No. S203124

IN THE SUPREME COURT OF CALIFORNIA

JERRY BEEMAN and PHARMACY SERVICES et al.,

Plaintiffs-Respondents,

v.

ANTHEM PRESCRIPTION MANAGEMENT et al.,

Defendants-Appellants.

Question Certified from the En Banc United States Court of Appeals for the Ninth Circuit, Case Nos. 07-56692, 07-56693

APPELLANTS' CONSOLIDATED OPENING BRIEF

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STATEMENT OF THE ISSUE PRESENTED

The question certified by the United States Court of Appeals for the Ninth Circuit for this Court's review is: Does California Civil Code section 2527 compel speech in violation of article I, section 2 of the California Constitution?

INTRODUCTION

Civil Code section 2527 requires prescription drug claims processors to compile, summarize, and disseminate information on pharmaceutical fees that directly harms their interests by supporting pharmacists in negotiations over rates of reimbursement for pharmaceuticals and in the public debate over reimbursement rate regulation.

A divided Ninth Circuit panel held that the statute is not entitled to *any* constitutional scrutiny under either the California Constitution's free speech clause or the First Amendment, because the speech compelled is "fact based" and does not require claims processors "to advocate any position or 'endorse' any 'pledge or motto' that is contrary to their beliefs." But there is no exception to the free speech protections of either the California or federal Constitution for "fact-based" speech; indeed, the United States

Supreme Court held recently that the "First Amendment protects even dry information, devoid of advocacy, political relevance, or artistic expression." (*Sorrell v. IMS Health Inc.* (2011) 131 S.Ct. 2653, 2666–2667 (*Sorrell*).) And every California appellate court to address the question has held that section 2527 violates the California Constitution's free speech clause. (See *ARP Pharmacy Services, Inc. v. Gallagher Bassett Services, Inc.* (2006) 138 Cal.App.4th 1307 (*ARP*); accord *A.A.M. Health Group, Inc. v. Argus Health Systems, Inc.* (Cal. Ct. App. Feb. 28, 2007, No. B183468) 2007 WL 602968 (*A.A.M.*); *Bradley v. First Health Services Corp.* (Cal. Ct. App. Feb. 28, 2007, No. B185672) 2007 WL 602969, review den. June 13, 2007 (*Bradley*).)

These decisions recognized (and the Ninth Circuit majority ignored) that the text of California's free speech clause is indisputably broader than the First Amendment's, as it protects speech "on *all* subjects." (Cal. Const., art. I, § 2, subd. (b), italics added.) As a result, and as this Court has held, "[t]he state Constitution's free speech provision is at least as broad as *and in some ways is broader* than the comparable provision of the federal Constitution's First Amendment." (*Kasky v. Nike* (2002) 27 Cal.4th 939, 958–959

(*Kasky*), italics added, citations omitted.) Thus, apart from section 2527's invalidity under the First Amendment, the statute violates California's free speech clause.

Because section 2527 compels the content of speech, it is subject to strict scrutiny, which means that the statute is *presumptively invalid.* Plaintiffs can overcome this presumption only by showing that the government has a "compelling interest" the statute is "narrowly tailored" to promote. But the government's purported interest in buttressing pharmacists' strength in negotiating reimbursement rates is not "compelling." Nor are the statute's means "narrowly tailored"—the information at issue could be gathered by the government or published by the pharmacists (who already have the information). There is no basis for compelling *claims processors* to gather, summarize, and transmit information that is against their interests and could be used to harm them in the public debate over reimbursement rate regulation.

Section 2527 may not be construed as regulating "commercial" speech warranting lesser constitutional scrutiny, because section 2527 does not regulate a commercial transaction or speech that is inherently or even potentially deceptive. But even under intermediate scrutiny,

the statute should still be invalidated because it is not premised on a substantial government interest, but rather on a stated "hope" that dissemination of fee studies would, over time, increase the rates paid to retail pharmacies. Section 2527 thus fails any level of "heightened scrutiny," regardless of whether the speech compelled is deemed "commercial."

The California courts of appeal have uniformly and correctly held that section 2527 compels speech and therefore violates the free speech clause of the California Constitution. This Court should so hold as well.

STATEMENT OF THE CASE

Plaintiffs filed a putative class action complaint in 2002 and a second complaint in 2004, alleging that defendants violated Civil Code section 2527, subdivision (c), by failing to transmit the studies required by the statute. (See *Beeman v. TDI Managed Care Services, Inc.* (2006) 449 F.3d 1035, 1039 (*Beeman I*).) Defendants moved for judgment on the pleadings, arguing that section 2527 unconstitutionally compels speech in violation of both the California and federal Constitutions. (*Beeman v. Anthem Prescription Management, LLC* (9th Cir. 2011) 652 F.3d 1085, 1089 (*Beeman II*).)

The district court denied the motion, and certified its decision for interlocutory review, which the Ninth Circuit granted. (*Id.* at p. 1092.)

The Ninth Circuit then affirmed in a split decision. (*Beeman II*, *supra*, 652 F.3d at p. 1107.) Defendants petitioned for rehearing en banc, which the Ninth Circuit granted. (*Beeman v. Anthem Prescription Management, LLC* (9th Cir. 2011) 661 F.3d 1199, 1201.) The en banc court then certified the question presented here for this Court's review. (*Beeman v. Anthem Prescription Management, LLC* (9th Cir. June 6, 2012) 2012 WL 2775005, at *1–2 [en banc].) On July 18, 2012, this Court agreed to decide the certified question.

SUMMARY OF KEY FACTS AND PROCEDURAL HISTORY

I. Factual Background

A. The Relationship Between Pharmacy Benefit Managers, Payors, and Pharmacies

Defendants-appellants are current or former pharmacy benefit managers ("PBMs"), which contract with third-party payors or health plan administrators such as insurers, HMOs, governmental entities, and employers to facilitate cost-effective delivery of prescription drugs to health plan members or other persons to whom the third-party payors provide prescription drug benefits. (Ninth Circuit

Excerpts of Record "ER" 163–164; see *Beeman II*, *supra*, 652 F.3d at p. 1090.)[1] PBMs assist third-party payors and health plan administrators by, among other things, determining claims for prescription drug benefits submitted by pharmacies, thereby acting as intermediaries between third-party payors and pharmacies. (ER157–158, 179; see *Beeman II*, *supra*, 652 F.3d at p. 1090.)

PBMs may create networks of retail pharmacies that agree to accept certain reimbursement rates when they fill prescriptions for health plan members. Network reimbursements generally are lower than what pharmacies would charge uninsured, cash-paying customers. Such networks keep costs down for health plan sponsors, and being part of a network helps a pharmacy expand its customer base, thereby increasing its sales volume for both prescription drugs and other items. (See *Beeman II*, *supra*, 652 F.3d at p. 1090.)

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[1] The statutory scheme applies to "prescription drug claims processors," a term defined in the statute and subject to several exceptions. (Civ. Code, § 2527, subd. (b).) The PBM-defendants maintain they are not "prescription drug claims processors," and reserve their objections, but the trial court has not reached that issue, and it therefore is not ripe in this appeal. (See *Beeman v. Anthem Prescription Management, LLC* (9th Cir. June 6, 2012) 2012 WL 2775005, at *2, fn. 1 [en banc].)

Plaintiffs-respondents are pharmacists who allege that they own independent retail pharmacies licensed in California. (ER152–153, 177–178.)

B. Civil Code Section 2527's Requirements and Section 2528's Civil Penalty Scheme

Section 2527 of the Civil Code requires that every prescription drug claims processor in California conduct or obtain "the results of a study or studies which identifies the fees … of all, or of a statistically significant sample, of California pharmacies, for pharmaceutical dispensing services to private consumers ...." (Civ. Code, § 2527, subd. (c).) The fees "shall be computed by reviewing a sample of the pharmacy's usual charges for a random or other representative sample of commonly prescribed drug products, subtracting the average wholesale price of drug ingredients, and averaging the resulting fees by dividing the aggregate of the fees by the number of prescriptions reviewed." (*Ibid.*)

Along with the raw data, the report "shall include a preface, an explanatory summary of the results and findings including a comparison of the fees of California pharmacies by setting forth the mean fee and standard deviation, the range of fees and fee percentiles

(10th, 20th, 30th, 40th, 50th, 60th, 70th, 80th, 90th)." (Civ. Code, § 2527, subd. (c).)

The information described "shall be transmitted by certified mail by each prescription drug claims processor to the chief executive officer or designee, of each client for whom it performs claims processing services." (Civ. Code, § 2527, subd. (d).) These transmissions must occur every 24 months. (*Ibid.*)

In the event a claims processor does not comply with the commands of section 2527, it may be subject to a civil lawsuit under section 2528, which gives "[a]ny owner of a licensed California pharmacy ... standing to bring an action seeking a civil remedy." (Civ. Code, § 2527, subd. (c).) Plaintiffs in such suits may be entitled to "statutory damages of not less than one thousand dollars ($1,000) or more than ten thousand dollars ($10,000) depending on the severity or gravity of the violation," as well as "reasonable attorney's fees and costs, declaratory and injunctive relief, and any other relief which the court deems proper." (*Id.*, § 2528.)[2]

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[2] Section 2527 does not define a "violation," but plaintiffs have asserted that a violation occurs *each time a prescription is processed.* (ER60, 152–153.) They therefore seek aggregated penalties on behalf of 2,200 California pharmacies for "multiple" alleged "violations," which they claim warrant several *billion*

C. Pharmacists Lobbied for the Enactment of Section 2527 to Increase Prescription Reimbursement Rates

The legislative effort that resulted in section 2527 began in 1981, when "the California Pharmacists Association introduced a bill which would require PBM reimbursements at customary charges made by pharmacies rather than the rates unilaterally set by PBMs." (*Beeman I, supra*, 449 F.3d at p. 1038.) Assemblyman Lancaster, who carried Assembly Bill AB2044 for the Association, described the bill as a "proposed remedy" to a system whereby insurers "pay pharmacists Medi-Cal rates—or less." (ER134.)[3]

Assembly Committee staff prepared and distributed a background paper about the bill for use by committee members in connection with public hearings held on October 27, 1981. That paper described the proposed legislation and its sponsors:

> Assembly Bill 2044 is sponsored by the California Pharmacists Association. The membership of the association consists of individual pharmacists....

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dollars in penalties. (ER159, 167, 181, 189.) The potential for arbitrary and oppressive punishment from the aggregation of penalties in this way raises a whole host of constitutional problems that would need to be addressed if the statute were upheld. (See, e.g., *Hale v. Morgan* (1978) 22 Cal.3d 388, 397–398.)

[3] The relevant legislative history is part of the record on appeal. Cited excerpts are compiled at ER129–148.

> The association believes that the present system of reimbursement, which provides for a fixed fee plus actual cost of ingredients, rather than the usual and customary charge, is inequitable. A pharmacist is placed in the position of either signing up as a participant under the contract or facing a serious loss of volume of prescription business....
>
> The goal of the sponsor of the bill is to achieve by legislation a reimbursement policy which it believes is equitable, a goal members cannot achieve through collective bargaining and have not achieved through the courts. The goal of third-party administrators and payors, on the other hand, is to keep costs as low as possible, a goal in direct conflict with that of the pharmacists.

(ER141–142.)

Opposition to the bill developed, most notably from various California executive branch agencies. For example, the Department of Insurance opposed the bill, concluding: "The end result of the bill, we think, [would] be to increase premiums to all insureds, with *pharmacies* being the ultimate beneficiaries. We think it is not in the best interest of the insurance-buying public." (ER144, italics added.)

The initial price-setting bill never emerged from legislative committee. Instead, AB2044 was amended in several respects, most notably by eliminating the price-setting feature and substituting the requirements now at issue—compelling the claims processors to

disseminate reports on the fees that California pharmacies charge private consumers.

The proponents of the new provisions hoped that by forcing claims processors to report the fees being paid to pharmacies, the pharmacies would be able to use that data in negotiating for higher reimbursement rates from third-party payors. In describing these new provisions, staff to the Assembly Committee on Finance, Insurance, and Commerce explained:

> It is the position of the sponsor of the bill that a pharmacist should be reimbursed by a third party payor according to the pharmacist's usual and customary charge, and that instead, a pharmacist is presently reimbursed according to the Medi-Cal reimbursement. The purpose of this bill is to require claims processors to present objective data on the range and percentiles of usual and customary charges of pharmacists in the hope that at a time in the future this information will become the basis for reimbursement.

(*ARP*, *supra*, 138 Cal.App.4th at p. 1319 [quoting legislative history]; ER146.) The legislative purpose of the final version of AB2044 was:

> to encourage insurers to pay pharmacists a fair rate for drug dispensing services. Section 2527 sought to accomplish this goal by requiring drug claims processors to provide statistical surveys of the customary charges for dispensing services for private-pay consumers.

(*ARP*, at p. 1320.)

The pharmacists also have not lost hope on their original effort to pass legislation mandating more "fair" and "equitable" rates of reimbursement. They have contended that dissemination of the studies under section 2527 could inspire "lobby[ing] for legislative intervention should that be necessary" if higher, negotiated reimbursement rates are not achieved. (*Beeman I*, *supra*, 449 F.3d at p. 1039.)

II. Procedural History

These cases have had a long and complex path through the state and federal courts.

In 2002, plaintiffs filed a putative class action complaint in the United States District Court for the Central District of California alleging claims for: (1) violation of section 2527 for failure to conduct fee studies mandated by section 2527, subdivision (c); (2) unlawful, unfair, and fraudulent business acts in violation of California Business and Professions Code section 17200, predicated on alleged violations of section 2527; and (3) declaratory relief and unjust enrichment, also predicated on alleged violations of section 2527. (ER189–193.) In 2004, plaintiffs filed a second federal court complaint alleging virtually identical claims against a second group of

defendants on behalf of a putative class of pharmacists. (ER167–171.)

Defendants first moved to dismiss the claims due to plaintiffs' lack of standing under Article III of the United States Constitution. (*Beeman I*, *supra*, 449 F.3d at p. 1038.) The district court granted defendants' motion, but the Ninth Circuit reversed that decision and remanded the case, without ruling on the merits of defendants' free speech challenge. (*Id.* at p. 1040.)[4]

On remand, defendants filed motions for judgment on the pleadings, challenging the constitutionality of section 2527. The defendants relied on "three California state appellate court decisions, including *Bradley*, all of which held that § 2527 violates the California Constitution's free speech provision." (*Beeman II*, *supra*, 652 F.3d at p. 1092; see, e.g., *ARP*, *supra*, 138 Cal.App.4th at p. 1322 ["We conclude that the reporting requirement in section 2527 and the

---

[4] In the meantime, three of the five plaintiffs (represented by the same counsel here) filed suit against most of the *Beeman* defendants in Los Angeles County Superior Court, asserting the same three causes of action predicated on supposed violations of section 2527. (See *Bradley*, *supra*, 2007 WL 602969, at *1.) The trial court in *Bradley* declared section 2527 unconstitutional under state law and dismissed the action on demurrers, the court of appeal affirmed (*ibid.*), and this Court denied review on June 13, 2007.

related penalty and enforcement provisions in section 2528 violate the free speech provision of the California Constitution"]; accord *A.A.M.*, *supra*, 2007 WL 602968, at *2; *Bradley*, *supra*, 2007 WL 602969, at *2.)[5]

The district court denied defendants' motions, holding that section 2527 "does not violate the free speech rights of PBMs under either the federal or California Constitution." (ER118.) Although *ARP* involved the same claims and was directly on point (138 Cal.App.4th at p. 1322), the court rejected that decision, relying heavily on its analysis of *Rumsfeld v. Forum for Academic & Institutional Rights, Inc.* (2006) 547 U.S. 47 (*FAIR*), which it interpreted as "undermin[ing] *ARP*'s key holdings" (ER97). The court distinguished another United States Supreme Court decision relied upon by *ARP* (*Riley v. Nat. Federation of the Blind* (1988) 487 U.S. 781 (*Riley*)) on the ground that *Riley* protects only certain kinds of "core speech," such as political or ideological opinions (ER104, 108–109). In the district court's view, "the U.S. Supreme Court has

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[5] Appellants acknowledge that because the *Bradley* and *A.A.M.* decisions are unpublished they cannot be relied on as authority. (See Cal. Rules of Court, rule 8.1115(a).) The cases are relevant to the procedural history and basis for the Ninth Circuit's decision.

declined to subject statutes to any discernible level of constitutional scrutiny after determining that they involve no 'compelled recitation of a message containing an affirmation of belief.'" (ER114, citing, *inter alia*, *FAIR*, *supra*, 547 U.S. at pp. 62–65.)[6]

The Ninth Circuit affirmed in a split decision. The two-judge majority held that it was not required by *Erie Railway Co. v. Tomkins* (1938) 304 U.S. 64 to follow the California Court of Appeal's decisions in *ARP*, *A.A.M.*, and *Bradley*, because the panel majority disagreed with those courts' interpretations of the First Amendment. (*Beeman II*, *supra*, 652 F.3d at p. 1107.) The panel majority, like the district court, rejected *ARP*'s application of *FAIR* and *Riley*. The panel determined that under *FAIR*, the First Amendment is implicated only with respect to speech such as "Government-mandated pledge[s] or motto[s]," which the report required by section 2527 is not. (*Id.* at p. 1100.) And the court held that *Riley* applies only to reporting

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[6] The district court also separately granted in part defendants' motions for summary judgment based on *res judicata*. (ER36.) The court ruled that the three plaintiffs in *Bradley* were precluded by the final judgment in that state action from pursuing their overlapping claims in the federal case. However, the court refused to apply *res judicata* to the plaintiffs in the federal cases who were not also parties in *Bradley*. (*Ibid.*) Those rulings are not at issue in this appeal.

requirements that chill speech otherwise protectable under the court's view of *FAIR*. (*Id.* at pp. 1099–1100.)

Judge Wardlaw dissented from the panel's decision, noting that "[t]he majority disregard[ed] not one but three intermediate California appellate decisions holding that California Civil Code § 2527 violates Article I, section 2 of the California Constitution." (*Beeman II*, *supra*, 652 F.3d at p. 1107 [dis. opn. of Wardlaw, J.].) She also rejected the majority's proffered distinctions of *FAIR* and *Riley*, and explained that *Sorrell v. IMS Health Inc.*, *supra*, 131 S.Ct. 2653, which the majority addressed only once in a footnote, was directly on point, as it held that the "First Amendment protects even dry information, devoid of advocacy, political relevance, or artistic expression." (*Beeman II*, at p. 1111, quoting *Sorrell*, at pp. 2666–2667.)

The en banc Ninth Circuit vacated the panel decision and ordered rehearing. (*Beeman v. Anthem Prescription Management, LLC* (9th Cir. 2011) 661 F.3d 1199, 1201.) It then certified the question presented here for this Court's review: "whether section 2527 is subject to some level of constitutional review because it compels speech in violation of California's free speech clause and the First Amendment." (*Beeman v. Anthem Prescription Management,*

LLC (9th Cir. June 6, 2012) 2012 WL 2775005, at *5 [en banc], citing *Sorrell*, *supra*, 131 S.Ct. at p. 2667 ["This Court has held that the creation and dissemination of information are speech within the meaning of the First Amendment"].)

DISCUSSION

I. Section 2527 Compels Speech

A. California's Free Speech Clause Covers Both the Right to Speak and the Right *Not* to Speak

Article I, section 2 of the California Constitution guarantees that "[e]very person may freely speak, write, and publish his or her sentiments on all subjects." This Court has ruled consistently that because the "right" to "speak" guaranteed by the free speech clause "results from what a speaker chooses to say and *what he chooses not to say*, the right in question comprises both a right to speak freely *and also a right to refrain from doing so at all*." (*Gerawan Farming, Inc. v. Lyons* (2000) 24 Cal.4th 468, 491 (*Gerawan*), italics added; see also *Wooley v. Maynard* (1977) 430 U.S. 705, 714 (*Wooley*).) This includes requiring persons or entities to express a message with which they disagree or subsidize a message they do not wish to fund—even if the speaker is not required to endorse the content. (*Gerawan*, at p. 491; see also *Johanns v. Livestock Marketing Assn.* (2005) 544 U.S.

550, 557; *Pacific Gas & Electric Co. v. Public Utilities Com. of Cal.* (1986) 475 U.S. 1, 2 (*Pacific Gas*).)

Every state appellate court to consider the question has held that section 2527 violates California's free speech clause. (See *Beeman II*, *supra*, 652 F.3d at p. 1093, citing *ARP*, *supra*, 138 Cal.App.4th at p. 1313; *A.A.M.*, *supra*, 2007 WL 602968, at *5; *Bradley*, *supra*, 2007 WL 602969, at *2.) The leading case, *ARP Pharmacy Services, Inc. v. Gallagher Bassett Services, Inc.*, involved a claim by a licensed pharmacy against a group of drug claims processors for violations of section 2527—virtually identical to the claim presented here. The court in *ARP* held that "the reporting requirement in section 2527 and the related penalty and enforcement provisions in section 2528 violate the free speech provision of the California Constitution." (*ARP*, at p. 1322.)

Writing for a unanimous panel, Justice Epstein in *ARP* relied on this Court's statement in *Gerawan* (quoted above) that the free speech clause is implicated when the government "compel[s one] to say what he otherwise would not say." (*ARP*, *supra*, 138 Cal.App.4th at p. 1314, quoting *Gerawan*, *supra*, 24 Cal.4th at p. 491.) The relevant question in a compelled speech case is "whether the regulation

requires transmission of specific content," which section 2527 indisputably does: It "requires drug claims processors to transmit specific information—drug processing costs—that the processors do not wish to send to their clients." (*ARP*, at p. 1315.) And "[t]he fact that it is essentially statistical information does not make it less entitled to First Amendment scrutiny." (*Ibid.*, citing *Riley*, *supra*, 487 U.S. at pp. 782–783.)

This Court has not had occasion to address the doctrine of compelled speech in the context of a statute such as section 2527 that requires a party to compile, summarize, and distribute factual data. But the United States Supreme Court reaffirmed recently in *Sorrell*—with respect to a statute very similar to section 2527—that "the creation and dissemination of [factual, prescriber-identifying] information are speech within the meaning of the First Amendment." (131 S.Ct. at p. 2667.) This Court regularly consults the Supreme Court's First Amendment jurisprudence when interpreting California's free speech clause (see, e.g., *Gerawan*, *supra*, 24 Cal.4th

at p. 489), and thus *Sorrell* is particularly instructive on the scope of article 1, section 2.[7]

Section 2527 and the Vermont statute at issue in *Sorrell* are remarkably similar. As discussed above, section 2527 requires claims processors to collect data regarding fees, package and summarize that data, and publish it. (Civ. Code, § 2527, subds. (c)–(d).) The Vermont statute also targets pharmacies, but *restricts* pharmacies from selling, disclosing, or using pharmacy records that reveal the prescribing practices of doctors. (Vt. Stat. Ann., tit. 18, § 4631.) As Judge Wardlaw remarked, "[t]he Vermont law in [*Sorrell*] is the flip side of California's § 2527; they involve similar speech that Vermont prohibits and California compels." (*Beeman II*, *supra*, 652 F.3d at p. 1111 [dis. opn. of Wardlaw, J.].)

The statutes share the same general purpose as well. The genesis of the Vermont statute was pharmacies' sale of prescribing information to data miners who would then package the information and sell it to pharmaceutical companies who used the information for marketing. The Vermont statute was enacted to protect smaller drug

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[7] *Sorrell* was decided only a few weeks before the Ninth Circuit panel issued its decision.

companies, who could not afford the "expensive pharmaceutical marketing campaigns to doctors." (*Sorrell*, *supra*, 131 S.Ct. at p. 2661.) Similarly, as discussed above, the California legislature enacted section 2527 to provide pharmacists with leverage in negotiating reimbursement rates with claims processors. (See *id.* at p. 2660; pp. 9–12, *ante*.) In both cases, the statute either restricts or compels the disclosure of "facts" in order to confer a benefit on one group of businesses to the detriment of another.

As a result, it follows from *Sorrell*'s holding that "the creation and dissemination of [factual, prescriber-identifying] information are speech within the meaning of the First Amendment" (131 S.Ct. at p. 2667) that the reports that section 2527 requires claims processors to publish are also "speech" covered by the First Amendment (and therefore California's free speech clause). The transmission of the reports mandated by section 2527 is undeniably "speech," as even the Ninth Circuit majority acknowledged. (*Beeman II*, *supra*, 652 F.3d at p. 1102, fn. 19 ["Consistent with the cases cited by the Dissent, we readily agree that the transmission of the pricing survey results constitutes speech"].) And the Court in *Sorrell* rejected any exception to the First Amendment for the sort of "factual" information covered

by section 2527: "Facts, after all, are the beginning point for much of the speech that is most essential to advance human knowledge and to conduct human affairs. There is thus a strong argument that prescriber-identifying information is speech for First Amendment purposes." (131 S.Ct. at p. 2666.)

The United States Supreme Court has frequently reiterated "the principle that freedom of speech prohibits the government from telling people what they must say." (*FAIR*, *supra*, 547 U.S. at p. 61.) The Court has consistently eschewed any distinction between laws or regulations *prohibiting* speech and those that *compel* speech. (See, e.g., *Pacific Gas*, *supra*, 475 U.S. at p. 11 ["*all speech* inherently involves choices of what to say *and what to leave unsaid*"], italics added; *Wooley*, *supra*, 430 U.S. at p. 714 ["The right to speak and the right to refrain from speaking are complementary components of the broader concept of 'individual freedom of mind'"].) And it has applied this doctrine even to the sort of statistical data that section 2527 requires the claims processors to disseminate. (See, e.g., *Sorrell*, *supra*, 131 S.Ct. at p. 2666; *Riley*, *supra*, 487 U.S. at p. 797.)

For example, in *Riley*, the Court struck down a statute that compelled professional charitable fundraisers to inform donors of the

percentage of charitable contributions used for charitable and administrative purposes. (487 U.S. at p. 788.) The Court explained that there is no constitutional difference between "compelled statements of opinion" and "compelled statements of fact" because anything that "mandat[es] speech that a speaker would not otherwise make necessarily alters the content of the speech." (*Id.* at p. 798; see also *ibid.* [referring to the "*constitutional equivalence* of compelled speech and compelled silence"], italics added.) Accordingly, a statute that compels an individual to speak—even if the compelled speech is simply facts and data (as in *Riley* and *Sorrell*)—is subject to heightened scrutiny and is "presumptively unconstitutional." (*R.A.V. v. City of St. Paul* (1992) 505 U.S. 377, 382 (*R.A.V.*).)

Even if there were some room for disagreement regarding the scope of the First Amendment and whether its protections extend to the speech compelled by section 2527, California's free speech clause nevertheless would "enjoy[] existence and force independent of the First Amendment." (*Gerawan*, *supra*, 24 Cal.4th at p. 489.) Indeed, "[t]he state Constitution's free speech provision is at least as broad as *and in some ways is broader* than the comparable provision of the federal Constitution's First Amendment." (*Kasky*, *supra*, 27 Cal.4th

at pp. 958–959, italics added; see also *L.A. Alliance for Survival v. City of L.A.* (2000) 22 Cal.4th 352, 366 ["This court, and the California Courts of Appeal, likewise have indicated that the California liberty of speech clause is broader and more protective than the free speech clause of the First Amendment"].)

For example, whereas the text of the First Amendment simply places a restriction on the legislature ("Congress shall make no law ... abridging the freedom of speech"), article I, section 2, subdivision (a) grants every individual and entity the "right" to "freely speak, write and publish his or her sentiments *on all subjects*," and mandates that a "law may not *restrain or abridge* liberty of speech or press." (Italics added.) The free speech clause further provides that the press cannot be punished "for *refusing to disclose* the source of any information." (Cal. Const., art. I, § 2, subd. (b), italics added.)

California's free speech clause is thus more expansive than the First Amendment both in the types of speech it covers ("on *all subjects*") and its sensitivity to burdens on that speech ("law may not *restrain or* abridge"). This Court articulated the principle well in *Gerawan*:

> [A]rticle I's right to freedom of speech, unlike the First Amendment's, is unlimited in scope. Whereas the First

> Amendment does not embrace all subjects, article I does indeed do so, *in ipsissimis verbis*: "Every person may freely speak, write and publish his or her sentiments *on all subjects* ...."

(24 Cal.4th at p. 493; see also *Robins v. Pruneyard Shopping Center* (1979) 23 Cal.3d 899, 908 ["Though the framers could have adopted the words of the federal Bill of Rights they chose not to do so"].) In other words, whereas the First Amendment, by its terms, limits only *government* intrusion on speech, California's free speech clause expansively guarantees a "right" (a term not used in the First Amendment) against any restraint or abridgment of speech "on all subjects." (*Wilson v. Superior Court* (1975) 13 Cal.3d 652, 658 ["A protective provision more definitive and inclusive than the First Amendment is contained in our state constitutional guarantee of the right of free speech and press"].)

The statistical reports and summaries that claims processors are compelled to disseminate are "speech" subject to heightened constitutional scrutiny under the First Amendment, and because California's free speech clause offers even broader protection, section 2527 triggers heightened review under that standard as well. (*ARP*, *supra*, 138 Cal.App.4th at pp. 1314–1315 ["section 2527, which requires drug claims processors to obtain and transmit drug processing

cost reports to its clients, is properly classified as 'true' compelled speech"].)

B. The California Courts Have Properly Applied the First Amendment Caselaw, Which Requires Heightened Scrutiny Where the Government Compels Dissemination of Factual and Statistical Data

ARP discussed and analyzed First Amendment precedents as part of its determination that California's free speech clause requires heightened scrutiny of section 2527. (*ARP*, *supra*, 138 Cal.App.4th at pp. 1314–1316.) The court of appeal focused in particular on *Riley*, which involved an "analogous reporting requirement of statistical information." (*Id.* at p. 1315.) Justice Epstein reiterated the Supreme Court's explanation that "[m]andating speech that a speaker would not otherwise make necessarily alters the content of the speech." (*Ibid.*, citing *Riley*, *supra*, 487 U.S. at p. 795.) *ARP* held that "[f]or the same reasons, section 2527 is a content-based regulation of speech." (*Ibid.*)

The divided Ninth Circuit panel, however, disagreed with *ARP*'s analysis of the federal caselaw, holding that *FAIR* and *Riley* drew a distinction between compelled speech that warrants First Amendment protection and compelled speech that does not. (*Beeman*

II, *supra*, 652 F.3d at p. 1098.)[8] But as discussed below, the panel majority's restrictive reading of the United States Supreme Court's First Amendment decisions was both erroneous and incomplete (the majority mentioned *Sorrell* only once, in a footnote).

The primary basis for the Ninth Circuit's decision that the speech compelled by section 2527 is not constitutionally protected was the panel majority's conclusion that *FAIR* "makes clear that not all fact-based disclosure requirements are subject to First Amendment scrutiny." (*Beeman II*, *supra*, 652 F.3d at p. 1099.) The court held that the First Amendment is only implicated if the law at issue "affect[s] the content of the message or speech by forcing the speaker to endorse a particular viewpoint or by chilling or burdening a message that the speaker would otherwise choose to make." (*Id.* at p. 1100.) And because section 2527 simply requires the reporting of data and does not require claims processors to "endorse" any "pledge or motto" that is contrary to their beliefs, the panel majority held that the First Amendment provides no protection whatsoever. (*Ibid.*)

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[8] Because the Ninth Circuit granted rehearing en banc, the panel's decision has been vacated. (*Beeman v. Anthem Prescription Management, LLC* (9th Cir. 2011) 661 F.3d 1199, 1201.)

As an initial matter, as the panel majority acknowledged and the dissent reiterated, section 2527 does *not* simply require the reporting of data—it also requires "a preface, an explanatory summary of the results and findings including a comparison of the fees of California pharmacies by setting forth the mean fee and standard deviation, the range of fees and fee percentiles ...." (Civ. Code, § 2527, subd. (c); see also *Beeman II*, *supra*, 652 F.3d at p. 1100, fn. 13 [quoting subdivision (c)]; *id.* at p. 1108 [dis. opn. of Wardlaw, J.] ["The statute requires drug claims processors to undertake or obtain studies about pharmacy pricing, summarize the results, and transmit the material to their clients"].) It is therefore inaccurate to say that the claims processors must only turn over data they have already collected. If that data is not prepared, claims processors are required to *generate* it, and then they must *summarize* and *compare* the data. (Civ. Code, § 2527, subd. (c).)

Moreover, *FAIR* did not hold that only "political messages," such as the "Government-mandated pledge or motto" at issue in *Wooley* and *West Virginia State Board of Education v. Barnette* (1943) 319 U.S. 624, are entitled to First Amendment protection—the Court's holding was that the statute in *FAIR* did not regulate "speech"

at all. The issue in *FAIR* was whether the Solomon Amendment, which conditioned funding to universities on the schools granting access to military recruiters, compelled the universities to endorse the military's "don't ask don't tell" policy. The Court held that the Solomon Amendment did no such thing—it required the universities to treat the military the same as other employers that recruited on campus—but it did not compel any sort of speech. Although offering recruiting assistance to military recruiters "often includes elements of speech," because "schools may send e-mails or post notices on bulletin boards on an employer's behalf," there was no evidence that this occurred with respect to the parties in the case. (*FAIR*, *supra*, 547 U.S. at pp. 61–62.) Indeed, "[t]he Solomon Amendment ... d[id] not dictate the content of the speech at all, which is only 'compelled' if, and to the extent, the school provides such speech for other recruiters." (*Id.* at p. 62.)[9] Here, by contrast, section 2527 compels the collection, summary, and dissemination of information.

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[9] (See also *FAIR*, *supra*, 547 U.S. at p. 60 ["the Solomon Amendment neither limits what law schools may say nor requires them to say *anything*"]; *ibid.* ["As a general matter, the [statute] regulates conduct, not speech"]; *id.* at p. 64 ["accommodating the military's message does not affect the law schools' speech, because the schools are not speaking when they host interviews and recruiting receptions"].)

The Supreme Court further clarified this distinction in *Sorrell*, in evaluating a law similar to section 2527, citing *FAIR* for the proposition that "the First Amendment does not prevent restrictions directed at commerce or conduct from imposing incidental burdens on speech." (131 S.Ct. at pp. 2664–2665; see also *Nevada Com. on Ethics v. Carrigan* (2011) 131 S.Ct. 2343, 2350 [citing *FAIR* for the same proposition]; *Entertainment Software Assn. v. Blagojevich* (7th Cir. 2006) 469 F.3d 641, 653 [in *FAIR*, "the Court concluded that there was no expressive activity threatened by simply allowing the military equal recruiting access as other employers"].)

The holding in *FAIR* has no applicability here, because the core purpose and effect of section 2527 is the *transmission* of the data, which the statute was enacted in order to facilitate. That the information must be gathered in order for it to be transmitted does not change the statute into a regulation of conduct. (See, e.g., *Sorrell*, *supra*, 131 S.Ct. at p. 2667 [attempt to distinguish "the actual performance of the pricing studies" from "the transmission of their results" is unavailing, as both "the creation and dissemination of information are speech within the meaning of the First Amendment"]; *Bartnicki v. Vopper* (2001) 532 U.S. 514, 527 ["It is true that the

delivery of a tape recording might be regarded as conduct, but given that the purpose of such a delivery is to provide the recipient with the text of recorded statements, it is like the delivery of a handbill or a pamphlet, and as such, it is the kind of 'speech' that the First Amendment protects"].) As Judge Wardlaw explained in dissent, "[a]ll government compulsion of speech requires some conduct incident to the expression," but that does not insulate the speech regulation from constitutional scrutiny. (*Beeman II*, *supra*, 652 F.3d at p. 1109, fn. 2 [dis. opn. of Wardlaw, J.].)

The Ninth Circuit majority repeatedly relied upon language from *FAIR* referring to a "Government-mandated pledge or motto," and held that *FAIR* limited the First Amendment's protections to only such speech. But the Supreme Court in *FAIR* distinguished compelled pledges and mottos precisely because such speech is *compelled*, whereas the Solomon Amendment *did not compel any speech*. *FAIR* did not hold or suggest that compelled speech must be akin to a "pledge" or "motto" in order to warrant First Amendment protection. Indeed, the Court acknowledged that "compelled statements of fact"—such as "'The U.S. Army recruiter will meet interested students in Room 123 at 11 a.m.'"—"like compelled statements of

opinion, are subject to First Amendment scrutiny." (*FAIR*, *supra*, 547 U.S. at p. 62.)

Numerous other decisions have rejected the "additional step" (*Beeman II*, *supra*, 652 F.3d at p. 1100, fn. 12) the Ninth Circuit grafted onto the compelled speech doctrine, which would only preclude the government from compelling "political messages."[10] Fact-based news reporting is protected under the First Amendment and the California Constitution (see, e.g., *Lafayette Morehouse, Inc. v. Chronicle Publishing Co.* (1995) 37 Cal.App.4th 855, 864), as are numerous other forms of speech that communicate only factual information (see, e.g., *44 Liquormart, Inc. v. Rhode Island* (1996) 517 U.S. 484, 489 [state law prohibiting the advertising of liquor prices];

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[10] (See, e.g., *Hurley v. Irish-Am. Gay, Lesbian & Bisexual Group of Boston* (1995) 515 U.S. 557, 573 ["this general rule, that the speaker has the right to tailor the speech, applies not only to expressions of value, opinion, or endorsement, but equally to statements of fact the speaker would rather avoid"]; *Greater Baltimore Center for Pregnancy Concerns, Inc. v. Mayor & City Council of Baltimore* (4th Cir. 2012) 683 F.3d 539, 552 ["strict scrutiny applies even in cases where the compelled disclosure is limited to factually accurate or non-ideological statements"]; *Axson-Flynn v. Johnson* (10th Cir. 2004) 356 F.3d 1277, 1284, fn. 4 ["the First Amendment's proscription of compelled speech does not turn on the ideological content of the message"; rather, the "constitutional harm—and what the First Amendment prohibits—is being forced to speak rather than to remain silent"].)

Linmark Associates, Inc. v. Willingboro (1977) 431 U.S. 85, 96 ["For Sale" and "Sold" signs in front of houses]; *Va. State Bd. of Pharmacy v. Va. Citizens Consumer Council, Inc.* (1976) 425 U.S. 748, 770 [product price information]). And *Riley* rejected a purported distinction between compelled statements of "fact" and compelled statements of "opinion": "[E]ither form of compulsion burdens protected speech." (*Riley*, *supra*, 487 U.S. at pp. 797–798.) The distinction the panel drew between speech worthy of First Amendment protection and speech that is not was therefore erroneous and this Court should reject it.[11]

Any ambiguity in the *FAIR* decision was resolved in *Sorrell*, which held that the "First Amendment protects *even dry information, devoid of advocacy, political relevance, or artistic expression*," and did not require or suggest that a separate harm to "important" or "worthy" speech was required to trigger heightened review. (131 S.Ct. at pp. 2666–2667, italics added.) Vermont argued that "sales,

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[11] A few categories of speech not relevant here have historically received less protection, such as defamation, obscenity, and "fighting words." (See *Miller v. California* (1973) 415 U.S. 13; *New York Times Co. v. Sullivan* (1964) 376 U.S. 254; *Chaplinsky v. New Hampshire* (1942) 315 U.S. 568.) The "commercial speech" doctrine is addressed in section III.A, *post*.

transfer, and use of prescriber-identifying information are conduct, not speech," but the Court rejected that narrow view of protected speech. (*Id.* at p. 2666.) The Court held that "the creation and dissemination of information are speech within the meaning of the First Amendment," and that facts and data are no less "speech" than political opinions. (*Id.* at p. 2667.)

The Ninth Circuit panel acknowledged that *Riley* struck down a statute compelling the transmittal of objective fact-based information. (*Beeman II*, *supra*, 652 F.3d at pp. 1098–1099 ["under *Riley*, compelled disclosures of fact, like compelled matters of opinion, *may* infringe upon the First Amendment"].) Nonetheless, the panel majority concluded that the decision "turned on the Court's finding that the compelled disclosure at issue had a direct and chilling effect on speech that was otherwise cloaked in First Amendment protection—charitable solicitations." (*Ibid.*) The Supreme Court had long held that the First Amendment protects charitable solicitations (e.g., *Schaumburg v. Citizens for a Better Environment* (1980) 444 U.S. 620, 632), and the panel majority held that it was only because the disclosure rule in *Riley* would have chilled the charitable solicitation speech that the statute was unconstitutional.

As Judge Wardlaw observed in her dissent, the panel majority misread *Riley*, which discussed the effects of the statute on future charitable contributions only in connection with the strict scrutiny analysis. (See *Riley*, *supra*, 487 U.S. at p. 795.) *Riley* did not hold that the speech compelled deserved constitutional protection only because it chilled other, more important speech. (See *Beeman II*, *supra*, 652 F.3d at p. 1110 [dis. op. of Wardlaw, J.] [explaining that the panel majority "confuses the initial inquiry into whether a regulation even implicates the First Amendment with the separate inquiry into whether it survives constitutional scrutiny"].) "In other words, the *Riley* Court held that the particular law compelling speech failed exacting scrutiny because of its chilling effect; it did not hold that a chilling effect is a prerequisite to any First Amendment scrutiny at all." (*Ibid.*)

Whereas it discussed *FAIR* and *Riley* at some length, the Ninth Circuit panel brushed *Sorrell* aside in a footnote, concluding summarily that *Sorrell* dealt with a *restriction* on speech, whereas section 2527 *requires* speech. (*Beeman II*, *supra*, 652 F.3d at p. 1101, fn. 17.) This analysis, however, simply restates an artificial and legally insignificant distinction between restricted and compelled

speech that this Court has squarely rejected. (See, e.g., *Gerawan*, *supra*, 24 Cal.4th at p. 491; see also p. 17, *ante*.) *Riley* also rejected the distinction the panel majority attempted to draw between restrictions on speech and compelled speech:

> North Carolina asserts that, even so, the First Amendment interest in compelled speech is different than the interest in compelled silence; the State accordingly asks that we apply a deferential test to this part of the Act. There is certainly some difference between compelled speech and compelled silence, but in the context of protected speech, the difference is without constitutional significance, for the First Amendment guarantees "freedom of speech," a term necessarily comprising the decision of both what to say and what *not* to say.

(487 U.S. at p. 796.) The Supreme Court has reiterated time after time that compelled speech receives the same constitutional scrutiny as restrictions on speech. (See, e.g., *Pacific Gas*, *supra*, 475 U.S. at pp. 9–11; *Wooley*, *supra*, 430 U.S. at p. 714; *Miami Herald Publishing Co. v. Tornillo* (1979) 418 U.S. 241, 256.) "[I]n the context of protected speech, the difference is without constitutional significance." (*Riley*, at p. 796.)

Thus, there is no meaningful difference between the type of speech restricted in *Sorrell* and the speech compelled by section 2527, and because the "First Amendment protects even dry information,

devoid of advocacy, political relevance, or artistic expression" (*Sorrell*, *supra*, 131 S.Ct. at pp. 2666–2667), the information claims processors are forced to disseminate is protected by the First Amendment and therefore the free speech clause of the California Constitution.

II. Because Section 2527 Is a *Content-Based* Regulation That Compels Speech, It Is Subject to and Fails Strict Scrutiny

Strict scrutiny applies to section 2527's compulsion of speech (*Kasky*, *supra*, 27 Cal.4th at p. 952; *Gerawan*, *supra*, 24 Cal.4th at p. 517), and the statute is therefore "presumptively invalid" (*R.A.V.*, *supra*, 505 U.S. at p. 382; see also *Summit Bank v. Rogers* (2012) 206 Cal.App.4th 669, 691 ["A content-based regulation is presumptively invalid, and is subject to strict scrutiny review"]). Indeed, plaintiffs bear the burden of rebutting the presumption of invalidity (*United States v. Playboy Entertainment Group, Inc.* (2000) 529 U.S. 803, 817), which requires them to establish "that the regulation be narrowly tailored (that is, the least restrictive means) to promote a compelling government interest" (*Kasky*, at p. 952). As discussed below, the statute plainly fails this standard.

First, section 2527 is a content-based speech regulation because it mandates discussion of a specific subject matter and was intended

specifically to "impact" the recipients of the speech. (*Boos v. Barry* (1988) 485 U.S. 312, 321.) The reports required by section 2527 are not "'unconcerned with the literal content of the spoken or written words'" (*Glendale Associates, Ltd. v. NLRB* (9th Cir. 2003) 347 F.3d 1145, 1155); they compel a specific type of speech and require that the speech be directed at a particular audience.

Dissemination of the reports plainly amounts to "impermissibly requir[ing] appellant[s] to associate with speech with which [they] may disagree." (*Pacific Gas*, *supra*, 475 U.S. at p. 15.) The transmittal requirements are based on "the possibility such information will improve reimbursement rates at some point in the future." (*Beeman I*, *supra*, 449 F.3d at p. 1040; *ARP*, *supra*, 138 Cal.App.4th at p. 1320.) Yet "[t]he goal of third-party administrators and payors ... is to keep costs as low as possible, a goal in direct conflict with that of the pharmacists." (ER141–142.)

Even worse, section 2527 requires claims processors to directly contradict their clients' interests in a free marketplace as well as the pharmacy reimbursement rate regulation debate. (See Ninth Circuit Supplemental Excerpts of Record at 17 [California Attorney General arguing in *A.A.M.* that "Section 2527's statistical dissemination

requirement is so that the disseminated data could potentially influence direct legislative price regulation if necessary"].) As discussed above, the pharmacists originally sought legislation to set rates for reimbursement that they considered fair and equitable. The requirement in section 2527 was a concession after the rate-regulation bill died in committee. (See pp. 9–12, *ante*.) But the pharmacist plaintiffs have argued that they intend to use the reports to lobby for mandatory higher reimbursement rates from claims processors. (ER163–164.) Section 2527 thus forces prescription claims processors to support a political position that is directly adverse to their interests.

In either case, as the Supreme Court has held, a statute that compels speech is by definition content-based, because a statute requiring the transmittal of information necessarily specifies the information to be disseminated. In other words, "[m]andating speech that a speaker would not otherwise make *necessarily* alters the content of the speech." (*Riley*, *supra*, 487 U.S. at p. 795; see also *Ingels v. Westwood One Broadcasting Services, Inc.* (2005) 129 Cal.App.4th 1050, 1074.) This is clearly true of section 2527—it prescribes specific data that must be gathered, organized, summarized, and

transmitted, and in doing so is necessarily a content-based regulation, thus triggering strict scrutiny.

Second, under the applicable strict scrutiny standard, section 2527 is plainly unconstitutional, because promotion of higher pharmacy reimbursement rates is not a sufficiently "compelling" interest. In order to survive strict scrutiny, there must be an "interest[] of the highest order," an "overriding state interest," or an "unusually important interest." (*Republican Party of Minn. v. White* (8th Cir. 2005) 416 F.3d 738, 749 [en banc].) The governmental interest in encouraging insurers and other third-party payors to reimburse pharmacists at a higher rate is not a compelling interest when compared to interests that the United States Supreme Court has found compelling. (Compare, e.g., *R.A.V.*, *supra*, 505 U.S. at p. 395 [ensuring basic human rights of groups subject to discrimination]; *Sable Communications of Cal., Inc. v. FCC* (1989) 492 U.S. 115, 126 [protecting well-being of children].)

The "information required by section 2527 is not necessary to protect the public health or safety, or even the public fisc; it is not aimed at protecting consumers, or insurers, from being misled." (*ARP*, *supra*, 138 Cal.App.4th at p. 1319; accord *R.J. Reynolds*

Tobacco Co. v. U.S. Food & Drug Admin. (D.D.C. 2012) 845 F.Supp.2d 266, 272 ["the graphic images here were neither designed to protect the consumer from confusion or deception, nor to increase consumer awareness of smoking risks"], affd. (D.C. Cir. Aug. 24, 2012) 2012 WL 3632003.) Rather, its purpose is to eliminate purported "unfair economic practices of drug claims processors by requiring them to disclose their own conflicts of interest and financial arrangements with third parties ...." (*ARP*, at p. 1318.) There is no legislative history suggesting any unlawful or misleading speech that section 2527 was intended to remedy. (See *id.* at p. 1316 ["we find no indication in the cited legislative history that the claimed marketplace inequities, if they exist, resulted from inaccurate, false, or misleading speech (or silence) by drug claims processors"].)

In other words, plaintiffs may not claim that section 2527 is a "consumer protection statute" or that the purportedly compelling interest is the protection of the public; to the contrary, the statute is intended to benefit independent pharmacies at the expense of claims processors and the third-party payors that are the claims processors' clients, and ultimately at the expense of *consumers* by causing higher prices for prescription medications. (ER163–164.) That is why the

Department of Insurance opposed the initial legislation. (See p. 10, *ante*.)[12] As a result, striking down section 2527 would not lead to a "parade of horribles" or have broader implications on disclosure laws designed to protect consumer health, safety, or the environment. (See, e.g., *Environmental Defense Center, Inc. v. U.S. EPA* (9th Cir. 2003) 344 F.3d 832, 848–850.) Indeed, there has been no sign of any such negative effects since section 2527 was first invalidated in 2006.

Nor is section 2527 narrowly tailored to any of the purported compelling interests upon which plaintiffs have relied. "In considering this question, a court assumes that certain protected speech may be regulated, and then asks what is the least restrictive alternative that can be used to achieve that goal." (*Ashcroft v. Am. Civil Liberties Union* (2004) 542 U.S. 656, 666.) And this "burden is not satisfied by mere speculation or conjecture; the party seeking to sustain the restriction must demonstrate that the harms it recites are

[12] There is some suggestion in the legislative history that consumers may ultimately benefit because they would be able to have their prescriptions filled at a greater number of retail pharmacies. (See *ARP*, *supra*, 138 Cal.App.4th at p. 1320.) But that is speculative, and is not a "compelling" state interest that could survive strict scrutiny.

real and that its restriction will in fact alleviate them to a material degree." (*ARP*, *supra*, 138 Cal.App.4th at p. 1320.)

If the state wished to generate the information section 2527 requires claims processors to divulge, there are a number of alternative and less restrictive means of doing so. The state could survey reimbursement rates, as it is required to do in other similar contexts. (See, e.g., Bus. & Prof. Code, § 4426 [requiring state to "conduct a study of the adequacy of Medi-Cal pharmacy reimbursement rates including the cost of providing prescription drugs and services"]; *Riley*, *supra*, 487 U.S. at p. 800 ["the State may itself publish the detailed financial disclosure forms it requires professional fundraisers to file. This procedure would communicate the desired information to the public without burdening a speaker with unwanted speech"].) Or the pharmacists, who already have the information covered by section 2527 (see *ARP*, *supra*, 138 Cal.App.4th at p. 1321 [quoting statement in legislative history from California Pharmacists Association that "[s]ince reliable studies are periodically conducted by the California Pharmacists Association, study costs to the claims processors can be *zero*"]), could distribute that information themselves.

Further, there is no evidence that dissemination of fee studies would increase the rate at which claims processors reimburse retail pharmacies for dispensing prescription drugs to health plan enrollees. Such a result would be counterintuitive—third-party payors are interested in *lowering* health care costs, not raising them. And the legislative history strongly indicates that rates would be unaffected, or at least that the impact of reimbursement studies on future pharmacy payments is speculative. The sponsor of the bill only "hope[d]" that the bill would change rates (*Beeman I*, *supra*, 449 F.3d at p. 1040), and the advice given to the Governor by his cabinet was that the bill "is fairly innocuous in its impact, since it merely requires a study to be made and distributed ... and does not require any action to be taken based on the study." (*Beeman II*, *supra*, 652 F.3d at p. 1091.) Accordingly, "[t]he mere transmission of the information, unaccompanied by any requirement that it be considered, utilized, or even read by the insurers, seems poorly designed to accomplish the state's goal." (*ARP*, *supra*, 138 Cal.App.4th at p. 1320.)

In short, the state's goal of encouraging insurers to pay an increased reimbursement rate to retail pharmacies is not a sufficiently "compelling" interest to survive strict scrutiny. And because there are

in any event clearly "more benign and narrowly tailored options" to achieving the state's goal (*Riley*, *supra*, 487 U.S. at p. 800), the statute fails strict scrutiny and is therefore unconstitutional.

III. Section 2527 Is Unconstitutional Regardless of Whether the Speech Compelled Is Deemed to Be "Commercial"

Plaintiffs have previously argued that the court should engage in a lesser degree of scrutiny over section 2527 because the speech it regulates is supposedly "commercial speech." But "[a] long line of Supreme Court cases ... confirms that speech does not become 'commercial' simply because it concerns economic subjects ...." (*Commodity Trend Service, Inc. v. CFTC* (7th Cir. 1998) 149 F.3d 679, 684.) Although strict scrutiny, not intermediate scrutiny, applies to section 2527, the statute also fails even intermediate scrutiny.

A. Even if the Speech That Section 2527 Regulates Were "Commercial," the Statute Would Also Fail Intermediate Scrutiny

The speech compelled by section 2527 is not "commercial speech" as this Court has defined that term, because the information section 2527 requires claims processors to transmit is not directed to an audience who may be influenced by that speech to engage in a commercial transaction with the claims processors. (*Kasky*, *supra*, 27 Cal.4th at p. 960.) The reason commercial speech is entitled to

intermediate, rather than strict, scrutiny is that commercial speech does "no more than propose a commercial transaction." (*Va. State Bd. of Pharmacy v. Va. Citizens Consumer Council, Inc.*, *supra*, 425 U.S. at p. 762.) That principle is inapplicable here, and therefore strict scrutiny, not intermediate scrutiny, applies.

But even if this Court were to determine that section 2527 compels commercial speech, thus subjecting it to "intermediate scrutiny," the statute still would violate California's free speech clause and the First Amendment.

For section 2527 to survive intermediate scrutiny, plaintiffs must show that (1) the government's interest is "substantial," (2) section 2527 directly advances that interest, (3) the regulation is "not more extensive than is necessary to serve that interest," and (4) there is a "'reasonable fit' between the government's purpose and the means chosen to achieve it." (*Kasky*, *supra*, 27 Cal.4th at p. 952, citing and quoting *Central Hudson Gas & Electric v. Public Service Com. of N.Y.* (1980) 447 U.S. 557, 566 (*Central Hudson*).)

No "substantial" governmental interest underlies section 2527 for the same reasons discussed above. (See pp. 40–42, *ante*.) In fact, section 2527 serves no real governmental interest at all. Presumably,

plaintiffs would argue that the governmental interest in section 2527 is to help support retail pharmacies in their negotiations with claims processors over reimbursement rates and in the public debate concerning whether reimbursement rates should be higher. That interest, such as it is, does not come close to being "substantial."

Even *assuming* there were a substantial state interest, section 2527 fails intermediate scrutiny, because it does not "directly advance" the legislature's asserted goal of increasing the rate by which third-party payors reimburse pharmacies for their dispensing services. While section 2527 compels claims processors to communicate the results of fee studies to their clients, it contains no mechanism to ensure that the insurers' receipt of the studies will result in increased reimbursement rates. There is only a "hope" that increased reimbursement will occur. (ER146; see p. 44, *ante*.) This speculative advancement of a state interest is insufficient to "demonstrate that the challenged regulation advances the Government's interest in a direct and material way." (*Gerawan Farming, Inc. v. Kawamura* (2004) 33 Cal.4th 1, 23, citations omitted.)

Moreover, the link between the state's supposed goal of helping retail pharmacies negotiate higher reimbursement rates from claims processors and the means used to achieve it "is, at most, tenuous." (*Central Hudson*, *supra*, 447 U.S. at p. 569.) The burden to show direct advancement of the government's interest "is not satisfied by mere speculation or conjecture; rather, a governmental body seeking to sustain a restriction on commercial speech must demonstrate that the harms it recites are real and that its restriction will in fact alleviate them to a material degree." (*Fla. Bar v. Went For It, Inc.* (1995) 515 U.S. 618, 626, citations omitted.) But plaintiffs have pointed to nothing that suggests pharmacists will in fact be able to obtain higher reimbursement rates as a result of the information that section 2527 requires claims processors to disseminate.

In addition, even the outcome required by section 2527—disseminating information concerning fees charged by California pharmacies—could be advanced by means that are a more "reasonable fit" and do not have an impact on free speech rights. For example, the state could require pharmacies to provide fee information to the state, which it could then publicize. Or the state could require pharmacies to supply insurers with reimbursement rate information received from

its customers. (See p. 43, *ante*.) These alternatives, among others, "would communicate the desired information to the [intended audience] without burdening a speaker with unwanted speech ...." (*Riley*, *supra*, 487 U.S. at p. 800.)

B. Section 2527 Does Not Warrant Lesser Scrutiny as an Allegedly Deceptive Advertising Regulation

The Supreme Court has allowed states to require dissemination of "purely factual and uncontroversial information ... as long as disclosure requirements are reasonably related to the State's interest in preventing deception of consumers." (*Zauderer v. Office of Disciplinary Counsel for Supreme Ct. of Ohio* (1985) 471 U.S. 626, 651 (*Zauderer*).) Plaintiffs have argued over the course of this litigation that section 2527 should receive the limited constitutional scrutiny articulated in *Zauderer* simply because the relationship between the pharmacists and the claims processors is "commercial." But in recent years, court after court—including the United States Supreme Court—has expressly tethered application of *Zauderer* to advertising that was either inherently or potentially deceptive.[13] This Court should as well.

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[13] The Second Circuit has applied limited scrutiny to a law that compelled special labels on mercury-containing light bulbs, noting

For example, the Supreme Court explained in *Milavetz, Gallop & Milavetz, P.A. v. United States* (2010) 130 S.Ct. 1324 that the key feature of the statute warranting lesser scrutiny was that it was intended "to combat the problem of inherently misleading commercial advertisements." (*Id.* at p. 1340.) The Court distinguished another decision (*In re R.M.J.* (1982) 455 U.S. 191) specifically on the ground that in that case "the restricted statements were not inherently misleading" (*Milavetz*, at p. 1340). Numerous other decisions have limited *Zauderer*'s lesser scrutiny to statutes aimed at preventing consumer deception.[14]

"Vermont's interest in protecting human health and the environment from mercury poisoning ...." (*Nat. Electrical Manufacturers Assn. v. Sorrell* (2d Cir. 2001) 272 F.3d 104, 115.) But where another Vermont labeling law (concerning synthetic growth hormones) did not implicate consumer health or safety, the Second Circuit held that *at least* intermediate scrutiny would be applied. (*Internat. Dairy Foods Assn. v. Amestoy* (2d Cir. 1996) 92 F.3d 67, 72–73.) These, and other precedents limiting constitutional scrutiny over commercial regulations, are questionable after the Supreme Court's decision in *Sorrell*. (*Sorrell*, *supra*, 131 S.Ct. at p. 2664 ["First Amendment requires heightened scrutiny whenever the government creates 'a regulation of speech because of disagreement with the message it conveys,'" and "[c]ommercial speech is no exception"].)

[14] (See, e.g., *Discount Tobacco City & Lottery, Inc. v. United States* (6th Cir. 2012) 674 F.3d 509, 523–524 [*Zauderer* test limited to regulations on "false, deceptive or misleading" speech]; *United States v. Philip Morris USA Inc.* (D.C. Cir. 2009) 566 F.3d 1095,

As discussed above, the pharmacies have presented no evidence or logical argument to suggest that section 2527 was enacted to combat consumer deceptions or to protect human health and safety. The court of appeal in *ARP* found "no indication in the cited legislative history that the claimed marketplace inequities, if they exist, resulted from inaccurate, false, or misleading speech (or silence) by drug claims processors." (*ARP*, *supra*, 138 Cal.App.4th at p. 1316.) And "[t]he information required by section 2527 is not necessary to protect the public health or safety." (*Id.* at p. 1318.) Strict scrutiny applies to section 2527.

1144–1145 [*Zauderer* standard "geared towards thwarting prospective efforts by Defendants to either directly mislead consumers or capitalize on their prior deceptions"]; *Video Software Dealers Assn. v. Schwarzenegger* (9th Cir. 2009) 556 F.3d 950, 966 [limited scrutiny in *Zauderer* "justified by the need to 'dissipate the possibility of consumer confusion or deception'"]; *United States v. Wenger* (10th Cir. 2005) 427 F.3d 840, 849 [*Zauderer* "presumes that the government's interest in preventing *consumer deception* is substantial"], italics added; see also *Glickman v. Wileman Brothers & Elliott, Inc.* (1997) 521 U.S. 457, 491 [dis. op. of Souter, J.] ["*Zauderer* carries no authority for a mandate unrelated to the interest in avoiding misleading or incomplete commercial messages"].)

C. Section 2527 Is Not Part of a Broader Regulatory Scheme and Thus Is Unconstitutional Under *United Foods*

Another constitutional infirmity in section 2527 is the fact that it is a lone regulation untethered to a broader regulatory scheme. Its sole purpose is to compel speech, and it therefore runs squarely into the Constitution's free speech protections.

In *United States v. United Foods, Inc.* (2001) 533 U.S. 405 (*United Foods*), the United States Supreme Court held that a regulatory scheme requiring the regulated entities to participate (through mandatory funding) in speech activities violates the First Amendment, regardless of whether the speech is commercial. The Court noted that it had "not upheld compelled subsidies for speech in the context of a program where the principal object is speech itself." (*Id.* at p. 415.) The Court distinguished the broad regulatory scheme at issue in *Glickman v. Wileman Brothers & Elliott, Inc.* (1997) 521 U.S. 457 (*Glickman*), which survived First Amendment scrutiny, on the grounds that in *Glickman*, "the mandated assessments for speech were ancillary to a more comprehensive program restricting marketing." In contrast, the speech in *United Foods*, "far from being ancillary, is the principal object of the regulatory scheme." (*United*

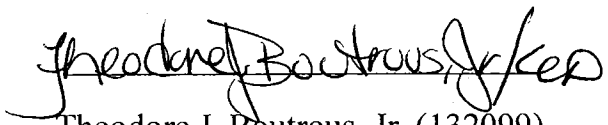
Foods, at pp. 411–412; see also *Delano Farms Co. v. Cal. Table Grape Com.* (9th Cir. 2003) 318 F.3d 895, 898–899 [invalidating statute because it was not "a 'comprehensive program' that 'displace[s] many aspects of independent business activity,' exempts the firms within its scope from the antitrust laws, and makes them 'part of a broader collective enterprise'"] (*Delano Farms*).)

United Foods and *Delano Farms* concerned compelled subsidies of speech, and section 2527 shares the offending characteristic of the regulations struck down in those cases. Section 2527 compels speech in the absence of a broader regulatory scheme—its sole directive is to require claims processors to undertake or obtain pharmacy fee studies and communicate the results of those studies to their clients. (Civ. Code, § 2527, subds. (b)–(d).) And unlike in *Glickman*, *supra*, 521 U.S at p. 462, where the regulation was intended to benefit the regulated entities, the speech compelled by section 2527 is not intended to, and does not, provide any benefit *to the claims processors*. Section 2527 "compel[s] subsidies for speech in the context of a program where the principal object is speech itself," and thus is unconstitutional under *United Foods*. (533 U.S. at p. 415.)

CONCLUSION

This Court should resolve the question certified in the affirmative, and hold that Civil Code section 2527 compels speech in violation of article I, section 2 of the California Constitution.

Dated: September 19, 2012 Respectfully submitted,



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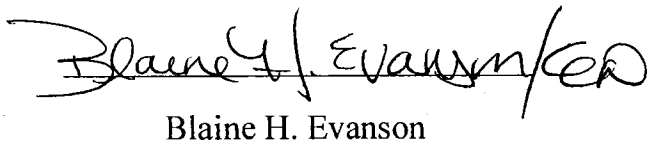
CERTIFICATE OF WORD COUNT

Pursuant to California Rule of Court 8.204, subdivision (c), I hereby certify that this brief contains 10,939 words, including footnotes, excluding those portions as permitted under Rule 8.204, subdivision (c)(3). I have relied on the word count of the computer program used to prepare the brief.

Dated: September 19, 2012



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PROOF OF SERVICE

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On September 19, 2012, I served a copy of **APPELLANTS' CONSOLIDATED OPENING BRIEF** in this action by placing a true and correct copy thereof, enclosed in a sealed envelope with postage fully prepaid, in the United States Mail on the following interested parties in this action:

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I declare, under penalty of perjury, that the foregoing is true and correct.

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