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## Competing With Antitrust Laws: How New York's Post and Hold Liquor Law Will Lose Against the Sherman Act

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# Competing with Antitrust Laws

## HOW NEW YORK'S POST AND HOLD LIQUOR LAW WILL LOSE AGAINST THE SHERMAN ACT

### INTRODUCTION

The distribution and sale of alcohol has a colorful past in this country,<sup>1</sup> and in certain respects, remains controversial to this day.<sup>2</sup> While we no longer live in the “Wild West” and are thus no longer concerned with the dangers of saloons,<sup>3</sup> alcohol is still linked to a host of societal problems.<sup>4</sup> In response to the social evils tied to alcohol, the states rely on both their police powers and the authority granted to them by the Twenty-first Amendment to promote temperance.<sup>5</sup> Accordingly, the states have enacted a variety of laws designed to achieve this goal.<sup>6</sup>

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<sup>1</sup> See generally Sidney J. Spaeth, *The Twenty-First Amendment and State Control Over Intoxicating Liquor: Accommodating the Federal Interest*, 79 CAL. L. REV. 161, 165-80 (1991) (recounting the origins of the battle for prohibition as linked to “the ubiquitous image of the debauched saloon” as fuel for the temperance movement). For example, in the 1800s, violence broke out against saloons, and women who were advocating temperance resorted to attacking saloons, with the hatchet as their “weapon of choice.” See *id.* at 169 (describing Carry Nation’s “hatchetations” on Kansas saloons”).

<sup>2</sup> See *infra* note 12 and accompanying text.

<sup>3</sup> See Clayton L. Silvernail, *Smoke, Mirrors and Myopia: How the States Are Able to Pass Unconstitutional Laws Against the Direct Shipping of Wine in Interstate Commerce*, 44 S. TEX. L. REV. 499, 505 (2003).

<sup>4</sup> Alcohol is a leading cause of car accidents, especially car accident fatalities. See, e.g., Bureau of Transportation Services: Table 2-20: Fatalities in Crashes by Number of Vehicles and Alcohol Involvement, [http://www.bts.gov/publications/national\\_transportation\\_statistics/html/table\\_02\\_20.html](http://www.bts.gov/publications/national_transportation_statistics/html/table_02_20.html) (last visited Jan. 4, 2010); MADD Campaign to Eliminate Drunk Driving: Statistics, <http://www.madd.org/Drunk-Driving/Drunk-Driving/Statistics/AllStats.aspx> (last visited Jan. 4, 2010). Alcohol is a necessary component of binge drinking and often a major factor in hazing among college students. See generally HANK NUWER, *WRONGS OF PASSAGE: FRATERNITIES, SORORITIES, HAZING, AND BINGE DRINKING* (1999). Excessive use of alcohol leads to severe liver damage and is actually the “[third] leading lifestyle-related cause of death for people in the United States each year.” Centers for Disease Control and Prevention: Alcohol and Public Health, <http://www.cdc.gov/alcohol/> (last visited Feb. 3, 2010).

<sup>5</sup> “The transportation or importation into any State, Territory, or possession of the United States for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited.” U.S. CONST. amend. XXI, § 2.

<sup>6</sup> See, e.g., *infra* notes 34, 99, 106, 151-152 and accompanying text.

New York, like many other states,<sup>7</sup> has enacted “price posting” and “post and hold” liquor laws designed to regulate the distribution of alcohol within the state.<sup>8</sup> New York’s price posting law requires manufacturers and wholesalers to file price schedules that report future prices.<sup>9</sup> The law is also considered a “post and hold” law, as it requires them to make resale prices public, then hold those prices for a defined period of time, rather than allow prices to fluctuate based on market forces.<sup>10</sup>

As with many other liquor laws,<sup>11</sup> there has been controversy over the years regarding the validity of the price posting laws, especially those classified as post and hold.<sup>12</sup> This Note argues that New York’s post and hold law is in contravention of the Sherman Antitrust Act<sup>13</sup> and hard to defend under current Twenty-first Amendment jurisprudence, which has steadily limited the broad grant of powers given to the states regarding the control of liquor within their borders.

Part I provides background information on both the history of alcohol distribution in the United States and the Sherman Act, as well as a brief overview of New York’s distribution system. Part II analyzes the evolution of the United States Supreme Court jurisprudence on the Twenty-first Amendment, illustrating how the Court has shifted its interpretation of the Amendment from a broad grant of authority to the states over liquor regulation to a balancing of competing interests.<sup>14</sup> Part III examines the steps of a federal antitrust challenge to a state law, and describes the federal decisions that specifically address the validity of price posting laws in Oregon,<sup>15</sup> Maryland,<sup>16</sup> and Washington,<sup>17</sup> which closely resemble New York’s statute. Part IV concludes that the New

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<sup>7</sup> For example, Oregon, Maryland, and Washington all had price posting laws. See *infra* notes 222-223, 235, 249 and accompanying text.

<sup>8</sup> See N.Y. ALCO. BEV. CONT. LAW § 101-b (McKinney 2009).

<sup>9</sup> *Id.* § 101-b(3)(a).

<sup>10</sup> *Id.* § 101-b(3)(b).

<sup>11</sup> See, e.g., *infra* notes 34, 97-99, 106, 151-152 and accompanying text.

<sup>12</sup> See *Costco Wholesale Corp. v. Maleng*, 522 F.3d 874, 895-96 (9th Cir. 2008) (holding that Washington’s “post and hold” liquor distribution regime violated the Sherman Act); accord *TFWS, Inc. v. Schaefer*, 242 F.3d 198, 209-10 (4th Cir. 2001); *Miller v. Hedlund*, 813 F.2d 1344, 1349-51 (9th Cir. 1987); see also *infra* Part III.B.

<sup>13</sup> See 15 U.S.C. § 1-7 (2006).

<sup>14</sup> See *infra* notes 81-85 and accompanying text.

<sup>15</sup> See *Miller*, 813 F.2d 1344.

<sup>16</sup> See *TFWS, Inc.*, 242 F.3d 198.

<sup>17</sup> See *Costco*, 522 F.3d 874.

York statute will not be able to survive an antitrust challenge in light of these recent cases because the state most likely cannot put up the formidable defense now required by the Supreme Court. As it stands, New York's post and hold regime should be struck down if challenged in court.

In late 2009, the New York State Law Revision Commission completed a two-year review of the New York Alcohol Beverage Control Law (the "ABC Law"), of which price posting is one narrow issue.<sup>18</sup> In its final report, the Commission flagged Section 101-b as a potential source of legal problems for the state due to the evolving nature of Twenty-first Amendment jurisprudence, especially in light of the invalidation of several post and hold liquor laws by the federal courts.<sup>19</sup> Thus, the state may actually be in a good position to take protective action if it so desires.

## I. BACKGROUND OF ALCOHOL AND ANTITRUST LAWS

### A. *A Brief History of Alcohol Distribution in the United States*

With the exception of Prohibition, there has always been prolific regulation of commerce in alcohol by the states, largely because governments viewed it as a source of revenue.<sup>20</sup> The real controversy over alcohol regulation began in the early to mid-1800s, when religious opposition began to form against alcohol consumption.<sup>21</sup> As a result of the lobbying efforts of anti-saloon groups and temperance societies, many states passed laws banning saloons and the "manufacture of 'spirituous or

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<sup>18</sup> See NEW YORK STATE LAW REVISION COMMISSION REPORT ON THE ALCOHOL BEVERAGE CONTROL LAW AND ITS ADMINISTRATION 1, 23 (December 15, 2009), available at <http://www.lawrevision.state.ny.us/abcls.php> (last visited Feb. 18, 2010).

<sup>19</sup> See *id.* at 217-20 (warning that the fact that Section 101-b survived an earlier antitrust challenge "should not make . . . the Legislature sanguine about the price posting and hold requirements.").

<sup>20</sup> See RICHARD MCGOWAN, GOVERNMENT REGULATION OF THE ALCOHOL INDUSTRY: THE SEARCH FOR REVENUE AND THE COMMON GOOD 3-6, 35 (1997) ("Throughout the history of the American alcohol industry, government has played a pivotal role in determining where, when, and how alcoholic beverages are sold. Every level of government (federal, state, and local) has revenue as well as regulatory interest in the industry.").

<sup>21</sup> See W. J. Rorabaugh, *Reexamining the Prohibition Amendment*, 8 YALE J.L. & HUMAN. 285, 288 (1996) ("The temperance campaign that started in the 1820's demanded personal abstinence both as the price of church membership and as a badge of middle-class respectability."); MCGOWAN, *supra* note 20, at 41 (noting that there was no religious opposition to the alcohol industry prior to the 1850s).

intoxicating liquors.”<sup>22</sup> Enforcement was largely unsuccessful because liquor continued to be smuggled across state lines,<sup>23</sup> and ultimately, the laws were repealed or struck down by state courts, at least in part, as unconstitutional.<sup>24</sup> However, when the issue reached the Supreme Court in *Mugler v. Kansas*,<sup>25</sup> the Court held that complete prohibition of alcohol sale and production was within a state’s police power.<sup>26</sup> Thirteen years later, the Supreme Court declared that *Mugler* “stood for the ‘undoubted right’ of states to regulate their internal affairs.”<sup>27</sup>

While the states were given free range to extensively regulate alcohol within their borders, Prohibitionists<sup>28</sup> were

<sup>22</sup> Silvernail, *supra* note 3, at 505; *see also* Spaeth, *supra* note 1, at 168-69. These laws were commonly referred to as “Maine laws.” *See id.* (internal quotation marks omitted); *see also* Rorabaugh, *supra* note 21, at 288-89 (noting that Maine was the first state to enact prohibition).

<sup>23</sup> Rorabaugh, *supra* note 21, at 289.

<sup>24</sup> There were several factors that led to the repeal of most of these early prohibition laws. First, they met strong opposition from immigrants and anti-reform groups. *See* JACK S. BLOCKER, IAN R. TYRRELL, AND DAVID M. FAHEY, ALCOHOL AND TEMPERANCE IN MODERN HISTORY: A GLOBAL ENCYCLOPEDIA 395 (2003) (explaining that immigrants and anti-reform groups became instrumental in the demise of the Maine laws by joining anti-temperance coalitions to speak out against them). Moreover, the laws were undermined by court rulings, including being struck down as unconstitutional. *See, e.g.*, *People v. Toynbee*, 2 Parker Crim. Rep. 329 (N.Y. 1855) (finding that the prohibition of the sale of intoxicating liquors was an unconstitutional interference with property in violation of individuals’ due process rights); *see also* BLOCKER, *supra* at 395 (by the end of the Civil War, most prohibition laws were “unenforced, overturned, or struck down by state courts as unconstitutional.”); *see also* RICHARD F. HAMM, SHAPING THE EIGHTEENTH AMENDMENT: TEMPERANCE REFORM, LEGAL CULTURE, AND THE POLITY, 1880-1920, at 20 (1995) (stating that most prohibition laws were rendered ineffective by the courts). Finally, the Civil War distracted proponents of temperance, to the point where “progress” was not only halted but reversed. *Id.* Even the laws that still survived after the Civil War suffered from “admittedly lax enforcement.” *Id.*

<sup>25</sup> 123 U.S. 623 (1887). Kansas was the first state to “go dry” by going further than the Maine laws and amending its constitution to forbid the manufacture and sale of alcohol within its borders. *See* Silvernail, *supra* note 3, at 505-06.

<sup>26</sup> *Mugler*, 123 U.S. at 662.

<sup>27</sup> Silvernail, *supra* note 3, at 507 (quoting *Leisy v. Hardin*, 135 U.S. 100, 122 (1890)) (“The effect of *Leisy* and prior decisions . . . was to give states carte blanche with regards to regulating intoxicating liquors within their bounds.”).

<sup>28</sup> An early group of Prohibitionists were working-class Americans—the Washingtonians—who “pledg[ed] not to drink any alcoholic liquors.” *See* HAMM, *supra* note 24, at 20. The movement spread to the middle class, who also sought to end alcohol consumption. *Id.* After the Civil War, abstinence increasingly became a religious talking point, “[i]n particular, pietists, members of evangelical sects, including Baptists, Methodists, and Presbyterians . . . saw prohibition as a needed corrective to the nation’s moral laxity and resulting social problems.” *Id.* at 22 (noting that religion was linked with ethnicity, and therefore Americans of English, Scottish, and sometimes Scandinavian descent were more likely to support Prohibition than the Irish, German, Italian, and Polish.) Two major Prohibitionist groups were the Prohibition Party, whose members came primarily from the Republican Party, and the National Women’s Christian Temperance Union, which consisted of middle-class

concerned that the states could not ban the importation of alcohol.<sup>29</sup> In response to this dilemma, they lobbied Congress for states' rights to keep alcohol out entirely, and their efforts were rewarded by the enactment of the Wilson Act in 1890.<sup>30</sup> The Wilson Act subjected imported alcohol to a state's applicable laws upon arrival.<sup>31</sup> Unfortunately for the Prohibitionists,<sup>32</sup> soon after the Wilson Act's enactment, the Supreme Court suggested that the Act did not give the states permission to prohibit the importation of alcohol.<sup>33</sup> The Court cemented this position seven years later, explicitly holding that laws interfering with the importation of alcohol were "wholly incompatible with and repugnant to" individuals' constitutional right to ship and receive goods to and from another state.<sup>34</sup>

Perhaps deflated by the Supreme Court's interpretation of the Wilson Act, the Prohibitionists lobbied Congress yet again to give states the right to ban alcohol importation,<sup>35</sup> which led to the passage of the Webb-Kenyon Act in 1913.<sup>36</sup> The Webb-Kenyon Act specifically authorized states to keep alcohol out of their borders.<sup>37</sup> The Act survived a constitutional

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women. *See id.* at 23-24. The Anti-Saloon League, "one of the most powerful political organizations in United States history," was another prohibitionist group, made up of churches and other temperance societies. Spaeth, *supra* note 1, at 170.

<sup>29</sup> *See* *Bowman v. Chicago & Northwestern Ry. Co.*, 125 U.S. 465, 500 (1888).

<sup>30</sup> *See* 27 U.S.C. § 121 (2006).

<sup>31</sup> *Id.* (stating, in relevant part, that imported alcohol "shall upon arrival in [a] State . . . be subject to the operation and effect of the laws of such State . . . enacted in the exercise of its police powers").

<sup>32</sup> *See* Silvernail, *supra* note 3, at 508 (describing the Wilson Act as a "hollow victory for the Prohibitionists" because the Supreme Court failed to interpret the Act as authority for the states to ban liquor importation).

<sup>33</sup> *Id.* at 509 ("[The Wilson Act] simply removed an impediment to the enforcement of the state laws . . . . [i]t imparted no power to the state not then possessed . . . .") Many people argue that the Wilson Act was intended to allow dry states to remain dry, or at least that the Supreme Court should have interpreted it in such a way. *See, e.g.*, Spaeth, *supra* note 1, at 172-73 & n.81 (explaining the impetus behind the passage of the Wilson Act, and quoting Senator Kenyon of Iowa, who expressed dismay that the Act was not used in such a way to give states the option to remain dry).

<sup>34</sup> *Vance v. W.A. Vandercook Co.*, 170 U.S. 438, 455 (1898) (striking down a law giving state agents the exclusive right to purchase imported alcohol, because the law gave the state, via its agents, opportunity to discriminate against sister states by selectively choosing which to buy from); *see also* *Rhodes v. Iowa*, 170 U.S. 412, 420 (1898) (rejecting Iowa's argument that the phrase "upon arrival" in the Wilson Act gave the state authority to seize imported alcohol the moment it crossed state lines because such an interpretation would give Iowa's law "extraterritorial operation," thus "render[ing] the act of Congress repugnant to the Constitution of the United States").

<sup>35</sup> *See* Silvernail, *supra* note 3, at 511.

<sup>36</sup> *See* 27 U.S.C. § 122 (2006).

<sup>37</sup> *Id.* (providing, in relevant part, that "[t]he shipment or transportation . . . of any [alcohol] . . . from one State . . . into any other State . . . in violation of any law of

challenge in *James Clark Distilling Co. v. Western Maryland Railway Company*,<sup>38</sup> in which the Supreme Court upheld a West Virginia law that prohibited the importation of alcohol for personal use.<sup>39</sup> It was not long after the passage of the Webb-Kenyon Act that the Prohibitionists finally achieved their desired goal with the ratification of the Eighteenth Amendment in 1919, which banned alcohol entirely.<sup>40</sup> However, the Prohibitionists ultimately lost their battle when the experiment of Prohibition failed miserably by lasting a mere fourteen years.<sup>41</sup> The Twenty-first Amendment was ratified in 1933 and is the current source of constitutional authority granted to the states regarding the regulation of liquor.<sup>42</sup> The Supreme Court's interpretation of the extent of this authority has fluctuated over time,<sup>43</sup> as discussed in detail in Part III. The price posting liquor laws have repeatedly been challenged as violations of the Sherman Act; thus, an elementary understanding of antitrust law, specifically the Sherman Act, will be helpful in addressing the constitutionality of New York's price posting law.

### B. *A Brief Introduction to the Sherman Antitrust Act*

Antitrust laws . . . are the Magna Carta of free enterprise.<sup>44</sup>

For better or worse,<sup>45</sup> the American economy is founded on free enterprise. In order for free enterprise to produce and

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such State . . . is prohibited"). Interestingly, President Taft vetoed the Act as "an unconstitutional delegation by Congress to the states of the exclusive power to regulate interstate commerce in liquors." Spaeth, *supra* note 1, at 173-74. Congress, however, overrode Taft's veto. *Id.* at 174.

<sup>38</sup> 242 U.S. 311 (1917).

<sup>39</sup> *See id.* at 332.

<sup>40</sup> U.S. Const. amend. XVIII (repealed 1933) ("[T]he manufacture, sale, or transportation of intoxicating liquors within, the importation thereof into, or the exportation thereof from the United States . . . is hereby prohibited."); *see also* Silvernail, *supra* note 3, at 512.

<sup>41</sup> The Eighteenth Amendment completed ratification in 1919 and was repealed by the Twenty-first Amendment in 1933. *See* U.S. CONST. amend. XVIII, Historical Notes (repealed 1933); U.S. CONST. amend. XXI.

<sup>42</sup> U.S. CONST. amend. XXI; *see also* Silvernail, *supra* note 3 at 500 ("The Twenty-first Amendment gives the states the power to regulate the manufacture, distribution, and sale of intoxicating liquors within their borders").

<sup>43</sup> *See infra* notes 81-85 and accompanying text.

<sup>44</sup> *United States v. Topco Assocs., Inc.*, 405 U.S. 596, 610 (1972).

<sup>45</sup> *See* JOHN H. SHENEFIELD & IRWIN M. STELZER, *THE ANTITRUST LAWS* 6 (1993) (noting that a common critique of America's market economy is its potential for abuse and inevitable inequality).

maintain a flourishing economy, there must be competition.<sup>46</sup> Competition promotes consumer welfare<sup>47</sup> and efficiency.<sup>48</sup> Since competition is vital to the success of the American economy, it is no surprise that laws have been enacted to prevent private actors from subverting it.<sup>49</sup> The most basic, and most important, “pro-competition” law is the Sherman Antitrust<sup>50</sup> Act<sup>51</sup> (the “Sherman Act”).<sup>52</sup>

The Sherman Act has lofty goals: it seeks to protect and encourage producers by “diffus[ing] economic power and maximiz[ing] individual opportunity” to create a “fair” playing field, while simultaneously “maximiz[ing] efficiency and consumer welfare.”<sup>53</sup> To effect these goals, the Sherman Act “proscribes agreements in restraint of trade”<sup>54</sup> as well as “monopoly abuse.”<sup>55</sup> Relevant types of prohibited restraints of

<sup>46</sup> See *id.* at 7 (“The engine of free enterprise is competition.”).

<sup>47</sup> See *id.* The authors point out that “[n]umerous sellers, vying for customers, must produce goods and services of sufficient quality, and at acceptable prices, or be driven from the field.” *Id.* Such a system results in better (and usually more) options for consumers because sellers have an incentive to be innovative to attract new customers and increase profits, or at least maintain a consistent quality of product to keep their current customers. See *id.* at 12.

<sup>48</sup> See *id.* at 7 (“[The] necessity [of vying for consumers] forces [sellers] to be efficient, to buy so-called inputs—labor and materials—at the lowest possible prices, and . . . [keep] production costs . . . to a minimum.”).

<sup>49</sup> See *id.* (noting that one way competition can fail is when “private participants in the market subvert competition and thus prevent market forces from operating freely”).

<sup>50</sup> “Antitrust” laws are so named as a result of practices of the large enterprises of Standard Oil, sugar, whiskey, and others of taking the forms of “trusts,” placing “shareholder voting power in the hands of a single managing trustee.” See *id.* at 8.

<sup>51</sup> 15 U.S.C. §§ 1-7 (2006). Additional antitrust laws were enacted to strengthen the Sherman Act. See SHENEFIELD & STELZER, *supra* note 45, at 9. Major ones include the Clayton Act, and the Federal Trade Commission Act. *Id.*

<sup>52</sup> WALTER ADAMS & HORACE M. GRAY, *MONOPOLY IN AMERICA*, v (1955) (describing the Sherman Act as “the first and most important antitrust [law]”).

<sup>53</sup> SHENEFIELD & STELZER, *supra* note 45, at 13; see also ADAMS & GRAY, *supra* note 52, at 177 (“competition provides an effective technique for reconciling the dual objectives of economic welfare and economic freedom.” (internal quotation marks omitted)).

<sup>54</sup> SHENEFIELD & STELZER, *supra* note 45, at 14; see also 15 U.S.C. § 1. A restraint of trade refers to an action or condition that is intended to prevent free competition in business. BLACK’S LAW DICTIONARY (8th ed. 2004). The Sherman Act refers to “contract, combination, . . . or conspiracy” as opposed to the term “agreement.” 15 U.S.C. § 1. Because Professors Lopatka and Page make a compelling argument that the Supreme Court is primarily concerned with the “element of agreement” when applying this section, see John E. Lopatka & William H. Page, *State Action and the Meaning of Agreement Under the Sherman Act: An Approach to Hybrid Restraints*, 20 YALE J. ON REG. 269, 278-79 & notes 38-43 (2003), this Note will generally use the term “agreement” as well to reflect the Sherman Act’s prohibition of concerted action to unreasonably restrain trade.

<sup>55</sup> See SHENEFIELD & STELZER, *supra* note 45, at 17; see 15 U.S.C. § 2.

trade include vertical price restraints and horizontal price fixing—as exemplified by New York’s ABC Law § 101-b.

Vertical price restraints involve attempts by manufacturers to set the prices at which their distributors will resell the manufacturers’ goods to consumers.<sup>56</sup> This type of behavior, also known as resale price maintenance,<sup>57</sup> falls within the category of “agreements in restraint of trade.”<sup>58</sup> Post and hold laws have typically been treated as horizontal price fixing, which generally involves an agreement among competitors to increase, set, or maintain prices.<sup>59</sup> Section 1 of the Sherman Act provides that agreements in restraint of trade are illegal, and thus actors who violate Section 1 may be subject to criminal prosecution.<sup>60</sup> The key concept in Section 1 is concerted action, or “agreement,” because without collective action there can be no violation of the provision, no matter how anticompetitive an individual’s conduct.<sup>61</sup>

The Supreme Court has interpreted Section 1 to apply only to restraints of trade that are unreasonable,<sup>62</sup> and has developed two categories of such unreasonable restraints.<sup>63</sup> First, there are restraints that are deemed unreasonable *per se*, and accordingly, these are *per se* violations of Section 1.<sup>64</sup>

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<sup>56</sup> See SHENEFIELD & STELZER, *supra* note 45, at 65. For a simple example: Company A manufactures whiskey and sells it to wholesalers, such as Costco or Sam’s Club, but only on the stipulation that they will sell the whiskey to their consumers at \$30 per bottle. This agreement is a vertical price restraint because Company A, as an upstream, or vertical, seller, is setting prices for a downstream seller rather than allowing market forces (supply and demand) to control the resale price of the whiskey. The same analysis would apply to a wholesaler who imposed a similar condition on downstream retail liquor stores that purchase the whiskey for future resale to individual consumers.

<sup>57</sup> See *id.* at 66.

<sup>58</sup> SHENEFIELD & STELZER, *supra* note 45, at 15; see also 15 U.S.C. § 1.

<sup>59</sup> See *infra* Part III.B.; see also Dep’t of Justice, U.S. Attorneys, Antitrust Resource Manual, Identifying Sherman Act Violations, available at [http://www.justice.gov/usao/eousa/foia\\_reading\\_room/usam/title7/ant00008.htm](http://www.justice.gov/usao/eousa/foia_reading_room/usam/title7/ant00008.htm) (last visited Jan. 4, 2010).

<sup>60</sup> 15 U.S.C. § 1 (“Every contract, combination . . . or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations is declared to be illegal. Every person who shall [engage in the prohibited activity] shall be deemed guilty of a felony.”).

<sup>61</sup> 15 U.S.C. § 1; see also Lopatka & Page, *supra* note 54, at 273; SHENEFIELD & STELZER, *supra* note 45, at 15.

<sup>62</sup> Standard Oil Co. of New Jersey v. U.S., 221 U.S. 1, 60-62 (1911).

<sup>63</sup> See SHENEFIELD & STELZER, *supra* note 45, at 15-16.

<sup>64</sup> See *id.* at 16; see also N. Pac. Ry. v. U.S., 356 U.S. 1, 5 (1958) (in which the Supreme Court states that “there are certain agreements or practices which because of their pernicious effect on competition and lack of any redeeming virtue are conclusively presumed to be unreasonable.”).

Per se unreasonable restraints include price-fixing.<sup>65</sup> The second category of unreasonable restraints of trade consists of restraints that are assessed under the “rule of reason.”<sup>66</sup> In addition to requiring an agreement to unreasonably restrain trade, the Sherman Act also requires that the wrongful conduct (i.e., anticompetitive practices) result in “competitive injury.”<sup>67</sup> Competitive injury includes artificially high prices, limited output of goods or services, or exclusion of competitors.<sup>68</sup> In summary, a vertical price restraint that violates the Sherman Act is one that involves an agreement to restrain trade (by setting/controlling prices irrespective of market forces) that causes competitive injury. New York’s price posting scheme, of which Section 101-b is an integral part, contemplates just such a prohibited restraint.<sup>69</sup>

### C. *A Brief Overview of New York’s Price Posting Scheme*

New York maintains a “three tier” alcohol distribution system.<sup>70</sup> This means that, with the exception of direct shipping in wine,<sup>71</sup> a manufacturer must sell alcohol to New York wholesalers, who in turn sell to retailers, who then sell to

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<sup>65</sup> See ADAMS & GRAY, *supra* note 52, at 164; see *infra* notes 252-253 and accompanying text.

<sup>66</sup> SHENEFIELD & STELZER, *supra* note 45, at 16. In general, antitrust law is not always black-and-white, and many activities are examined by the courts to determine “whether, on balance, the conduct is procompetitive or anticompetitive.” *Id.*

<sup>67</sup> *Id.* at 32 (“[T]he basic inquiry concerns competitive injury . . .”). Market participants can cause competitive injury without violating the Sherman Act, however. For example, a firm with a monopoly in a market is not necessarily violating the Sherman Act despite the fact that its conduct decreases competition by excluding competitors, as long as the firm did not achieve its monopoly status by entering into agreements with other firms to establish their respective market positions, as opposed to individually competing for consumers. See *id.* at 36 (“[P]ure, lawfully attained monopoly is not prohibited.”).

<sup>68</sup> *Id.* at 32.

<sup>69</sup> See *infra* Part IV.

<sup>70</sup> See *Arnold’s Wines, Inc. v. Boyle*, 571 F.3d 185, 187-88 (2d Cir. 2009) (describing New York’s three-tier regulatory system); see also FTC, POSSIBLE ANTICOMPETITIVE BARRIERS TO E-COMMERCE: WINE 5-7 (July 2003) (hereinafter FTC REPORT), available at <http://www.ftc.gov/os/2003/07/winereport2.pdf> (last visited Jan. 4, 2010).

<sup>71</sup> New York permits both out-of-state and in-state wineries to ship directly to consumers. N.Y. ALCO. BEV. CONT. LAW §§ 79-c, -d. For the interested reader, direct shipping of wine is also a controversial issue. The Supreme Court recently discussed the issue in *Granholm v. Heald*, 544 U.S. 460 (2005), and there are numerous scholarly articles available for more information. See e.g. Elizabeth Norton, *The Twenty-first Amendment in the Twenty-first Century: Reconsidering State Liquor Controls in Light of Granholm v. Heald*, 67 OHIO ST. L. J. 1465, 1471 (2006); Silvernail, *supra* note 3.

consumers.<sup>72</sup> The New York State Liquor Authority (the “SLA”) is responsible for enforcing New York’s Alcohol Beverage Control Law, which is a complex set of laws that generally prohibits deviation from the “three tier” system.<sup>73</sup>

This Note focuses on the “price posting” statute within the ABC Law, specifically whether compliance with the law is a violation of the Sherman Act. New York’s price posting scheme is found in Section 101-b of the ABC Law.<sup>74</sup> Within Section 101-b, there are requirements that both manufacturers and wholesalers file a monthly posting with the SLA that lists their products’ prices for the following pricing period.<sup>75</sup> After the prices are filed, the SLA produces a composite for inspection, and there is a three-day window in which wholesalers may lower their prices to the lowest posted prices for the same products.<sup>76</sup> After this window ends, the prices cannot be changed for the entire month without prior written permission from the SLA.<sup>77</sup>

In light of current Twenty-first Amendment jurisprudence, Section 101-b’s mandate that prices must not be changed without the SLA’s permission (as opposed to being dependent on market forces) constitutes an unreasonable restraint of trade, thereby violating the Sherman Act.<sup>78</sup> The Twenty-first Amendment may serve as a defense when a liquor law is challenged as preempted by the Sherman Act.<sup>79</sup> Therefore, the problems of Section 101-b should not be addressed without considering the Supreme Court’s approach to the Twenty-first Amendment and the regulatory powers it gave to the states regarding alcohol. This is especially true because of conflicting language in Supreme Court jurisprudence.<sup>80</sup>

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<sup>72</sup> See *Arnold’s Wines*, 571 F.3d at 187-88 (citing various provisions of New York’s Alcohol Beverage Control Law); see also FTC REPORT, *supra* note 70, at 5-7.

<sup>73</sup> See *Arnold’s Wines*, 571 F.3d at 187 n.1 (“With the exception of wineries, . . . all manufacturers’ products must pass through the three-tier system.”) (internal citations omitted).

<sup>74</sup> See generally N.Y. ALCO. BEV. CONT. LAW § 101-b.

<sup>75</sup> *Id.* § 101-b(3)(a).

<sup>76</sup> *Id.* § 101-b(4). The SLA also has the option to simply produce all filed price schedules for inspection, rather than creating a composite of them. *Id.*

<sup>77</sup> *Id.* § 101-b(3)(b).

<sup>78</sup> See *supra* Part I.B.

<sup>79</sup> See *infra* note 120 and accompanying text.

<sup>80</sup> See *infra* notes 89-95, 118 and accompanying text.

## II. EVOLUTION OF TWENTY-FIRST AMENDMENT JURISPRUDENCE

Over time, the interpretation of the scope of power that Section 2 of the Twenty-first Amendment gives the states has varied, especially regarding the “interplay between the Commerce Clause and the Twenty-first Amendment.”<sup>81</sup> Two main approaches to interpreting Section 2 have developed: the “absolutist” approach and the “federalist” approach.<sup>82</sup> Absolutists argue that the “plain language of the Twenty-first Amendment vests complete control of regulation over intoxicating liquor to the states.”<sup>83</sup> Federalists, on the other hand, stress that the Twenty-first Amendment “does not vest in the states any new powers, but merely restores the status quo that existed prior to Prohibition.”<sup>84</sup> The Supreme Court has evolved from an absolutist stance, which was highly deferential to state liquor laws at the expense of other federal laws, to an approach closer to the federalist view. Today, the Court examines these liquor laws in relation to pertinent federal laws.<sup>85</sup>

### A. *Policy of Non-Interference*

The Twenty-first Amendment incited controversy not only from Prohibitionists, but also from those who believed that it conflicted with Congress’ power to regulate interstate commerce.<sup>86</sup> Beginning in the late 1930s, the Supreme Court made it clear that it would take a deferential approach to state laws that invoked the Twenty-first Amendment to regulate

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<sup>81</sup> Duncan Baird Douglass, *Constitutional Crossroads: Reconciling the Twenty-first Amendment and the Commerce Clause to Evaluate State Regulation of Interstate Commerce in Alcoholic Beverages*, 49 DUKE L.J. 1619, 1636-37 (2000). Douglass refers often to the intersection of the Twenty-first Amendment and the dormant Commerce Clause. *See generally id.* at 1624-38. However, as he points out, the dormant Commerce Clause is a negative implication of the affirmative powers that the Commerce Clause grants the states; they are therefore intertwined. *Id.* at 1624. For clarity and consistency, this note will refer to the Commerce Clause or commerce powers, rather than the dormant Commerce Clause.

<sup>82</sup> Silvernail, *supra* note 3, at 513 (internal quotation marks omitted).

<sup>83</sup> *Id.*

<sup>84</sup> *Id.*

<sup>85</sup> Douglass, *supra* note 81, at 1636-37.

<sup>86</sup> *See Norton, supra* note 71, at 1471; *compare* U.S. CONST. art. I, § 8, cl. 3 (“Congress shall have Power . . . To regulate Commerce . . . among the several States”) with U.S. CONST. amend. XXI, § 2 (“The transportation or importation into any State, Territory, or possession of the United States for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited” (emphasis added)).

alcoholic beverages.<sup>87</sup> In a series of cases following the Amendment's ratification, the Supreme Court solidly established its absolutist approach to interpretation, as it repeatedly found that state liquor laws were not constrained by other provisions of the Constitution.<sup>88</sup>

The Supreme Court's most extreme language regarding the extent of states' power to control liquor can be found in *Ziffrin, Inc. v. Reeves*.<sup>89</sup> In *Ziffrin*, an Indiana corporation contracted with Kentucky distillers to receive whiskey and then ship it to Chicago.<sup>90</sup> When Kentucky enacted a law prohibiting this type of arrangement and provided law enforcement with the authority to seize goods,<sup>91</sup> the Indiana corporation claimed that the law was unconstitutional because it violated the Commerce Clause.<sup>92</sup> In upholding the law, the Supreme Court explicitly held in favor of state regulation of liquor, stating "[t]he Twenty-first Amendment sanctions the right of a state to legislate concerning intoxicating liquors brought from without, *unfettered by the Commerce Clause.*" (emphasis added)<sup>93</sup> With limited exceptions,<sup>94</sup> the Court only

<sup>87</sup> See Norton, *supra* note 71, at 1471.

<sup>88</sup> See e.g., State Bd. of Equalization v. Young's Market, 299 U.S. 59 (1936) (holding that state liquor laws are not limited by the Commerce or Equal Protection Clauses), *adhered to by* Ziffrin v. Reeves, 308 U.S. 132 (1939); Indianapolis Brewing Co. v. Liquor Control Comm'n, 305 U.S. 391 (1939); Mahoney v. Joseph Triner Corp., 304 U.S. 401 (1938). Accord Douglass, *supra* note 81, at 1637-38; Spaeth, *supra* note 1, at 183-84.

<sup>89</sup> 308 U.S. 132 (1939).

<sup>90</sup> *Id.* at 133.

<sup>91</sup> *Id.* at 133-35.

<sup>92</sup> *Id.* at 137. The Indiana corporation also argued the law violated the Due Process and Equal Protection Clauses. *Id.*

<sup>93</sup> *Id.* at 138 (emphasis added).

<sup>94</sup> See Silvernail, *supra* note 3, at 517-19. Silvernail uses two cases that came about a decade after *Young's Market* to illustrate his theory that the Court began to "introduc[e] chips into the foundation upon which the absolutist interpretation of the Twenty-first Amendment is constructed." *Id.* at 519. First, Silvernail points to *United States v. Frankfort Distilleries*, 324 U.S. 293 (1945) as "the first case where the Supreme Court showed signs of reining in the broad sweeping powers it so readily bestowed upon the states in *Young's Market.*" Silvernail, *supra* note 3, at 518. *Frankfort Distilleries* was the first time the Court stated that the powers given to the states by the Twenty-first Amendment are qualified by federal powers. *Id.*; see also *Frankfort Distilleries*, 324 U.S. 293. Although the Court refused to ultimately decide whether the Sherman Act limits state powers enacted under the Twenty-first Amendment in an antitrust suit against Colorado liquor producers, wholesalers, and retailers, the Court stated:

Granting the state's full authority to determine the conditions upon which liquor can come into its territory and what will be done with it after it gets there, it does not follow from that fact that the United States is wholly without power to regulate the conduct of those who engage in interstate trade outside the jurisdiction of [the state whose law is at issue].

began to “retreat[] substantially” from this approach to state liquor laws in the 1960s and 1970s.<sup>95</sup>

### B. *Limiting the Scope of Section 2*

Upon brief review of the Supreme Court’s early Twenty-first Amendment jurisprudence, one would think that the Supreme Court had forgotten the importance of the Commerce Clause.<sup>96</sup> However, in the landmark case<sup>97</sup> of *Hostetter v. Idlewild Bon Voyage Liquor Corp.*,<sup>98</sup> the Supreme Court finally used the Commerce Clause to strike down a New York liquor law that prohibited transportation of alcohol within state borders, because the shipments at issue were merely passing through New York for delivery and use in a foreign country.<sup>99</sup> The Court emphasized that New York was not trying to prevent alcohol from being unlawfully diverted for use within the state,<sup>100</sup> perhaps indicating that the law would have been permissible had that been New York’s goal. In reaching its holding, the Court explained that “[b]oth the Twenty-first Amendment and the Commerce Clause are parts of the same Constitution. Like other provisions of the Constitution, each must be considered in the light of the other, and in the context of the issues and interests at stake in any concrete case.”<sup>101</sup> This

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*Frankfort Distilleries*, 324 U.S. at 299. The second case Silvernail uses to illustrate that the Court was “chip[ping] into” its absolutist foundation was *Nippert v. City of Richmond*, 327 U.S. 416 (1946). Silvernail, *supra* note 3, at 518-19. In *Nippert*, which was not a “Twenty-first Amendment [case],” the Supreme Court reiterated the strength of the federal government’s commerce powers, citing *Frankfort Distilleries* for its proposition that “even the commerce in intoxicating liquors, over which the Twenty-first Amendment gives the states the highest degree of control, is not altogether beyond the reach of the federal commerce power. . .” *Nippert* at 425 n.15.

<sup>95</sup> See Douglass, *supra* note 81, at 1638; see also Norton, *supra* note 71, at 1472.

<sup>96</sup> See *supra* note 93 and accompanying text.

<sup>97</sup> See Spaeth, *supra* note 1, at 185 (“The Court consummated its full retreat from earlier broad readings of [T]wenty-first [A]mendment power, in a pair of decisions handed down in 1964: *Hostetter v. Idlewild Bon Voyage Liquor Corp.* and *Department of Revenue v. James B. Beam Distilling Co.*”).

<sup>98</sup> 377 U.S. 324 (1964).

<sup>99</sup> *Id.* at 333-34.

<sup>100</sup> *Id.* at 333.

<sup>101</sup> *Id.* at 332. The Supreme Court also uttered the oft-repeated comment that

To draw a conclusion from [early Twenty-first Amendment jurisprudence after ratification] that the Twenty-first Amendment has somehow operated to “repeal” the Commerce Clause wherever regulation of intoxicating liquors is concerned would, however, be an absurd oversimplification. . . . Such a conclusion would be patently bizarre and is demonstrably incorrect.

*Id.* at 331-32.

decision marked a notable shift in the Supreme Court's approach to interpreting Section 2 of the Twenty-first Amendment. For the first time, the Court clearly asserted that the Commerce Clause could limit a state's liquor laws.<sup>102</sup>

After *Hostetter*, the Court continued its retreat from giving the states excessive discretion with respect to their liquor laws. For example, less than a decade later, the Court made clear that it would no longer give deference to state liquor laws at the expense of the Fourteenth Amendment.<sup>103</sup> These decisions paved the way for the Court to further restrict the over-broad scope it had originally given to Section 2.

C. *The Current Approach to Twenty-first Amendment Cases: The "Accommodation Doctrine"*<sup>104</sup>

Beginning in 1980, the Supreme Court began clearly articulating its new approach to overreaching state liquor regulations. In *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*,<sup>105</sup> the Court held that Section 2 of the Twenty-first Amendment did not save a California liquor law that violated the Sherman Act by imposing a resale price maintenance scheme on wholesale wine producers.<sup>106</sup> The Court claimed that it was following early Twenty-first Amendment jurisprudence by acknowledging the extensive authority that the Amendment gave to the states to regulate liquor.<sup>107</sup>

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<sup>102</sup> *Id.*; see also Douglass, *supra* note 81, at 1638.

<sup>103</sup> See *Craig v. Boren*, 429 U.S. 190, 210 (1976) (acknowledging again the states' broad powers over liquor under the Twenty-first Amendment but refusing to uphold a liquor law that violated the Equal Protection Clause of the Fourteenth Amendment); *Wisconsin v. Constantineau*, 400 U.S. 433, 436-37 (1971) (holding that while the states were given a broad grant of power to regulate liquor by the Twenty-first Amendment, a liquor law could not deprive a person of due process). The Court in *Craig* reaffirmed that "each provision [of the Constitution must] 'be considered in the light of the other . . .'" *Id.* at 206 (quoting *Hostetter*, 377 U.S. at 332); see also Silvernail, *supra* note 3, at 521.

<sup>104</sup> The Court's current approach of balancing state and federal interests when a state liquor regulation conflicts with a federal law that implicates the Commerce Power has come to be known as the "accommodation doctrine." See Silvernail, *supra* note 3, at 524 (internal quotation marks omitted); see also Elizabeth D. Lauzon, Annotation, *Interplay Between Twenty-first Amendment and Commerce Clause Concerning State Regulation of Intoxicating Liquors*, 116 A.L.R.5th 149 (2004).

<sup>105</sup> 445 U.S. 97 (1980). *Midcal* holds particular significance for this Note, as it provides the foundation for how to analyze whether a liquor law violates the Sherman Act and, if so, whether it is protected by the Twenty-first Amendment; therefore the case is relied upon by almost all of the subsequent cases on this issue. See *infra* Part III.

<sup>106</sup> *Midcal*, 445 U.S. at 113-14.

<sup>107</sup> *Id.* at 106-10.

Nonetheless, in stark contrast with those early cases, the Court refused to defer to a state law because it conflicted with a federal law enacted pursuant to the Commerce Power.<sup>108</sup> In reaching its decision, the Court relied on *Hostetter*'s suggestion that examining state liquor laws may call for balancing the state's interests with federal interests, but it went a step further by actually requiring this balancing approach "in appropriate situations."<sup>109</sup>

Taking an even larger step away from the early Twenty-first Amendment jurisprudence, in *Capital Cities Cable, Inc. v. Crisp*,<sup>110</sup> the Court expanded on both *Hostetter* and *Midcal* to set a new standard for state liquor regulations that conflict with federal laws.<sup>111</sup> *Capital Cities* stands for the proposition that courts presented with such a regulation must ask "whether the interests implicated by a state regulation are so closely related to the powers reserved by the Twenty-first Amendment that the regulation may prevail, notwithstanding that its requirements directly conflict with express federal policies."<sup>112</sup> In other words, the test to determine whether a state liquor law that conflicts with a federal law is valid is to ask whether the state law at issue directly serves the purposes of the Twenty-first Amendment,<sup>113</sup> and whether those interests outweigh the interests of the countervailing federal law.<sup>114</sup>

In another notable opinion, *Bacchus Imports, Ltd. v. Dias*,<sup>115</sup> not only did the Court affirm this *Capital Cities* standard, but it was quite dismissive of the earlier Twenty-first Amendment cases, referring to the legislative history of the Twenty-first Amendment as "obscur[e]."<sup>116</sup> Most shockingly, the Court declared, "[i]t is by now clear that the [Twenty-first]

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<sup>108</sup> *Id.*

<sup>109</sup> *Id.* at 110 ("[T]here is no bright line between federal and state powers over liquor. . . . Although States retain substantial discretion to establish other liquor regulations, those controls may be subject to the federal commerce power in appropriate situations. The competing state and federal interests can be reconciled only after careful scrutiny of those concerns in a 'concrete case.'").

<sup>110</sup> 467 U.S. 691 (1984).

<sup>111</sup> *Id.* at 711-14.

<sup>112</sup> *Id.* at 714.

<sup>113</sup> *Id.*

<sup>114</sup> See *Midcal*, 445 U.S. at 110; see *supra* notes 109, 112 and accompanying text.

<sup>115</sup> 468 U.S. 263 (1984).

<sup>116</sup> See *id.* at 274 ("Despite broad language in some of the opinions of this Court written shortly after ratification of the Amendment, more recently we have recognized the obscurity of the legislative history of § 2." (internal citations omitted)); see also Silvernail, *supra* note 3, at 525.

Amendment did not entirely remove state regulation of alcoholic beverages from the ambit of the Commerce Clause.”<sup>117</sup> Such a statement directly contradicted the Court’s language in *Ziffrin* that state liquor laws are “unfettered by the Commerce Clause.”<sup>118</sup> After *Bacchus Imports*, there could be no doubt that under the accommodation doctrine the Supreme Court would take a hard look at state liquor regulations that conflicted with federal laws.<sup>119</sup> Still, knowing that a court will give rigorous scrutiny to New York’s post and hold statute is barely scratching the surface of the type of analysis required to determine the validity of Section 101-b.

### III. THE TWENTY-FIRST AMENDMENT VS. THE SHERMAN ACT: WHEN A LIQUOR LAW IS SUBJECT TO AN ANTITRUST CHALLENGE

When a state’s liquor law is challenged on constitutional grounds, one of the most common reactions of that state is to use the Twenty-first Amendment as a defense.<sup>120</sup> The same is true when a liquor law is challenged as being in violation of the Sherman Act.<sup>121</sup> The Supreme Court will no longer give great deference to liquor laws that conflict with federal legislation, such as the Sherman Act, simply because the laws are claimed to have been enacted pursuant to the Twenty-first Amendment.<sup>122</sup> As a result, courts faced with determining the validity of such a law must perform an analysis that involves wading through complex issues of antitrust law and assessing the legitimacy of states’ claimed interests in order to ultimately decide whether a state has proven that it can properly rely on the Twenty-first Amendment to shield a state law that conflicts with federal law.

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<sup>117</sup> *Bacchus Imports*, 468 U.S. at 275.

<sup>118</sup> *Ziffrin, Inc. v. Reeves*, 308 U.S. 132, 138 (1939); see *supra* Part II.A.

<sup>119</sup> See *supra* note 104.

<sup>120</sup> See *e.g.*, *Cal. Retail Liquor Dealers Ass’n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 106 (1980); see also *Lauzon*, *supra* note 104 (explaining that under the accommodation doctrine, after a court finds that a state liquor regulation violates the Commerce Clause, the burden shifts to the state to show that the law at issue is saved by the Twenty-first Amendment).

<sup>121</sup> See, *e.g.*, *Midcal*, 445 U.S. at 106.

<sup>122</sup> See *supra* Part II.C.

A. *Assessing the Validity of Liquor Laws Challenged as Violations of the Sherman Act*

Section 101-b is a state liquor law and should be treated as other state liquor laws that have run up against the Sherman Act. The Supreme Court laid the foundation for an intricate three-part sequential test to determine whether a state's liquor regulation may be sustained when challenged as a violation of the Sherman Act.<sup>123</sup> First, a court must determine whether the regulation is preempted by the Sherman Act.<sup>124</sup> If the law does not violate the Sherman Act, then the challenger will clearly lose because the law has antitrust immunity.<sup>125</sup> However, if the court finds that the liquor regulation does indeed violate the Sherman Act, it must perform the second step of the three-part analysis and determine whether the law has antitrust immunity under the state-action doctrine.<sup>126</sup> The law will be sustained if the court finds that it has antitrust immunity.<sup>127</sup> If not, the third step in the analysis is to determine whether Section 2 of the Twenty-first Amendment will serve as a valid defense and save the law.<sup>128</sup> Each step in this three-part test is broken down further, and while the Supreme Court has yet to give clear guidance for how to apply the test in a given case, the federal courts have developed and applied this test to many state liquor regulations challenged on the grounds of violating the Sherman Act.<sup>129</sup>

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<sup>123</sup> *Midcal*, 445 U.S. at 102-06.

<sup>124</sup> *Id.* at 102. In striking down a California liquor regulation, the Supreme Court noted “[t]he threshold question is whether [the liquor regulation] . . . violates the Sherman Act.” *Id.*

<sup>125</sup> *Id.* at 102-03. For example, a unilateral restraint is not preempted by the Sherman Act, or in other words, has antitrust immunity. *See infra* Part III.A.1.

<sup>126</sup> *Midcal*, 445 U.S. at 103 (after finding that California's wine pricing scheme violated the Sherman Act, the Court then considered whether it was immune); *Parker v. Brown*, 317 U.S. 341, 368 (1943). The state-action doctrine is essentially a two-part test to determine whether the challenged liquor law should be treated as “state action,” and thus immune from the Sherman Act, despite the fact that private actors are involved in the law's enforcement. *See infra* Part III.A.2. The doctrine is intended to address the tension between serving the federal interests of the Sherman Act, e.g. promoting competition, and the rights of the states as sovereign entities. *See infra* Part III.A.2.

<sup>127</sup> *See supra* note 123 and accompanying text.

<sup>128</sup> *Midcal*, 445 U.S. at 106 (turning to an analysis of whether the Twenty-first Amendment served as a basis for upholding the challenged law after finding the law conflicted with the Sherman Act and had no antitrust immunity).

<sup>129</sup> *See infra* Part III.B.

### 1. Step One: Whether a State Liquor Law Is Preempted by the Sherman Act

As a threshold issue, a court must look at the challenged law to determine whether it conflicts with the Sherman Act.<sup>130</sup> Even this threshold issue is complex, requiring its own sequential two-step analysis.<sup>131</sup> Assume that the challenged law is a restraint of trade, in that it hampers free competition.<sup>132</sup> As discussed above, the Sherman Act prohibits agreements to engage in unreasonable restraints of trade.<sup>133</sup> Therefore, a court must determine two things: (1) whether the required element of agreement has been met; and (2) whether the restraint is unreasonable. Whether the first element, a finding of agreement, will be satisfied largely depends on whether the challenged law may be classified as a unilateral<sup>134</sup> or a hybrid<sup>135</sup> restraint.<sup>136</sup> If the restraint is deemed unilateral, then the law has antitrust immunity because it is a sovereign act by the state that the Sherman Act was not intended to prohibit.<sup>137</sup> If, however, the law is deemed a hybrid restraint, the court will proceed to the second step in the analysis: determining whether the restraint actually violates the Sherman Act.<sup>138</sup> Thus, applying the rule to Section 101-b, the two-step test for whether it conflicts with the Sherman Act consists of asking (1)

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<sup>130</sup> *Midcal* 445 U.S. at 102.

<sup>131</sup> See *TFWS, Inc. v. Schaefer*, 242 F.3d 198, 207 (4th Cir. 2001).

<sup>132</sup> See *supra* note 54 (defining restraint of trade).

<sup>133</sup> See *supra* Part I.B.

<sup>134</sup> A unilateral restraint is typically a state law, or governmental action, that forces private individuals to engage in anticompetitive behavior simply by complying with the law; there is no agreement among the individuals. See *infra* Part.III.A.1.a; see also *Fisher v. City of Berkeley*, 475 U.S. 260, 266-67 (1986) (finding a rent control ordinance to be a unilateral restraint and noting that the landlords whose prices were restricted by the ordinance had made no agreement to put a ceiling on rent prices); *Lopatka & Page, supra* note 54, at 273; A unilateral restraint is in direct contrast with a private restraint, in which private individuals agree to restrain trade, and there is no related governmental regulation shaping their behavior. See *id.* at 284-85.

<sup>135</sup> A hybrid restraint is not easily defined, but as a general matter involves a state regulation in which private individuals have some discretion as to whether they will comply with the regulation in a way that consists of anticompetitive behavior that would violate the Sherman Act, if not immune. See *infra* Part.III.A.1.a. In other words, hybrid restraints involve a mixture of government and private action. See *Lopatka & Page, supra* note 54, at 287.

<sup>136</sup> See *TFWS, Inc.*, 242 F.3d at 207 (describing this step in the analysis); see also *Lopatka & Page, supra* note 54, at 284-85.

<sup>137</sup> See *Parker v. Brown*, 317 U.S. 341, 352 (1943). The Sherman Act was intended to sanction private parties that agree to restrain trade, not to prevent states from taking affirmative action to regulate commerce. *Id.*

<sup>138</sup> See *TFWS, Inc.*, 242 F.3d at 207.

whether Section 101-b is a unilateral or hybrid restraint in order to find whether the element of agreement has been satisfied; and (2) if Section 101-b is a hybrid restraint, whether it constitutes an unreasonable restraint of trade.

*a. Step 1(a): Is There an Agreement?*

The Sherman Act expresses the concept of agreement as a “contract, combination . . . or conspiracy.”<sup>139</sup> However, as scholars have noted, “the meaning of agreement is . . . notoriously complex.”<sup>140</sup> Indeed, it has been argued that the term’s meaning varies depending on whether a restraint is characterized as unilateral or hybrid.<sup>141</sup> Since unilateral restraints are automatically immune from preemption by the Sherman Act,<sup>142</sup> the determination of whether a restraint is unilateral or hybrid may effectively result in the invalidation of a law.<sup>143</sup> Therefore, attempting to draw a line between the two categories is critical.

The distinction between unilateral and hybrid restraints of trade is not always clearly articulated by the courts.<sup>144</sup> What can be gleaned from the cases is that the less discretion private individuals have in affecting competition by complying with the law, the more likely it is that a court will find the law to be a unilateral restraint.<sup>145</sup> In contrast, the more discretion private market participants are given by the law, the more likely it is that a court will deem the law a hybrid restraint.<sup>146</sup> In other words, the restraint’s classification turns on the issue of control.

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<sup>139</sup> 15 U.S.C. § 1; Lopatka & Page, *supra* note 54, at 271.

<sup>140</sup> Lopatka & Page, *supra* note 54, at 288 (“[Agreement] is a term of art whose peculiar contours vary with the Court’s understanding of a particular restraint’s likely competitive effects.”).

<sup>141</sup> *See id.* at 297 (“[T]he definition of agreement in the context of hybrid restraints differs from the definition of agreement in the contexts of private restraints and purely governmental restraints.”).

<sup>142</sup> *See supra* note 137 and accompanying text.

<sup>143</sup> Lopatka & Page, *supra* note 54, at 272.

<sup>144</sup> *See id.* at 269 (stating “the Supreme Court’s precedents are not entirely consistent” in distinguishing between unilateral and hybrid restraints).

<sup>145</sup> *Id.* at 283-84.

<sup>146</sup> Looking forward briefly, a hybrid restraint of trade that conflicts with the Sherman Act may fail to qualify as immune under the state action doctrine. There are several steps before declaring that a challenged law is not immune. However, a law deemed to be a unilateral restraint escapes the lengthy scrutiny that a hybrid restraint will receive, especially if that hybrid restraint is deemed a per se violation of the Sherman Act. *See infra* notes 167-71 and accompanying text.

While unilateral restraints take away private control over competitive decision-making, hybrid restraints allow private individuals to retain at least some degree of control. For example, in *Fisher v. City of Berkeley*, the Supreme Court declared that Berkeley's Rent Control Ordinance setting maximum rent prices that landlords could charge was a unilateral restraint because the Ordinance removed price-setting control from the landlords and gave it to the City.<sup>147</sup> The Court went on to characterize hybrid restraints as using "nonmarket mechanisms [to] merely enforce private marketing decisions," stating that "the regulatory scheme may be attacked" when "private actors" are given "a degree of private regulatory power."<sup>148</sup> The *Fisher* Court took the concept of "hybrid restraints" from a concurrence in an earlier case;<sup>149</sup> the Court then used two cases to illustrate the concept.<sup>150</sup> Although the opinions in those cases did not reference hybrid restraints, they nonetheless serve as guidance since the Court has clearly pointed to them (albeit ex post) as examples of hybrid restraints.

First, the Court in *Fisher* pointed to *Schwegmann Bros. v. Calvert Distillers Corp.*,<sup>151</sup> in which the Court had struck down a Louisiana statute authorizing distributors to enter resale price contracts with retailers selling their products and to enforce those price-fixing agreements against not only those retailers, but other retailers selling the distributors' products who were not party to the price-fixing agreement.<sup>152</sup> The Court

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<sup>147</sup> *Fisher v. City of Berkeley*, 475 U.S. 260, 269 (1986) (stating the Ordinance "place[d] complete control over maximum rent levels exclusively in the hands of the Rent Stabilization Board. Not just the controls themselves but also the rent ceilings they mandate have been unilaterally imposed on the landlords by the city."). Similarly, the First Circuit compared a Massachusetts law limiting liquor storeowners to a maximum of three liquor store licenses to the Rent Control Ordinance in *Fisher*, because it did not give any control over competitive decision-making to private individuals. See *Mass. Food Ass'n v. Mass. Alcoholic Beverages Control Comm'n*, 197 F.3d 560, 565-66 (1st Cir. 1999) (in finding that the law at issue was not preempted by the Sherman Act, the court stated "[t]he Massachusetts statute . . . does not authorize or direct any private agreements or permit any competitor to determine the price or location of another. . . . As in *Fisher*, the restrictions have been 'unilaterally imposed by government . . . to the exclusion of private control.'" (quoting *Fisher*, 475 U.S. at 266)).

<sup>148</sup> *Fisher*, 475 U.S. at 267-68 (internal quotation marks omitted).

<sup>149</sup> *Id.* (citing *Rice v. Norman Williams*, 458 U.S. 654, 665 (1982) (Stevens, J., concurring)).

<sup>150</sup> See *Fisher*, 475 U.S. at 268.

<sup>151</sup> 341 U.S. 384 (1951).

<sup>152</sup> *Schwegmann Bros. v. Calvert Distillers Corp.*, 341 U.S. 384, 395 (1951). At the time this Louisiana statute was in effect, the Miller-Tydings Act amended Section 1 of the Sherman Act to allow agreements setting minimum resale prices for certain commodities in intrastate transactions; that Act is now repealed. 15 U.S.C. § 1,

in *Fisher* distinguished the Rent Control Ordinance, pursuant to which Berkeley set maximum rents, from the Louisiana law that allowed the distributors to set minimum resale prices, thus leaving some control in the hands of private individuals.<sup>153</sup> Next, the *Fisher* Court referred to *Midcal*.<sup>154</sup> According to the *Fisher* Court, the resale price maintenance scheme in *Midcal* was a hybrid restraint because “[t]he trade restraint condemned in *Midcal* entailed a similar degree of free participation by private economic actors.”<sup>155</sup>

Even if *Schwegmann Bros.* and *Midcal* were not decided based on the concept of “hybrid restraints,” the Supreme Court has come to rely on them as examples of the concept, stressing that each case turned on the fact that private individuals had discretion to affect competition, and their decisions would be enforced by the state.<sup>156</sup> In particular, both *Schwegmann Bros.* and *Midcal* dealt with price restraints, and the *Fisher* Court stressed the importance of the fact that the private market participants were the ones setting prices rather than the state, which merely enforced them.<sup>157</sup> This seems to indicate that where a law authorizes price restraints, and the state does not set the prices itself as it did in *Fisher*, it is especially prone to being characterized as a hybrid restraint. Assuming that the challenged law is found to be a hybrid restraint, the element of agreement has been satisfied and the next step in the analysis is to assess whether the restraint is a violation of the Sherman Act.<sup>158</sup>

*b. Step 1(b): Is There a Violation of the Sherman Act?*

As noted above, the Sherman Act only prohibits *unreasonable* restraints of trade.<sup>159</sup> Of course, a state would

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Amendments (showing enactment of 50 Stat. 693 (1937), and its repeal, 89 Stat. 801 (1975)).

<sup>153</sup> See *Fisher*, 475 U.S. at 268-69.

<sup>154</sup> See *supra* notes 105-109 and accompanying text.

<sup>155</sup> *Fisher*, 475 U.S. at 268.

<sup>156</sup> See, e.g., *id.*

<sup>157</sup> *Id.* at 268-69.

<sup>158</sup> See *supra* note 138 and accompanying text. It may seem counterintuitive, if not unjust, to find an illegal agreement under Section 1 of the Sherman Act where individuals are complying with a state liquor law *without actually agreeing to restrain trade*. However, the Supreme Court has affirmatively stated that a violation of the Sherman Act may be found *in the absence of private agreement* if the state compels activity that would otherwise be a per se violation. *324 Liquor Corp. v. Duffy*, 479 U.S. 335, 345 (1987).

<sup>159</sup> See *supra* Part I.B.

prefer that a law be deemed a unilateral restraint and therefore not subject to Sherman Act preemption.<sup>160</sup> Even if the restraint is hybrid, though, the state will still have the opportunity to show that the restraint is not unreasonable.<sup>161</sup> Post and hold statutes, like other price restraints, have generally been treated as per se violations.<sup>162</sup> A state statute is a per se violation of the Sherman Act if it “mandates or authorizes conduct that necessarily constitutes a violation of the antitrust laws in all cases, or if it places irresistible pressure on a private party to violate the antitrust laws in order to comply with the statute.”<sup>163</sup> If, as in the cases involving “post and hold” statutes, the restraint does violate the Sherman Act,<sup>164</sup> the court must then determine whether the law is immune under the state-action doctrine espoused by *Parker v. Brown*.<sup>165</sup> Considering the treatment of other post and hold liquor laws,<sup>166</sup> Section 101-b should certainly reach this level of analysis.

## 2. Step Two: State-Action Doctrine

Assuming that Section 101-b of the ABC Law is deemed a hybrid price restraint that violates the Sherman Act, New York would certainly argue that it is entitled to antitrust immunity under the state-action doctrine. The state-action doctrine originated in *Parker*, where the Supreme Court pointed out that the Sherman Act was not intended to prohibit the states from taking affirmative action that restrains competition.<sup>167</sup> Unilateral restraints are not subject to the scrutiny that hybrid restraints receive because unilateral restraints qualify as this type of affirmative state action.<sup>168</sup> Although hybrid restraints do not automatically qualify for

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<sup>160</sup> See *supra* note 137 and accompanying text.

<sup>161</sup> See *supra* Part I.B. Determining whether a restraint violates the Sherman Act is typically fact-specific, but it can be superficially described as two basic approaches. While some restraints of trade are per se unreasonable, and thus in conflict with the Sherman Act without further analysis, other restraints are assessed under the “rule of reason,” which essentially consists of determining whether a restraint is reasonable in light of the circumstances. See *id.*

<sup>162</sup> See *infra* Part III.B.

<sup>163</sup> *Rice v. Norman Williams Co.*, 458 U.S. 654, 661 (1982).

<sup>164</sup> See *infra* Part III.B.

<sup>165</sup> 317 U.S. 341 (1943) (finding California’s regulation of the state’s 1940 raisin crop to be proper regulation of state industry not interfering with federal commerce powers).

<sup>166</sup> See *infra* Part III.B.

<sup>167</sup> *Parker v. Brown*, 317 U.S. 341, 352 (1943).

<sup>168</sup> See *supra* note 137 and accompanying text.

such immunity, the Supreme Court in *Midcal* held that a hybrid restraint will be immune from the Sherman Act under *Parker's* state-action doctrine if it satisfies two requirements.<sup>169</sup> First, the restraint must be “clearly articulated and affirmatively expressed as state policy.”<sup>170</sup> Second, the restraint must be “actively supervised by the State itself.”<sup>171</sup>

*a. Step 2(a): Is the Restraint Clearly Articulated and Affirmatively Expressed as State Policy?*

The first hurdle of *Midcal*, i.e., whether the state has “clearly articulated and affirmatively expressed [the restraint] as state policy,” has typically been overcome.<sup>172</sup> This makes sense considering that the state does not have to do much to satisfy the standard. For example, in *Midcal*, the Court said that the California wine-pricing scheme (already deemed a hybrid restraint) satisfied the first prong of the immunity test because “[t]he legislative policy [was] forthrightly stated and clear in its purpose to permit resale price maintenance.”<sup>173</sup> So long as the legislature makes its intent to displace competition clear, the first prong will most likely be satisfied.<sup>174</sup>

*b. Step 2(b): Is the Restraint Actively Supervised by the State Itself?*

It is the second *Midcal* prong that has more often prevented a challenged restraint from establishing immunity.<sup>175</sup> In *Midcal*, the Supreme Court struck down California’s wine-pricing scheme because it was not actively supervised by the

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<sup>169</sup> Cal. Retail Liquor Dealers Ass’n v. Midcal Aluminum, Inc., 445 U.S. 97, 105 (1980).

<sup>170</sup> *Id.* (internal quotation marks omitted).

<sup>171</sup> *Id.* (internal quotation marks omitted).

<sup>172</sup> *Id.* (internal quotation marks omitted). See generally *Costco Wholesale Corp. v. Maleng*, 522 F.3d 874, 902 (9th Cir. 2008); *TFWS, Inc. v. Schaefer*, 242 F.3d 198, 210-11 (4th Cir. 2001).

<sup>173</sup> *Midcal*, 445 U.S. at 105.

<sup>174</sup> But see *Freedom Holdings, Inc. v. Spitzer*, 357 F.3d 205, 230 (2d Cir. 2004) (finding that New York’s Contraband Statutes failed prong one of *Midcal* because the state’s articulated interest in using them as a method of revenue production was not legitimate); *infra* notes 286-288 and accompanying text. The Supreme Court has not spoken on the issue, but if the Second Circuit’s approach is correct, then a clearly stated intent to displace competition may nonetheless fail to satisfy *Midcal*’s first prong if the court finds the policy behind the intent illegitimate.

<sup>175</sup> *Midcal*, 445 U.S. at 105-06; see *Costco Wholesale Corp.* 522 F.3d at 902-03; *TFWS, Inc.*, 242 F.3d at 210-11.

state, stating in a frequently-quoted phrase that “[t]he State neither establishes prices nor reviews the reasonableness of the price schedules . . . . [t]he State does not monitor market conditions or engage in any ‘pointed reexamination’ of the program.”<sup>176</sup> In striking down New York ABC Law § 101-bb, a “markup” statute, the Court similarly found a lack of active supervision.<sup>177</sup> Rather, “[t]he State ha[d] displaced competition among liquor retailers without substituting an adequate system of regulation.”<sup>178</sup> The Supreme Court seems to have established two ways for a state to protect an anticompetitive liquor regulation. If the regulation allows private individuals to set prices, i.e., gives private individuals discretion or control over prices, the state must have a system in place to ensure that these prices are reasonable.<sup>179</sup> Alternatively, the consequences of allowing individuals to set prices must be reasonable.<sup>180</sup> If the state is unable to show reasonableness, the restraint will not be immune, and the state must then rely on the Twenty-first Amendment’s grant of power for redemption.

### 3. Step Three: The Twenty-first Amendment Defense

After a state law is deemed a hybrid restraint and fails to obtain antitrust immunity, the Twenty-first Amendment is the final obstacle to invalidation,<sup>181</sup> or in other words, Section 101-b’s last resort for protection. The courts have developed yet another two-part test for determining whether the Twenty-first

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<sup>176</sup> *Midcal*, 445 U.S. 97, 105-06 (1980) (after finding the scheme to be a hybrid restraint preempted by the Sherman Act). *See, e.g., Costco Wholesale Corp.*, 522 F.3d at 889 (quoting *Midcal*); *Miller v. Hedlund*, 813 F.2d 1344, 1351 (9th Cir. 1987) (quoting *Midcal*).

<sup>177</sup> New York ABC Law section 101-bb required retailers to “markup” the “posted” wholesale price for liquor by 112 percent (but allowed wholesalers to sell to retailers at less than the “posted” price). *324 Liquor Corp. v. Duffy*, 479 U.S. 335, 335, 337 (1987).

<sup>178</sup> *Id.* at 344-45.

<sup>179</sup> *See, e.g., 324 Liquor*, 479 U.S. at 344-45; *Midcal*, 445 U.S. at 105-06.

<sup>180</sup> The Court has indicated that it is worried about state authorization of private price-fixing that essentially fosters cartelization, with no check on the individual market participants’ power. *See 324 Liquor*, 479 U.S. at 342 (discussing the possibility that “industrywide resale price maintenance . . . may facilitate cartelization”); *Midcal*, 445 U.S. at 106 (“The national policy in favor of competition cannot be thwarted by casting such a gauzy cloak of state involvement over what is essentially a private price-fixing arrangement.”). While the Court expresses its concerns, it does not elaborate as to what kinds of consequences would be considered reasonable, and neither do the federal courts applying the Supreme Court’s jurisprudence in this area.

<sup>181</sup> *See Midcal*, 445 U.S. at 106.

Amendment serves as a valid defense to a restraint that violates the Sherman Act.<sup>182</sup> First, the restraint must be intended to serve a legitimate state policy.<sup>183</sup> Second, the state must show that the restraint “substantiates” that policy.<sup>184</sup> At this point, under the accommodation approach,<sup>185</sup> the Twenty-first Amendment will only protect a challenged restraint if it directly serves the policies of the Amendment and those policies outweigh the goals of the Sherman Act.<sup>186</sup> If the restraint can pass this final test, it will have survived its antitrust challenge.<sup>187</sup>

*a. Step 3(a): Was the Restraint Intended to Serve a Legitimate State Policy?*

Even if Section 101-b purports to serve legitimate state concerns, it will not necessarily be saved by the Twenty-first Amendment. In essence, there must be a balancing of a state’s legitimate interests and the federal interest in the Sherman Act.<sup>188</sup> For example, in *Bacchus Imports*, the Supreme Court refused to uphold a discriminatory state liquor tax because it “was [not] designed to promote temperance or carry out any other purpose of the Twenty-first Amendment.”<sup>189</sup> While *Bacchus* involved a challenge based on discrimination in violation of the Commerce Clause as opposed to an antitrust challenge, it is the clearest statement of the type of reasoning that has been applied in the liquor antitrust cases.<sup>190</sup> Specifically, if a state liquor law does not promote the goals of the Twenty-first Amendment, it will be invalidated.

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<sup>182</sup> Both prongs must be satisfied for the restraint to survive an antitrust challenge. *Id.* at 113-14.

<sup>183</sup> *See id.*

<sup>184</sup> *Id.* The word “substantiate” appears to be used as a term of art by the Supreme Court and the federal courts to assess whether the restraint at issue effectuates the policy asserted in support of it. For consistency, this Note will use this term as well with the same intended meaning.

<sup>185</sup> *See supra* Part II.C.

<sup>186</sup> *See supra* note 114 and accompanying text. The goals of the Sherman Act are fairness among producers, economic efficiency, and consumer welfare. *See supra* note 53 and accompanying text.

<sup>187</sup> *See supra* notes 123-128 and accompanying text.

<sup>188</sup> *See, e.g., Midcal*, 445 U.S. at 108-14.

<sup>189</sup> *Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263, 276 (1984); *see Douglass, supra* note 81, at 1641-42.

<sup>190</sup> *See, e.g., 324 Liquor Corp. v. Duffy*, 479 U.S. 335, 347-49 (1987); *Midcal*, 445 U.S. at 113-14.

Therefore, in order to serve a legitimate state policy, the restraint must be based on a concern that relates directly to the Twenty-first Amendment, *and* that concern must outweigh the federal interests served by the Sherman Act.<sup>191</sup> So far, legitimate state interests have included temperance and protecting small retailers.<sup>192</sup> Economic protectionism is an example of a state interest that is *not* legitimate because it is not a “core concern[]” of the Twenty-first Amendment.<sup>193</sup> The fact that a restraint purports to serve legitimate state interests, however, will not be enough to save the restraint if it is not *effectively* serving those interests.<sup>194</sup>

*b. Step 3(b): Does the Restraint Substantiate the State’s Legitimate Concerns?*

If a court finds that Section 101-b serves clearly articulated interests that are expressed as state policies, and those interests outweigh the interests of the Sherman Act, the court will have one final inquiry before it may declare Section 101-b valid. The Supreme Court has held that “*unsubstantiated* state concerns . . . simply are not of the same stature as the goals of the Sherman Act.”<sup>195</sup> Courts have repeatedly struck down restraints that were put into place to serve legitimate interests for failing to actually promote these interests.<sup>196</sup> For example, in *324 Liquor Corp. v. Duffy*,<sup>197</sup> the Court acknowledged the legitimacy of New York’s desire to protect small retail establishments, but struck down the state’s “markup” statute because the state failed to show that the restraint helped those retailers.<sup>198</sup> The Court went even further than this, however, by pointing out that the *Midcal* Court had cited evidence showing that other states with similar laws had experienced increased failure of firms and decreased growth of small retail establishments.<sup>199</sup> While the Supreme Court has not stated a clear rule for when an interest is substantiated, it has

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<sup>191</sup> See *supra* note 115 and accompanying text.

<sup>192</sup> See *Midcal*, 445 U.S. at 113-14.

<sup>193</sup> Lauzon, *supra* note 104.

<sup>194</sup> See *Midcal* 445 U.S. at 113.

<sup>195</sup> *Id.* (emphasis added).

<sup>196</sup> See, e.g., *324 Liquor Corp.*, 479 U.S. 335, 350 (1987); *Midcal*, 445 U.S. at 113-14.

<sup>197</sup> 479 U.S. 335 (1987).

<sup>198</sup> *Id.* at 350.

<sup>199</sup> *Id.*

clearly shown that it is willing to not only require empirical evidence from the state but that it will also look at evidence to the contrary.<sup>200</sup> This type of approach is a far cry from the original deference applied to state liquor laws.<sup>201</sup>

*B. Post and Hold Cases Challenged as Violations of the Sherman Act*

There have been several “post and hold” cases in the federal courts since the Supreme Court’s decision in *Midcal*, which can be considered the most instructive case for analyzing whether a liquor law that is challenged as preempted by the Sherman Act may be saved by the Twenty-first Amendment. With one exception, each time a federal circuit has considered the validity of a post and hold law, it has found that it was preempted by the Sherman Act,<sup>202</sup> did not qualify for antitrust immunity under *Parker*,<sup>203</sup> and was not saved by the Twenty-first Amendment because the law’s purported goals were not substantiated.<sup>204</sup> These cases illustrate the analysis outlined above and are indicative of how a court will treat ABC Law Section 101-b.

Each of the cases discussed in this section involved restraints considered “post and hold” laws, like ABC Law Section 101-b.<sup>205</sup> The only case in which a federal circuit upheld a challenged post and hold restraint was *Battipaglia v. New York State Liquor Authority*,<sup>206</sup> decided twenty-four years ago. The challenged restraint addressed by the Second Circuit in *Battipaglia* was none other than ABC Law Section 101-b.<sup>207</sup> The majority held that Section 101-b did not violate the Sherman Act, and alternatively that if it did violate the Sherman Act, it was entitled to prevail because of the Twenty-first

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<sup>200</sup> *Id.*

<sup>201</sup> *See supra* Part II.A.

<sup>202</sup> *See Costco Wholesale Corp. v. Maleng*, 522 F.3d 874, 895-96 (9th Cir. 2008); *TFWS, Inc. v. Schaefer*, 242 F.3d 198, 209-10 (4th Cir. 2001); *Miller v. Hedlund*, 813 F.2d 1344, 1349-50 (9th Cir. 1987).

<sup>203</sup> *See TFWS, Inc.*, 242 F.3d at 211; *Miller*, 813 F.2d at 1351-52; *see infra* notes 254-255 and accompanying text.

<sup>204</sup> *See infra* notes 256-259 and accompanying text. Two of the cases, *Miller v. Hedlund* and *TFWS, Inc. v. Schaefer* were remanded on this issue and in both instances, the post and hold laws ultimately were struck down for failing to substantiate the states’ interests. *See infra* notes 229-233, 243-247 and accompanying text.

<sup>205</sup> *See supra* Part I.C. for a reminder of what Section 101-b requires.

<sup>206</sup> 745 F.2d 166 (2d Cir. 1984).

<sup>207</sup> *Id.* at 167.

Amendment.<sup>208</sup> First, the court distinguished *Midcal*, claiming that *Midcal* involved a “resale price maintenance” scheme in which wine producers could dictate prices charged by downstream sellers,<sup>209</sup> and thus was not dispositive because New York “merely requires wholesalers to post and adhere to their own unilaterally determined prices and nothing more.”<sup>210</sup> The majority noted that courts had disagreed over whether compliance with a state law could be grounds for the finding of “agreement” as required by the Sherman Act, but declined to choose a side.<sup>211</sup> Instead, the court held that there was no preemption because this was a facial attack, which required proof that Section 101-b was a per se violation of the Sherman Act in all instances.<sup>212</sup> Section 101-b was characterized as the “exchange of specific information,” an activity that should be subject to the rule of reason<sup>213</sup> antitrust analysis, rather than be deemed a per se violation.<sup>214</sup> The majority then found that even if Section 101-b violated the Sherman Act, it should prevail anyway because it was intended to serve a strong state interest in preventing price discrimination, and the state had not intended to reduce competition.<sup>215</sup>

In response to the majority in *Battipaglia*, Judge Winter, in dissent, argued that Section 101-b is a per se violation of the Sherman Act. Under Judge Winter’s analysis, not only does Section 101-b contemplate the exchange of price information, but it also requires adherence to publicly announced prices, which was always held to be illegal irrespective of reasonableness.<sup>216</sup> Judge Winter then went on to opine that the element of “agreement” should be found because *Midcal* does

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<sup>208</sup> *Id.* at 170. The majority declined to answer whether Section 101-b would be immune under the state-action doctrine. *Id.*

<sup>209</sup> *Id.* at 172; see also *supra* note 56 and accompanying text.

<sup>210</sup> *Battipaglia*, 745 F.2d at 172.

<sup>211</sup> *Id.* at 173 (internal quotation marks omitted). However, the court commented that “state compulsion of individual action is the very antithesis of an agreement.” *Id.*

<sup>212</sup> *Id.* at 174-75.

<sup>213</sup> See *supra* note 66 (explaining that not all anticompetitive activity results in a per se violation of the Sherman Act).

<sup>214</sup> *Battipaglia*, 745 F.2d at 175.

<sup>215</sup> *Id.* at 178-79. The court noted that Section 101-b could create disincentives to reducing prices, but that the plaintiffs challenging the law had not argued this or provided any evidence that it was occurring. *Id.* at 178.

<sup>216</sup> *Id.* at 179 (Winter, J., dissenting).

apply to Section 101-b, contrary to what the majority reasoned.<sup>217</sup> After determining that Section 101-b was thus preempted by the Sherman Act, Judge Winter found that while the intentions of New York were clearly stated and affirmatively expressed, as required by *Midcal*'s first prong, Section 101-b was not immune under the state-action doctrine because New York does not actively supervise whether Section 101-b carries out its intended policies.<sup>218</sup> In concluding, Judge Winter commented that temperance would be a valid interest under the Twenty-first Amendment but that the Amendment should not apply in the case before the court because, in his opinion, the law was intended to allow liquor dealers to "seek out their profit-maximizing price/output level[s]."<sup>219</sup> Accordingly, he did not address whether Section 101-b substantiated the state's purported interest in preventing price discrimination.<sup>220</sup>

A few years after *Battipaglia* came *Miller v. Hedlund*,<sup>221</sup> in which the Ninth Circuit Court of Appeals found that several features of Oregon's liquor distribution regime violated the Sherman Act.<sup>222</sup> The problematic provisions included: a requirement to post future prices at least ten days before the prices were to go into effect, a requirement that permissible price decreases remain in effect for a specified period, and a requirement that the posted price not be increased because of transportation costs.<sup>223</sup> In essence, this was a post and hold regime because of the requirements to post resale prices in advance and adhere to those prices. In considering whether the regulations violated the Sherman Act, the court relied on *Schwegmann* and *Midcal* to find that they constituted hybrid restraints.<sup>224</sup> After determining that they were also per se violations of the Act because "[a]n agreement to adhere to

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<sup>217</sup> *Id.* In essence, Judge Winter determined that this was a hybrid restraint, although he did not use the language. *See id.* (explaining that Section 101-b contemplated a combination of state and private action).

<sup>218</sup> *Battipaglia*, 745 F.2d at 180 (Winter, J., dissenting). Judge Winter stated that New York does not set the prices, review them for reasonableness, monitor the liquor industry's market conditions, or review the scheme. *Id.* He quoted *Midcal*: "the national policy in favor of competition is thwarted by casting a . . . gauzy cloak of state involvement over what is essentially a private price-fixing agreement." *Id.* (quoting *Cal. Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 106 (1980)).

<sup>219</sup> *Battipaglia*, 745 F.2d at 180 (Winter, J., dissenting).

<sup>220</sup> *Id.*

<sup>221</sup> 813 F.2d 1344 (9th Cir. 1987).

<sup>222</sup> *Id.* at 1351.

<sup>223</sup> *Id.* at 1347. Oregon's ban on volume discounts was also challenged, but not at issue on appeal. *Id.* at 1348 n.3.

<sup>224</sup> *Miller*, 813 F.2d at 1350-51.

previously announced prices . . . is unlawful per se under the Sherman Act,”<sup>225</sup> the court proceeded to apply the test for *Parker’s* state-action immunity.<sup>226</sup> Again, the court relied on *Midcal* and denied immunity to the regulations, stating that Oregon failed to actively supervise them.<sup>227</sup> Specifically, the court noted that Oregon neither set the prices nor determined their reasonableness.<sup>228</sup> Finally, the court considered the state’s Twenty-first Amendment defense, stressed the importance of balancing the state’s claimed interests served by these regulations against the Sherman Act’s interests in fostering competition, and ultimately remanded because the factual record had not been developed on this issue.<sup>229</sup>

In the case’s conclusion, the District Court of Oregon assessed the state’s purported interests in the price posting regime, asking whether the regime in fact substantiated those interests.<sup>230</sup> Oregon argued that its intent was to prevent price discrimination.<sup>231</sup> However, the court found that there was no evidence that price posting helped the state identify instances of price discrimination; instead, the court found that the price posting laws “authoriz[ed], facilitat[ed], and induc[ed] horizontal price fixing.”<sup>232</sup> Consequently, Oregon was enjoined from enforcing its post and hold laws since they were not shielded by the Twenty-first Amendment.<sup>233</sup>

About a decade later, another post and hold case was decided, this time in Maryland. In *TFWS, Inc. v. Schaefer*,<sup>234</sup> the owner of a large retail liquor store in Maryland sued the State Comptroller on the grounds that the state’s liquor regulatory scheme, which required liquor wholesalers to file price schedules with the state and adhere to those prices for at least

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<sup>225</sup> *Id.* at 1349. The Supreme Court held in *324 Liquor* that a per se violation may be found in the absence of a private agreement if the state compels activity that would be a per se violation. *324 Liquor Corp. v. Duffy*, 479 U.S. 335, 345-46 (1987). In other words, the concept of agreement is treated differently for hybrid restraints in that the individuals complying with the law do not actually have to agree to fix prices in the normal sense of the word “agree.” See *supra* note 141; see generally *supra* Part III.A.1.a.

<sup>226</sup> *Miller*, 813 F.2d at 1351-52.

<sup>227</sup> *Id.* at 1351-52.

<sup>228</sup> *Id.* at 1351-52 n.6.

<sup>229</sup> *Id.* at 1352.

<sup>230</sup> See generally *Miller v. Hedlund*, 717 F. Supp. 711 (D. Or. 1989).

<sup>231</sup> *Id.* at 712.

<sup>232</sup> *Id.* at 715-16.

<sup>233</sup> *Id.* at 716.

<sup>234</sup> 242 F.3d 198 (4th Cir. 2001).

a month after posting, violated the Sherman Act.<sup>235</sup> The Fourth Circuit Court of Appeals first declared that “[t]he post-and-hold system is a classic hybrid restraint”<sup>236</sup> because it requires private parties (wholesalers) to set prices, which are not reviewed for reasonableness, thus giving those parties a great deal of “private regulatory power.”<sup>237</sup> Next, the court relied on *Miller’s* analysis to hold that the law was a per se violation of the Sherman Act.<sup>238</sup> The court explained that the post and hold regime “mandate[d] activity that is essentially a form of horizontal price fixing, which has been called ‘the paradigm of an unreasonable restraint of trade.’”<sup>239</sup> Maryland, like Oregon, was unable to establish state-action immunity for the post and hold laws, with the court relying on *Midcal*<sup>240</sup> and *324 Liquor*<sup>241</sup> to explain that the state failed to set prices, review the privately-set prices for reasonableness, monitor market conditions in the liquor industry, or “engage in any ‘pointed reexamination’ of the [post and hold regime].”<sup>242</sup>

With respect to Maryland’s Twenty-first Amendment defense, the Fourth Circuit remanded the case to develop the record, in order to determine whether the post and hold pricing scheme substantiated Maryland’s avowed interest in promoting

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<sup>235</sup> *Id.* at 201-02. Also at issue in the case was a ban on volume discounts, which the Court struck down. *See id.* at 202, 210. New York law also bans volume discounts, N.Y. ALCO. BEV. CONT. LAW § 101-b(2)(a), and it is reasonable to believe that this would be struck down as well, based on the reasoning that applies to the post and hold law. *See infra* note 237.

<sup>236</sup> *TFWS Inc.*, 242 F.3d at 208.

<sup>237</sup> *Id.* at 208-09. The Court also noted that “[t]he volume discount ban is a part of the hybrid restraint because it reinforces the post-and-hold system by making it even more inflexible.” *Id.* at 209. The court later went on to hold that the volume discount ban was also a per se violation of the Sherman Act. *Id.* at 210.

<sup>238</sup> *Id.* at 209-10. The Court commented that “[s]everal district courts have reached the same result,” citing *Beer & Pop Warehouse v. Jones*, 41 F. Supp. 2d 552, 560-62 (M.D. Pa. 1999) (“holding that Pennsylvania post-and-hold pricing statute for beer was a per se violation of the Sherman Act”) and *Canterbury Liquors & Pantry v. Sullivan*, 16 F. Supp. 2d 41, 47-48 (D. Mass. 1998) (“holding that Massachusetts post-and-hold liquor pricing scheme was a per se violation of § 1 [of the Sherman Act]”). *Id.* at 210. The court acknowledged *Battipaglia’s* approach, see *supra* notes 206-215 and accompanying text, and then declined to follow, saying that no other court has followed it and a “leading commentator on antitrust law” had agreed with Judge Winter. *TFWS Inc.*, 242 F.3d at 210; *supra* note 216 and accompanying text.

<sup>239</sup> *TFWS*, 242 F.3d at 209 (quoting *N.C.A.A. v. Bd. of Regents of the Univ. of Okla.*, 468 U.S. 85, 100 (1984)).

<sup>240</sup> *See supra* notes 176-179 and accompanying text.

<sup>241</sup> *See supra* notes 176-179 and accompanying text.

<sup>242</sup> *TFWS, Inc.*, 242 F.3d at 211 (internal citation omitted) (quoting *324 Liquor Corp. v. Duffy*, 479 U.S. 335, 344-45 (1987)).

temperance.<sup>243</sup> The case went through several stages in both the district court and back up to the Fourth Circuit before it was finally resolved in 2007, in favor of TFWS (the liquor storeowner).<sup>244</sup> After extensive evidentiary findings (and disputes) involving expert testimony on both theoretical and empirical studies<sup>245</sup> the district court determined that the state's evidence that the scheme promoted temperance was tenuous, and thus outweighed by the federal interest in fostering competition.<sup>246</sup> In other words, Maryland was unable to save its post and hold laws because although it had a valid interest in promoting temperance, that interest was not substantiated, as required by *Midcal* and *324 Liquor*.<sup>247</sup>

The most recent federal decision to find that a post and hold law violated the Sherman Act was in the Ninth Circuit Court of Appeals, this time addressing a Washington law in *Costco Wholesale Corp. v. Maleng*.<sup>248</sup> Washington had a post and hold system similar to both Oregon and Maryland, in that wholesalers were required to file prices and adhere to them for a specified period after they went into effect.<sup>249</sup> The *Costco* court's analysis was not as clear as that of *Miller* or *TFWS*. For example, it appeared that the court wanted to collapse the inquiry of whether the post and hold law was a hybrid restraint with the inquiry of whether the post and hold system was actively supervised by the state for purposes of antitrust immunity under the state action doctrine.<sup>250</sup> While the *Costco* court questioned the clarity of the unilateral-hybrid restraint versus an active supervision analysis, it ultimately followed the approach of *Miller* and *TFWS*, first concluding that the law

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<sup>243</sup> See *TFWS, Inc.*, 242 F.3d at 212-13. The court acknowledged that temperance is an interest contemplated by the Twenty-first Amendment. *Id.* at 213.

<sup>244</sup> See *TFWS, Inc. v. Schaefer*, No. WDQ-99-2008, 2007 WL 2917025, at \*10 (D. Md. Sept. 27, 2007).

<sup>245</sup> See, e.g., *TFWS, Inc. v. Schaefer*, 183 F. Supp. 2d 789, 791-94 (D. Md. 2002); *TFWS, Inc. v. Schaefer*, 315 F. Supp. 2d 783, 783-84 & n. 1 (D. Md. 2004); *TFWS, Inc.* 2007 WL 2917025, at \*2-8.

<sup>246</sup> *TFWS, Inc.*, 2007 WL 2917025, at \*10.

<sup>247</sup> See *supra* notes 176-179 and accompanying text.

<sup>248</sup> 522 F.3d 874 (9th Cir. 2008).

<sup>249</sup> See *id.* at 883; see *supra* note 223 and accompanying text; see *supra* note 235 and accompanying text.

<sup>250</sup> See *Costco*, 522 F.3d at 887-88. The court was fairly reasonable in concluding that this is a "doctrinally confusing area." *Id.* at 888. However, it is clear that a law may be considered a hybrid restraint, in that it gives a degree of regulatory power to individuals, see *supra* Part III.A.1.a., but that the law may also be immune because the state reviews the individuals' exercise of that power for reasonableness. See *supra* Part III.A.2.b.

was a hybrid restraint. The court explained that while the wholesalers are not required to match others' prices, "the logical result of the restraints is a less uncertain market, a market more conducive to collusive and stabilized pricing, and hence a less competitive market."<sup>251</sup> In other words, Washington set up a system that facilitated price-fixing by private parties.<sup>252</sup> The court then concluded that the law was also a per se violation of the Sherman Act because it was "highly likely to facilitate horizontal collusion among market participants."<sup>253</sup>

Moving on to the antitrust immunity issue, i.e., state-action doctrine, the court applied *Miller* to the case and held that Washington, like Oregon, failed to actively supervise its post and hold scheme,<sup>254</sup> and thus had not established immunity for the scheme.<sup>255</sup> Finally, the court considered whether the post and hold restraint was saved by the Twenty-first Amendment defense.<sup>256</sup> This time, a factual record had been developed on the issue and the district court had already decided against Washington.<sup>257</sup> The court affirmed the decision against the state, agreeing with the district court that temperance was a "valid and important interest" under the Twenty-first Amendment, but Washington failed to show that the post and hold regulation promoted temperance.<sup>258</sup> In doing so, the court repeated the district court's finding that "there was little empirical evidence documenting the relationship between such pricing schemes and consumption."<sup>259</sup>

Although Section 101-b was facially challenged and upheld in *Battipaglia*,<sup>260</sup> it has become clearer over time that contrary to *Battipaglia*'s characterization of Section 101-b as the "exchange of price information" that should be subject to a rule of reason analysis,<sup>261</sup> it is in fact a post and hold provision and thus a "classic hybrid restraint."<sup>262</sup> It is inappropriate to

<sup>251</sup> *Costco*, 522 F.3d at 888, 893-94.

<sup>252</sup> *See id.* at 894-95.

<sup>253</sup> *Id.* at 895-96. Like the court in *TFWS*, the *Costco* court discussed *Battipaglia* and then declined to follow it. *See id.* at 893-94; *supra* note 238.

<sup>254</sup> *Costco*, 522 F.3d at 901 n.22.

<sup>255</sup> *See supra* Part III.A.2.b. (explaining that states are often barred from immunity due to the absence of active supervision)

<sup>256</sup> *Costco*, 522 F.3d at 901-04.

<sup>257</sup> *Id.* at 902-03.

<sup>258</sup> *Id.*

<sup>259</sup> *Id.* at 903.

<sup>260</sup> *See supra* notes 206-215 and accompanying text.

<sup>261</sup> *Battipaglia v. New York State Liquor Auth.*, 745 F.2d 166, 174-75 (2d Cir. 1984).

<sup>262</sup> *TFWS, Inc. v. Schaefer*, 242 F.3d 198, 208 (4th Cir. 2001).

conclude that Section 101-b will be struck down on an antitrust challenge without any evidence regarding the Twenty-first Amendment defense.<sup>263</sup> Nevertheless, the following section will apply the analysis outlined above<sup>264</sup> to Section 101-b to demonstrate why it is unlikely that the State of New York can protect Section 101-b in an antitrust challenge.

#### IV. ABC LAW SECTION 101-b WILL LIKELY LOSE ON AN ANTITRUST CHALLENGE

Given the evolution of the jurisprudence in the Supreme Court and the federal courts regarding liquor laws that mandate anticompetitive behavior, it seems very unlikely that Section 101-b would be able to withstand another antitrust challenge. Section 101-b, like the post and hold restraints at issue in *Miller*,<sup>265</sup> *TFWS*,<sup>266</sup> and *Costco*,<sup>267</sup> requires not only the filing of prices, but also adherence to those prices. To recap the requirements of Section 101-b, manufacturers and wholesalers must file a monthly posting with the State Liquor Authority (“SLA”) that will go into effect for the following pricing period after a three-day window in which prices may be reduced to match the lowest posted price for the same product.<sup>268</sup> Once the prices are in effect, they cannot be changed without the SLA’s prior written permission.<sup>269</sup> Since Section 101-b is very similar to the post and hold restraints challenged and struck down by *Miller*, *TFWS*, and *Costco*, it should be analyzed in the same manner.

First, Section 101-b is preempted by the Sherman Act because it is a hybrid restraint and a per se violation of the Act. As noted above, while the Second Circuit declared that Section 101-b simply requires exchanging price information, the majority conveniently overlooked the holding aspect of Section

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<sup>263</sup> See *Miller v. Hedlund*, 813 F.2d 1344, 1352 (9th Cir. 1987); see also *supra* note 243 and accompanying text.

<sup>264</sup> See *supra* Part III.A (illustrated in Part III.B.).

<sup>265</sup> See *supra* notes 221-233 and accompanying text.

<sup>266</sup> See *supra* notes 234-247 and accompanying text.

<sup>267</sup> See *supra* notes 248-259 and accompanying text.

<sup>268</sup> See *supra* notes 75-77. At first glance, the statute may seem beneficial to consumers as it allows manufacturers and wholesalers to decrease their prices to the lowest price posted. The harm is that generally there is an ongoing possibility that, in a free market, prices for a good will fluctuate; here, after the three-day window ends the manufacturers and wholesalers are unable to lower prices even if the market would justify a reduction. In other words, consumers lose the benefits of competition as the manufacturers and wholesalers simply have no incentives to compete via price changes after the posting period goes into effect (because they know they cannot be undercut).

<sup>269</sup> See *supra* notes 75-77.

101-b,<sup>270</sup> which is the primary reason this type of law is problematic. The holding aspect of Section 101-b “logical[ly] result[s] . . . [in] a less uncertain market, . . . and hence a less competitive market.”<sup>271</sup> In 2004, the Second Circuit stated, “[w]here the anticompetitive effects of a state statute obviate the need for private parties to act on their own to create an anticompetitive scheme, the statute may be attacked as a ‘hybrid’ restraint.”<sup>272</sup> Section 101-b is therefore a hybrid restraint because it delegates private regulatory power to the distributors and wholesalers by allowing them to set the prices, which the State merely enforces. In other words, Section 101-b is not a unilateral restraint because of the degree of power given to private market participants, and it is also not a private restraint because of the State’s authorization.<sup>273</sup> It is also significant that Section 101-b involves a price restraint because a price restraint is especially prone to being deemed a hybrid restraint.<sup>274</sup> Consistent with the Second Circuit’s requirements under its more recent approach to the issue of hybrid restraints, New York’s price posting regime reduces the need for liquor dealers and wholesalers to create their own anticompetitive scheme. Thus, Section 101-b is a hybrid restraint subject to preemption.

Section 101-b is also a per se violation of the Sherman Act and is thus preempted. By forcing manufacturers and wholesalers to hold to their announced prices, the state “mandates activity that is essentially a form of horizontal price fixing.”<sup>275</sup> As the *Costco* court explained, horizontal collusion allows market participants to maximize profits via price (and production) coordination at the expense of consumers by increasing prices (and decreasing production).<sup>276</sup> Requiring adherence to posted prices makes price cuts irrevocable, and thus “much less likely.”<sup>277</sup> Furthermore, as the *Miller* court

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<sup>270</sup> The dissent, meanwhile, emphasized the significance of the holding requirement. See *supra* note 216 and accompanying text.

<sup>271</sup> *Costco Wholesale Corp. v. Maleng*, 522 F.3d 874, 892-94 (9th Cir. 2008).

<sup>272</sup> *Freedom Holdings, Inc. v. Spitzer*, 357 F.3d 205, 223-24 (2d Cir. 2004) (holding that New York’s Contraband Statutes were hybrid restraints subject to preemption by the Sherman Act for enforcing price-fixing among major tobacco producers).

<sup>273</sup> See *supra* Part III.A.1.a.

<sup>274</sup> See *supra* notes 157-158 and accompanying text.

<sup>275</sup> *TFWS, Inc. v. Schaefer*, 242 F.3d 198, 208 (4th Cir. 2001).

<sup>276</sup> *Costco*, 522 F.3d at 896.

<sup>277</sup> *Id.*

explicitly stated, “[a]n agreement to adhere to previously announced prices . . . is unlawful *per se* under the Sherman Act.”<sup>278</sup> While the majority in *Battipaglia* refrained from deciding whether Section 101-b could be preempted by the Sherman Act without actual agreement between the manufacturers and/or wholesalers, that issue has since been decided.<sup>279</sup> In *324 Liquor*, the Supreme Court held that a *per se* violation may be found in the absence of a private agreement if the state compels activity that would otherwise be a *per se* violation.<sup>280</sup> Indeed, the Second Circuit has since acknowledged that the Supreme Court does not require actual agreement as a prerequisite to preemption under the Sherman Act.<sup>281</sup> Thus, Section 101-b is a hybrid restraint for delegating regulatory power to private individuals, and it is a *per se* violation because adhering to posted prices is illegal under the Sherman Act.

Second, Section 101-b is most likely not immune under the state-action doctrine. As required by prong one of the *Midcal* test for antitrust immunity,<sup>282</sup> New York has “clearly articulated and affirmatively expressed as state policy” its intent to promote temperance and orderly market conditions by prohibiting price discrimination with Section 101-b.<sup>283</sup> In *Midcal*, California satisfied prong one of the test when it clearly stated its goal of permitting price resale maintenance as legislative policy.<sup>284</sup> The Supreme Court similarly found prong one satisfied in *324 Liquor*, where New York also clearly intended to allow price resale maintenance.<sup>285</sup> Interestingly, in *Freedom Holdings, Inc. v. Spitzer*,<sup>286</sup> the Second Circuit found that New York failed to satisfy prong one of *Midcal* when it claimed an interest in revenue production was the underlying

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<sup>278</sup> *Miller v. Hedlund*, 813 F.2d 1344, 1349 (9th Cir. 1987).

<sup>279</sup> *See 324 Liquor Corp. v. Duffy*, 479 U.S. 335, 345-46 (1987).

<sup>280</sup> *Id.*

<sup>281</sup> *See Freedom Holdings, Inc. v. Spitzer*, 357 F.3d 205, 224 n.17 (2d Cir. 2004); *see 324 Liquor Corp.*, 479 U.S. at 345-46 & n.8.

<sup>282</sup> *See supra* Part III.A.2.a. for a refresher on *Midcal*'s first prong to establish immunity under the state-action doctrine.

<sup>283</sup> *Battipaglia v. New York State Liquor Auth.*, 745 F.2d 166, 176 (2d Cir. 1984) (quoting *Cal. Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 105). In dissent, Judge Winter stated that New York's policy of “creating a cartel” with Section 101-b was “one clearly articulated and affirmatively expressed” by the state,” which satisfied the first part of the *Midcal* test. *Id.* at 180 (Winter, J. dissenting) (quoting *Midcal*, 445 U.S. 97 at 105); *see also* N.Y. ALCO. BEV. CONT. LAW § 101-b(1).

<sup>284</sup> *See Midcal*, 445 U.S. at 105.

<sup>285</sup> *See 324 Liquor Corp.*, 479 U.S. at 344.

<sup>286</sup> 357 F.3d 205 (2d Cir. 2004).

goal of enforcing a price-fixing scheme among major tobacco producers.<sup>287</sup> The Second Circuit explained, “an ancillary function of the first *Midcal* prong is to establish the legitimate State policy underlying the decision to displace the Sherman Act.”<sup>288</sup> Even if the legitimacy of New York’s interests are assessed at this stage of the analysis, as opposed to waiting until the Twenty-first Amendment defense is raised,<sup>289</sup> New York will still likely satisfy prong one of *Midcal* because its interests in promoting temperance and orderly market conditions involve public and economic interests beyond mere revenue production for the state.

While Section 101-b will probably pass the first inquiry under *Midcal*, it most likely will fail *Midcal*’s second prong, which requires that New York “actively supervise” the implementation of Section 101-b.<sup>290</sup> Post and hold restraints similar to Section 101-b have repeatedly failed to satisfy prong two of *Midcal* because the states responsible for the laws “neither establishe[d] prices nor review[ed] the reasonableness of the price schedules,” and the states failed to “monitor market conditions or engage in any ‘pointed reexamination’ of the program[s].”<sup>291</sup> In finding that ABC Law Section 101-bb was not actively supervised by New York, the Supreme Court in *324 Liquor* reasoned, “[t]he State has displaced competition among liquor retailers without substituting an adequate system of regulation.”<sup>292</sup> Judge Winter, in his dissent from the *Battipaglia* majority, stated that New York “does nothing whatsoever to establish the actual prices charged, review their reasonableness, monitor market conditions, or engage in reexamination of the program.”<sup>293</sup> As it had done in *324 Liquor*, New York persists in displacing competition without an

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<sup>287</sup> See *id.* at 230.

<sup>288</sup> *Id.*

<sup>289</sup> See *supra* Part III.A.3.

<sup>290</sup> See *supra* Part III.A.2.b.

<sup>291</sup> Cal. Retail Liquor Dealers Ass’n v. Midcal Aluminum, Inc., 445 U.S. 97, 105-06 (1980) (citation omitted); see also Costco Wholesale Corp. v. Maleng, 522 F.3d 874, 901 n.22 (9th Cir. 2008); TFWS, Inc. v. Schaefer, 242 F.3d 198, 211 (4th Cir. 2001); Miller v. Hedlund, 813 F.2d 1344, 1351-52 & n.6 (9th Cir. 1987).

<sup>292</sup> 324 Liquor Corp. v. Duffy, 479 U.S. 335, 344-45 (1987).

<sup>293</sup> Battipaglia v. New York State Liquor Auth., 745 F.2d 166, 180 (2d Cir. 1984) (Winter, J., dissenting). Indeed, the New York State Law Revision Commission reported that the SLA does not monitor posted prices. See NEW YORK STATE LAW REVISION COMMISSION REPORT ON THE ALCOHOL BEVERAGE CONTROL LAW AND ITS ADMINISTRATION [Hereinafter COMMISSION REPORT PART ONE], 34 (September 30, 2009), available at <http://www.lawrevision.state.ny.us/abcls.php> (last visited Feb. 18, 2010).

adequate system of regulation by giving manufacturers and wholesalers discretion over prices and enforcing them without regard to their reasonableness. Accordingly, Section 101-b will most likely not be immune, for failing prong two of *Midcal*.

Finally, it is very unlikely that Section 101-b will prevail if New York asserts the Twenty-first Amendment defense. Not only must New York have a legitimate policy supporting Section 101-b, the law must also be effective in serving that policy.<sup>294</sup> In determining whether New York's interests are legitimate, a court must find that they are "closely related" to the goals of the Twenty-first Amendment,<sup>295</sup> and that New York's interests outweigh the federal interests of the Sherman Act, which has been described as "the Magna Carta of free enterprise."<sup>296</sup> As an initial matter, New York's stated interest in promoting temperance is certainly a legitimate state interest.<sup>297</sup> New York also has expressed intent to prohibit price discrimination for the purpose of orderly markets,<sup>298</sup> which is also likely a legitimate state interest.<sup>299</sup> However, the Twenty-first Amendment will likely fail to protect Section 101-b because New York will probably not be able to meet its burden of showing that Section 101-b actually promotes temperance, prevents price discrimination, or promotes orderly markets.

In order to show that Section 101-b substantiates its purported goals, New York will have to spend considerable time and money to produce persuasive evidence. With respect to showing that Section 101-b promotes temperance, perhaps New York could prepare analytic state studies on consumption, possibly distinguishing between New York and another state without a post and hold restraint in place. However, a

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<sup>294</sup> See *supra* Part III.A.3.

<sup>295</sup> *Capital Cities Cable, Inc. v. Crisp*, 467 U.S. 691, 714 (1984); see *supra* note 112-113 and accompanying text.

<sup>296</sup> *Midcal*, 445 U.S. at 110; see *supra* Part III.A.3.

<sup>297</sup> See *supra* notes 192, 243, and 258 and accompanying text.

<sup>298</sup> N.Y. ALCO. BEV. CONT. LAW § 101-b(1) (McKinney 2009).

<sup>299</sup> With respect to New York's interest in promoting orderly markets, this argument was addressed in a footnote by the *Costco* court. See *Costco Wholesale Corp. v. Maleng*, 522 F.3d 874, 902 n.23 (9th Cir. 2008). Washington cited *North Dakota v. United States*, 495 U.S. 423, 432 (1990) as support for its argument that it had an interest in orderly markets, but the court explained the concept of "orderly markets" was hard to define and thus there could be no clear error by the district court in deciding that this interest was not substantiated by the challenged post and hold restraint. *Id.* With respect to prohibiting price discrimination, the *Miller* court apparently accepted that this was a legitimate state interest as well, as the court went on to inquire whether the interest was substantiated, ultimately finding it was not. See *Miller v. Hedlund*, 813 F.2d 1344, 1352; see also *supra* notes 231-233.

challenger may rebut such evidence and a court does not have to give deference to the state's evidence.<sup>300</sup> With respect to preventing price discrimination and promoting orderly markets, New York could present state agency reports and/or congressional studies regarding effects of Section 101-b on market conditions, and empirical economic evidence.<sup>301</sup> Of course, these studies must first be performed, assuming no such studies on this precise issue have been prepared as of yet.<sup>302</sup> A challenger may also produce conflicting studies, again giving a court the choice of whose evidence to accept.<sup>303</sup> Finally, New York will most likely need to produce expert witness testimony as well,<sup>304</sup> which may also be rebutted.

This is not to say that it is impossible for New York to save Section 101-b if it is challenged. Rather, it is to emphasize the amount of effort that New York will have to invest to show that Section 101-b should be sustained, and that even with extensive evidence, there is no guarantee that a court will find in New York's favor. Unless New York is able to develop a record showing Section 101-b fosters its stated interests, Section 101-b will be struck down on an antitrust challenge. *Unsubstantiated* state interests, no matter how closely related to the Twenty-first Amendment, cannot outweigh the Sherman Act's policy of promoting competition.<sup>305</sup>

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<sup>300</sup> See *supra* note 200 and accompanying text (explaining that a court will examine evidence to the contrary).

<sup>301</sup> See *supra* notes 243-247 and accompanying text.

<sup>302</sup> This seems to be a fair assumption considering the New York State Law Revision Commission's recent findings:

The SLA is unable to determine industry's compliance with the law. Price posting information is not monitored so it is no surprise that the SLA would fail to detect abuses in the industry. Because it does not monitor the information, it is unable to demonstrate that the objectives of the post and hold process are achieved.

COMMISSION REPORT PART ONE at 34.

<sup>303</sup> For example, in *Miller*, while Washington argued that its post and hold restraint prevented price discrimination, the court agreed with the challenger that rather than prevent price discrimination, the price posting laws simply "authoriz[ed], facilitat[ed], and induc[ed] horizontal price fixing." *Miller v. Hedlund*, 717 F. Supp. 711, 715-16 (D. Or. 1989).

<sup>304</sup> See *supra* notes 243-247 and accompanying text.

<sup>305</sup> See *supra* note 195 and accompanying text.

## CONCLUSION

Given the problems that alcohol has caused in the past and continues to cause today,<sup>306</sup> it is no surprise that New York wants to have special regulations imposed on the liquor industry. However, it is unreasonable to be overly concerned with the regulation of alcohol distribution at the expense of the Sherman Act, and the goals of the Sherman Act should not be discarded. Quite the contrary, these goals are just as important to the promotion of social welfare as the desire to prevent excessive consumption and price discrimination.<sup>307</sup> However, if New York insists upon sacrificing the pro-competition policy of the Sherman Act, it must take a more proactive role in implementing Section 101-b,<sup>308</sup> which would probably take no more effort than putting up a strong defense under the Twenty-first Amendment. Whether New York wishes to create or find evidence conclusively showing that Section 101-b actually promotes temperance, prevents price discrimination, or promotes orderly markets, or whether New York wishes to take a more active role in supervising its price posting system, one thing is clear: some sort of action should be taken to prevent the law invalidation in the event of an antitrust challenge. Despite confusing and sometimes inconsistent individual opinions regarding the Twenty-first Amendment's protection of liquor regulations,<sup>309</sup> it has become increasingly clear over time that the current state of the law will not permit Section 101-b to stand if challenged.

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<sup>306</sup> See *supra* notes 1-5 and accompanying text.

<sup>307</sup> See *supra* notes 44-53 and accompanying text.

<sup>308</sup> If New York takes this action, then Section 101-b would likely qualify for antitrust immunity under the state-action doctrine as an actively supervised hybrid restraint. See *supra* Part III.A.2.b.

<sup>309</sup> See *supra* Part II.

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