



BUREAU OF COMPETITION

UNITED STATES OF AMERICA
FEDERAL TRADE COMMISSION
WASHINGTON, D.C. 20580

1770002
V890032
COMMISSION AUTHORIZED

March 13, 1989

George L. Schroeder
Director
Legislative Audit Council
State of South Carolina
620 NCNB Tower
Columbia, South Carolina 29201

Dear Mr. Schroeder:

The staff of the Federal Trade Commission 1/ is pleased to respond to the invitation of the Legislative Audit Council of the State of South Carolina to comment on Regulation 11-17 of the South Carolina Board of Architectural Examiners. 2/ Regulation 11-17, as interpreted by the Board, 3/ prohibits architects from participating in competitive bidding or "donat[ing] services" to clients with the intent of influencing the client's award of a project. We believe that the regulation is likely to harm competition and suggest that the Council consider the regulation's anticompetitive effects in determining whether it should be retained.

I. Interest and Experience of the Federal Trade Commission

The Federal Trade Commission is charged by statute with preventing unfair methods of competition and unfair or deceptive acts or practices in or affecting commerce. 15 U.S.C. § 45. Under this statutory mandate, the Commission seeks to identify restrictions that impede competition or increase costs without offering countervailing benefits to consumers. The Commission has sought to improve consumer access to professional services by initiating antitrust enforcement proceedings 4/ and conducting

1/ These comments represent the views of the staff of the Federal Trade Commission's Bureau of Competition and do not necessarily represent the views of the Commission itself or any individual Commissioner.

2/ Regulations of Board of Architectural Examiners, § 11-17.

3/ Board of Architectural Examiners, Administrative Interpretation of Regulation 11-17 (September 1988).

4/ See, e.g., Massachusetts Board of Registration in Optometry, [FTC Complaints and Orders transfer binder] 5 Trade Reg. Rep.
(continued...)

studies concerning various facets of the regulation of licensed professions. 5/ In addition, the Commission's staff has submitted comments to state legislatures and administrative agencies on various issues of professional licensing and regulation. 6/ As one of the two federal agencies with principal responsibility for enforcing the antitrust laws, the Commission is particularly interested in restrictions that may adversely affect the competitive process and raise prices to consumers.

II. Analysis of Regulation 11-17

Regulation 11-17 of the South Carolina Board of Architectural Examiners states in its entirety: "Architects shall not enter into a contract for professional services on any basis other than direct negotiation thereby precluding participation in any system requiring a comparison of compensation." As interpreted in a September 1988 administrative interpretation of the Board, Regulation 11-17 prohibits architects from participating in competitive bidding or "donat[ing]" architectural services to prospective clients. 7/ These prohibitions are discussed below.

4/(...continued)

(CCH) ¶ 22,555 (June 21, 1988); Rhode Island Board of Accountancy, 107 F.T.C. 293 (1986)(consent order); Louisiana State Board of Dentistry, 106 F.T.C. 65 (1985) (consent order); American Medical Ass'n, 94 F.T.C. 701 (1979), aff'd, 638 F.2d 443 (2d Cir. 1980), aff'd mem. by an equally divided court, 455 U.S. 676 (1982); American Dental Ass'n, 94 F.T.C. 403 (1979), modified, 100 F.T.C. 448 (1982), 101 F.T.C. 34 (1983) (consent order).

5/ See, e.g., Cleveland Regional Office and Bureau of Economics, Federal Trade Commission, Improving Consumer Access to Legal Services: The Case for Removing Restrictions on Truthful Advertising (1984); Bureaus of Consumer Protection and Economics, Federal Trade Commission, A Comparative Analysis of Cosmetic Lens Fitting by Ophthalmologists, Optometrists, and Opticians (1983); Bureau of Economics, Federal Trade Commission, Effects of Restrictions on Advertising and Commercial Practice in the Professions: The Case of Optometry (1980).

6/ In the past two years, Commission staff have commented on rules of professional conduct or regulations governing attorneys, chiropractors, dentists, optometrists, pharmacists, physical therapists, physicians, and real estate brokers.

7/ Architects are subject to disciplinary action for "dishonest practice, unprofessional conduct or incompetent practice" if they violate the Board's rules. Regulations of Board of Architectural Examiners, § 11-15, 11-15(A)(3).

(a) The Ban on Competitive Bidding

Regulation 11-17 and the Board's interpretation prohibit architects from participating in competitive bidding. Under the regulation, architects may not participate in a "system requiring a comparison of compensation," such as competitive bidding. The Board's interpretation permits architects to disclose their compensation only "in direct negotiations where architectural services necessary to protect the public health, safety and welfare have been defined." 8/

As you know, the Supreme Court has held that a ban on competitive bidding imposed by the National Society of Professional Engineers violated section 1 of the Sherman Act. 9/ Similar bans in the medical 10/ and accounting 11/ professions have also been held unlawful. 12/ While a prohibition on competitive bidding may not eliminate price competition, it increases customers' search costs in procuring the services of architects. Because Regulation 11-17 permits architects to disclose their price only in individual negotiations, purchasers of architectural services are forced to engage in a process of preliminarily selecting an architect, negotiating a price, and then either hiring the architect or selecting another architect and beginning the process afresh. 13/ Because such a process often will be less efficient than a single competitive bidding

8/ Administrative Interpretation of Regulation 11-17, supra note 3.

9/ National Society of Professional Engineers v. United States, 435 U.S. 679 (1978).

10/ American Medical Association, 94 F.T.C. at 1014-15.

11/ United States v. Texas State Board of Public Accountancy, 464 F. Supp. 400 (W.D. Tex. 1978), aff'd as modified, 592 F.2d 919 (5th Cir.), cert. denied, 444 U.S. 925 (1979).

12/ You have requested the staff's views "on whether this regulation promotes any restrictive or anticompetitive practices." Accordingly, we do not comment on whether the Board of Architectural Examiners is immune under the state action doctrine to an antitrust action for its promulgation and enforcement of Regulation 11-17. These comments thus do not address the lawfulness of the regulation but solely its effects on consumer welfare.

13/ This was the process required by the rule condemned in the Professional Engineers case. See 435 U.S. at 692.

contest, it necessarily increases search costs. As a result, the dispersion of prices in the market will tend to be greater than in the absence of a prohibition on competitive bidding. ^{14/} In addition, such a prohibition may increase the average price paid by consumers for architectural services. ^{15/}

The Board's interpretation appears to link the competitive bidding prohibition to considerations of the public health and safety. Other private and public means that are less restrictive of competition, however, may be available to protect these interests. For example, construction projects are subject to building codes, which are specifically designed to protect the public health and safety. ^{16/} In addition, potential exposure to tort liability creates an incentive for all parties involved in a building project -- from the client, to the architect, to the builder -- to take actions necessary to protect public safety. Consequently, restrictions on competitive bidding may not be necessary to protect the public health and safety. As the Supreme Court has observed, the notion that price competition may threaten public safety is "nothing less than a frontal assault on the basic policy of the Sherman Act." ^{17/}

(b) The Ban on "Donating" Services

The Board's interpretation also prohibits architects from "offer[ing] to donate professional services with the intent of

^{14/} See generally G. Stigler, The Organization of Industry 171-87 (1968). The term dispersion refers to the scattering of prices above or below their average level.

^{15/} See Butters, Equilibrium Distributions of Sales and Advertising Prices, 44 Rev. Econ. Stud. 465 (1977).

^{16/} Moreover, Regulation 11-15(B)(3) of the Board requires architects who discover any decision by a client that violates applicable building codes or "materially affect[s] the safety to the public of the finished project" to take specific corrective actions, including notification of governmental authorities.

^{17/} National Society of Professional Engineers v. United States, 435 U.S. at 695. The Court added: "Exceptions to the Sherman Act for potentially dangerous goods and services would be tantamount to repeal of the statute. In our complex society, the number of items that may cause serious harm is almost endless -- automobiles, drugs, foods, aircraft components, heavy equipment, and countless others, cause serious harm to individuals if defectively made. The judiciary cannot indirectly protect the public against this harm by conferring monopoly privileges on the manufacturers." Id. at 695-96.

influencing the judgment of an existing or prospective client in connection with a project in which the architect is interested." 18/ This prohibition is likely to have anticompetitive effects by reducing the ability of new entrants into the architectural services market to compete with incumbent firms.

New entrants into competitive markets for professional services often must engage in promotional activities to bring themselves to the attention of prospective clients. A new entrant into the architectural services market may be able to compete with more established firms by submitting to a potential client a preliminary design for a project on which the entrant is bidding. This service reduces the client's uncertainty as to the quality of the services offered by the new entrant and allows the new entrant to compete more effectively with incumbents in the market. A prohibition on the "donation" of services in order to secure a project increases the client's cost of uncertainty associated with the hiring of a new and untested entrant and thereby reduces the ability of new entrants to compete. The prohibition could also reduce competition in the quality of design by hampering a prospective client's ability to compare the design ideas of competing architects.

III. Conclusion

Regulation 11-17, as interpreted by the Board of Architectural Examiners, is likely to impede competition in the market for architectural services in South Carolina. Prohibitions on participation in competitive bidding similar to the one contained in Regulation 11-17 have been held to violate the federal antitrust laws because they injure consumers. The Council should consider the costs imposed by the regulation on South Carolina consumers in light of the questionable benefits offered by the regulation.

Sincerely,


Jeffrey I. Zuckerman
Director

18/ Administrative Interpretation, supra note 7. The interpretation permits architects to donate services solely for altruistic reasons.