert testimony on competitive harm

could be submitted to the ALJ. The court denied this request, noting that FTC staff withheld this evidence at the original trial, and instructed the FTC to dismiss the case.

Impact of Decision on Professional Associations

The court of appeals ruling underscores the inherent difficulty under the rule of reason of showing that limited restrictions on ads for professional services have had a net anticompetitive effect. At the same time, the decision shows the importance of documenting that such restrictions are adopted and enforced for procompetitive purposes, and are narrowly-focused on correcting demonstrable (or intuitively obvious) problems with such ads, which themselves may harm competition.

Despite CDA's victory, professional associations should proceed with caution in adopting and enforcing policies that restrict member ads. There are several reasons for such caution.

The court of appeals found that CDA caused an actual harm to competition, primarily because its restrictions applied without regard to whether challenged ads in fact were shown to be false or deceptive. In its 1997 decision, the court based this conclusion on a cursory assessment of the scope and character of the restrictions, not on detailed market evidence of actual detrimental effects on price, output, or quality of services. The court now has reaffirmed this conclusion following remand again without direct supporting evidence of actual competitive harm. The court's reasoning suggests that at least a limited presumption of anticompetitive effect may be permissible if a restriction on ads is overbroad, despite the Supreme Court's direction that a "less quick" rule of reason analysis be used to evaluate the competitive effects of CDA's conduct. Thus, a professional association still may have to overcome a presumption of anticompetitive effect if its restriction on member ads is sufficiently broad in scope to prohibit some ads that appear capable of benefitting customers.

The court's ruling also was influenced by tactical decisions of FTC staff which are not likely to recur in future cases. The court declined to remand the case to the FTC for further trial proceedings because FTC staff chose not to introduce additional evidence of anticompetitive effects at the original trial. The staff presumably based its trial strategy on FTC decisions in other cases, in which a quick-look standard was applied to restraints on ads for (or other conduct associated with the marketing of), professional services. In future cases, the FTC or other claimants are likely to focus on proving net anticompetitive effects directly, rather than relying on presumptions.

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The Supreme Court left unresolved whether a rule of reason analysis more truncated than that employed by the court of appeals following remand, may properly be applied in other contexts to restrictions on ads for professional services. This may depend not only on the nature of the restrictions and the type of professional services in question, but also on whether there is evidence of anticompetitive intent. Moreover, both courts emphasized that CDA's restrictions were far from a total restraint on member ads, which suggests that a more restrictive program still may be judged under a more abbreviated rule of reason standard, or even declared illegal per se. Both courts also emphasized the procompetitive benefit of reducing information disparities between dentists and their customers, but the extent of this concern may vary as to advertising for other professional services, particularly where customers are businesses rather than consumers. By the same token, the other procompetitive benefits suggested by CDA and considered by the court of appeals are not a "litmus test" that necessarily will apply to other restrictions on ads for professional services. Each program must be judged based on the particular market setting in question, and the harm to consumers or businesses which the restrictions seek to prevent.

Advertising restraints remain an active focus of government antitrust enforcement, particularly for the FTC, and most associations that have been the subject of a government investigation for such conduct have entered into consent orders rather than litigate. The case against CDA already has spanned over seven years (not including the FTC's precomplaint investigation), and the court of appeals decision still is subject to possible review by the Supreme Court. Many associations may lack the resources, or the organizational resolve shown by CDA, to persist in defense of a program restricting ads by members.

In recent testimony, FTC Chairman Robert Pitofsky noted that the FTC cleared restrictions proposed by the Direct Marketing Association on unsolicited direct mail or telephone marketing practices of its members, and likely would not oppose industry-sponsored restrictions on ads and other marketing directed at children for entertainment products with violent content. *See Antitrust Implications of Entertainment Industry Self-Regulation To Curb the Marketing of Violent Entertainment Products To Children*, Prepared Statement of the Federal Trade Commission by Robert Pitofsky, Chairman, Before the Committee on the Judiciary, United States Senate, www.ftc.gov/os/2000/09/jctestimony.htm (Sept. 20, 2000). In each case, however, special circumstances were noted the former program is based on consumer self-selection to opt out of receiving unsolicited ads; the latter would address special

problems associated with ads directed at children, and would not extend to adult-focused ads and marketing. Pitofsky stated that the FTC will support industry self-regulation that, on balance, has procompetitive benefits for consumers, but reaffirmed that the FTC will continue to challenge such efforts if they restrict, rather than further, the competitive process.

Conclusion

The court of appeals decision is a significant vindication of CDA advertising restrictions, and also is significant as the first direct application of the Supreme Court's 1999 decision limiting the use of presumptions of competitive harm to invalidate restrictions on ads for professional services. The court's analysis, however, underscores that the rule of reason is inherently fact-specific, and that professional associations must carefully evaluate the competitive effect of restrictions on member ads in the particular market setting in question. Thus, despite CDA's victory, professional associations should ensure that such programs have a clearly-documented procompetitive purpose, are focused narrowly on ads that pose a meaningful and demonstrable risk of misleading consumers or causing some other identifiable harm, and are carefully administered in consultation with antitrust counsel to avoid unintended anticompetitive effects.

- Return to: Trade & Professional Association Bulletin
- Return to the Vedder Price: Publications Page.
- Return to: Top of Page.

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Top of Page