17-2003-cv

United States Court of Appeals

for the

Second Circuit

CONNECTICUT FINE WINE AND SPIRITS, LLC, DBA Total Wine & More,

Plaintiff-Appellant,

– v. –

COMMISSIONER MICHELLE H. SEAGULL, DEPARTMENT OF CONSUMER PROTECTION, JOHN SUCHY, DIRECTOR, DIVISION OF LIQUOR CONTROL,

Defendants-Appellees,

WINE & SPIRITS WHOLESALERS OF CONNECTICUT, INC., CONNECTICUT BEER WHOLESALERS ASSOCIATION, INC., CONNECTICUT RESTAURANT ASSOCIATION, CONNECTICUT PACKAGE STORES ASSOCIATION, INC., BRESCOME BARTON, INC.,

Intervenors-Defendants-Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF CONNECTICUT

REPLY BRIEF FOR PLAINTIFF-APPELLANT

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INTRODUCTION

The State Defendants and the Intervenors all contend that Total Wine's facial challenge fails because the Connecticut statutes, "on [their] face," do not "irreconcilably conflict[] with federal antitrust policy," as required by *Rice* v. *Norman Williams Co.*, 458 U.S. 654, 659 (1982). But Total Wine's Complaint clearly states a valid facial challenge to the interrelated Connecticut statutes and regulations under the Supreme Court's opinions in *California Retail Liquor Dealers Ass'n* v. *Midcal Aluminum, Inc.*, 445 U.S. 97 (1980), which was reaffirmed in *Rice*, and *324 Liquor Corp.* v. *Duffy*, 479 U.S. 335 (1987), which was decided five years after *Rice*. A careful analysis and application of these decisions, and the antitrust principles they embody, demonstrate that the District Court erred in dismissing Total Wine's Complaint on a preliminary motion.

The Supreme Court's principal decisions in this area also demonstrate that the District Court made two errors in failing to recognize that the statutes authorize and compel horizontal price restraints that are *per se* invalid. The District Court failed to analyze the Connecticut pricing statutes as integrated elements of a unitary pricing regime, and failed to credit Total Wine's well-pleaded allegations about the indisputable horizontal price restraints that are among the

anticompetitive effects of the statutes.[1] This Reply focuses on the impact of these seminal Supreme Court decisions on the challenged statutes and regulations. Total Wine cannot address herein all points raised in the 125 combined pages of briefing submitted by the Appellees, but emphasizes that its opening Brief counters all of the significant arguments raised by Appellees.

ARGUMENT

I. Appellees Have Misunderstood and Misapplied the Challenged Connecticut Statutes[2]

The Appellees in their various Briefs have not fairly described the inter-related requirements of the challenged statutes and regulations. Moreover, they have attempted to separate the provisions and ascribe to them distinct purposes and effects.[3] To reiterate, § 30-63(c) of the Connecticut Liquor Control Act requires,

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[1] The District Court correctly held that at least two of the statutory provisions constituted "hybrid restraints" that create regulatory mechanisms for enforcing private market decisions, but failed to recognize that those provisions have the effect of enforcing price fixing restraints that have *both* horizontal and industry-wide vertical effects throughout Connecticut's entire alcoholic beverage industry. The Appellees' arguments that each of the challenged statutes imposes a "unilateral restraint" fail because the wholesalers set and hold the posted case prices (without state involvement), and they manipulate the minimum bottle prices in a manner that controls retail prices and profit margins. *See* JA 19-21 (Compl. ¶ ¶ 16-22); note 4 *infra*.

[2] The challenged Connecticut statutes and the state agency's implementing regulations on price posting are set out verbatim in the Statutory Addendum to this Reply Brief.

[3] A dominant theme of the Appellees is that the Connecticut statutes were designed to protect small retailers from the "dangers" of price competition from more

among other things, that all wholesalers post with the State on a monthly basis their bottle, can, and case prices for all alcoholic beverages they offer for sale. After a period permitting brand competitors to match those prices, the statute requires that the posted prices "shall be the controlling price … for the month following such posting." This is the post and hold statute that precludes price negotiations by retailers with wholesalers, and that also authorizes competing wholesalers to match and hold their posted prices for the identical products, and for comparable competing brands. Under prevailing Supreme Court authority, § 30-63(c) clearly authorizes *horizontal* price fixing.

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efficient retail stores. They cite the prospect of "unfair" competition in the form of predatory pricing. *See, e.g.*, Combined Br. of Intervenor App'ees, at 6-8. But nothing in this case involves predatory "below cost" pricing. The case involves instead a challenge to statutory prohibitions on retail sales by Total Wine and other efficient retailers that are competitive on price and above the retailers' actual costs. *See* JA 21 (Complaint, ¶ 22). Moreover, the Supreme Court has never recognized the protection of small retailers as a state interest that overrides the federal interest in free competition mandated by the Sherman Act. *See 324 Liquor Corp*., 479 U.S. at 350-51 & n.12 (holding that New York's "asserted interest in protecting small retailers does not suffice to afford immunity from the Sherman Act," and noting that "[w]e have no occasion in this case to consider whether the State's interest in protecting small retailers *ever* could prevail against the federal interest in enforcement of the antitrust laws.") (emphasis added). *See also Leegin Creative Leather Products, Inc*. v. *PSKS, Inc*., 551 U.S. 877, 905-06 (2007) (explaining that the rationale for state fair trade laws, designed to "save inefficient retailers from their inability to compete," is "foreign to the Sherman Act" whose purpose is to protect "competition, not competitors," and noting that the previous antitrust exemption for these laws contained in the Miller-Tydings Fair Trade Act, 50 Stat. 693 (1937), was repealed by Congress in the Consumer Goods Pricing Act, 89 Stat. 801 (1975)).

The effect of § 30-63(c) is not limited, however, to the fixing of case prices pursuant to which wholesalers supply their products to retailers. The same statute also requires the posting and fixing of "bottle" prices each month, which has a direct impact on the retail market. That impact derives from the related requirement in § 30-68m(b) that "no retail permittee shall sell liquor at a price below his or her cost," coupled with the provision in § 30-68m(a)(1) that defines a retailer's "cost" for wine and spirits as "*the posted bottle price from the wholesaler* plus any charge for shipping or delivery to the retailer permittee's place of business . . . ." (Emphasis added). The State Defendants misleadingly claim that "bottle price is derived from the case price by [a] pricing algorithm set forth in the statute, which the wholesaler must obey." Def. App'ee Br. at 34. In fact, the "algorithm" in § 30-68m(a)(3) sets a *minimum* mark-up. The wholesalers are free to set and post minimum bottle prices at any level above that arithmetic formula that they choose. More important, when the wholesalers decide to "post off" or discount their case prices for a given product, they are not required to change their posted bottle prices, which are predicated on a markup over the full case price that typically prevails during most of the year.

Thus, there are months when the posted minimum bottle price for a given product bears no relationship to the actual case price paid by retailers, nor to the statutory "algorithm" imposed for calculating minimum markups. The result, as

outlined in the Complaint, is that wholesalers collectively are required and authorized by the Connecticut statutes: (i) to fix (*i.e.*, post and hold) the case prices that will be paid by their retailers every month; (ii) to fix (*i.e.*, post and hold) the minimum retail prices that will be paid by all Connecticut consumers; and (iii) to fix guaranteed profit margins that will protect all liquor stores from effective price competition at the retail level.[4]

Intervenor Brescome Barton argues that the impact of these statutes in reducing price competition among competing wholesalers selling the same brands

[4] In attempting to contrast the Connecticut regime with the New York statutes at issue in *324 Liquor*, the State Defendants contend that while a Connecticut "wholesaler may 'post off' the case price to a retailer, it may not 'post off' the bottle price once that price has been posted." Def. App'ee Br. at 35. It is not clear what that passage is supposed to mean. The challenged statutes contain no restrictions on wholesalers changing their posted minimum bottle prices once a month, and the record plainly reflects that wholesalers sometimes "post off" their bottle prices when they reduce their case prices, and sometimes they do not, and that they do not necessarily use the statutory algorithms when setting minimum bottle prices. In fact, the statutes at issue authorize wholesalers to post and hold minimum bottle prices in such a fashion as to guarantee healthy profit margins for the retailers to whom they sell. *See, e.g.*, JA 24 (Table 1 to the Complaint). For example, Table 1 reflects that four separate wholesalers maintained *identical* case prices for Jameson's whiskey of $49.91 per bottle during most months, and *identical* minimum bottle prices of $49.99 (8 cents over the bottle price per case) during those months, but that when all four wholesalers posted off their case prices by almost $15 to $35.01 per bottle in February 2016, they all reduced their minimum bottle prices by only $5 to $44.99. When the same four wholesalers posted off their case prices for Jameson's by $10 to $39.91 in May, 2016, they all kept their minimum bottle price fixed at $49.99. In every instance, the wholesalers' case and minimum bottle prices moved in precise tandem over the course of the year. In every instance, during post-off months the minimum bottle prices bore no relationship either to the retailers' actual costs or to the statutory algorithm defining minimum markups.

– one clear horizontal impact of the post and hold regime – is softened by the fact that "[m]ost alcoholic products are sold by a wholesaler on an exclusive basis," and that "Total Wine's claims, therefore, apply only to a small portion of the number of *alcoholic products* offered for sale." Int. BB Br. at 4 (emphasis added). Brescome Barton's contention is not based on any facts of record, and is carefully phrased to refer to the number of distinct products that are offered for sale, rather than the total volume of alcohol products that are sold. Total Wine's assertion of blatant intrabrand price fixing among competing wholesalers is in fact a widely prevalent fact when one focuses attention on the sale of popular brands. For example, the uncontested facts set forth in the Tables attached to the Complaint reflect that at least two to four wholesalers "compete" with each other for the sale of many of the "brand name" products that are among those most widely purchased in the State – Absolut, Grey Goose, Skyy and Smirnoff vodkas; Bombay, Bombay Sapphire, and Tanqueray gins; Jack Daniels, Jim Beam, and Maker's Mark bourbon whiskeys; and Dewar's and Johnnie Walker scotch whiskeys. *See* JA 24-31. There is little doubt that most of the high volume brand name liquors and many popular wines sold in Connecticut are sold by multiple wholesalers, and that those wholesalers are "authorized" by the statutes in question to post and hold identical case prices to retailers, while at the same time manipulating the posted and held

identical minimum bottle prices at which these popular brands must be sold to Connecticut consumers.[5]

The third aspect of the Connecticut statutory scheme at issue here is the flat prohibition on wholesale discounts based on quantity purchases set forth both in § 30-63(b) and reiterated in § 30-68k and § 30-94. While the District Court found the quantity discount ban, unlike the other challenged provisions, to be a unilateral restraint imposed by statute, in context it is not. The statutory prohibition on quantity discounts enables private and state enforcement of the related post and hold and minimum bottle pricing laws, as was recognized by the Fourth Circuit in *TFWS, Inc.* v. *Franchot*, 572 F.3d 186, 193-94 (4th Cir. 2009). Moreover, the quantity discount ban obviously affects only prices from which discounts might otherwise be calculated – *i.e.*, the posted and held case and minimum bottle prices that wholesalers are required to publish each month. In other words, the quantity discount ban in §§ 30-63(b) and 30-68k is a prohibition on wholesalers offering discounts to retailers from the posted and held prices established by § 30-63(c).

[5] Published issues of the *Connecticut Beverage Journal* also demonstrate that most popular brands of liquor and many wines are offered for sale by multiple wholesalers. Those brands account for a substantial percentage of alcohol sales in the state, even though they may represent a much smaller percentage of the total number of branded alcohol products sold in Connecticut. See, e.g., Vol. 81, Connecticut Beverage Journal, No. 10 (October, 2016), at pps. 3a-21a (listing hundreds of brands of liquor for which there are multiple Connecticut wholesalers).

II. The Challenged Statutes Are Invalid Under *Midcal*

In *Midcal*, a unanimous Supreme Court held that California's wine pricing system – which included both a resale price maintenance provision *and* a price posting statute – violated the Sherman Act, 15 U.S.C. § 1, and was not saved either by the "state action" doctrine nor by the Twenty-first Amendment.[6] Contrary to the approach of the District Court below, the Supreme Court clearly reviewed the effect of the statutes in tandem. *See* 445 U.S. at 99-100. The Court also observed that an earlier decision of the California Supreme Court had struck down parallel restrictions on the sale of distilled liquors, and "emphasized that the California system not only permitted vertical control of prices by producers, but also frequently resulted in horizontal price fixing," because "[u]nder the program, many comparable brands of liquor were marketed at identical prices." *Id*. at 101. In a footnote reminiscent of the Tables attached to the Complaint in this case, the Supreme Court observed that there was "record evidence [from the prior California decision] that in July 1976 five leading brands of gin each sold in California for $4.89 for a fifth of a gallon, and that five leading brands of Scotch whiskey sold for either $8.39 or $8.40 a fifth." *Id.* at 101, n. 3 (citing *Rice* v. *Alcoholic Beverage Control Appeals Bd.*, 21 Cal. 3d 431, 454 & nn. 14, 16 (1978)).

[6] Neither the state action doctrine enunciated in *Parker* v. *Brown*, 317 U.S. 341 (1943), nor the Twenty-first Amendment were relied upon by the State Defendants and Intervenors below in their Motions to Dismiss.

Based on the language of the statutes in question, and on their pernicious effects on horizontal competition as found by the California courts, the Supreme Court had no difficulty in concluding that "California's system for wine pricing plainly constitutes resale price maintenance in violation of the Sherman Act." 445 U.S. at 103. The Court noted that "[t]he wine producer holds the power to prevent price competition by dictating the prices charged by wholesalers." *Id*. And the Court credited the observation of Justice Hughes in *Dr. Miles Medical Co*. v. *John D. Park & Sons Co.*, 220 U.S. 373, 408 (1911), that "such vertical control destroys *horizontal competition* as effectively as if wholesalers 'formed a combination and endeavored to establish the same restrictions . . . by agreement with each other." *Midcal*, 445 U.S. at 103 (emphasis added). The Court was buttressed in its conclusion concerning the anticompetitive horizontal aspects of the California wine pricing system by the decision of the California Supreme Court in *Rice*, whose reasoning had been adopted by the California appellate court in *Midcal*. *See id*. at 103, n.7.

In rejecting the State's *Parker* v. *Brown* immunity defense, the Supreme Court also observed that under the California wine pricing statutes, the "State simply authorizes price setting and enforces the prices established by private parties." *Id.* at 105. That is the essence of a hybrid restraint and the Court's observation applies fully to the Connecticut statutes at issue here.

In all respects, the decision in *Midcal* is instructive. Total Wine contends in its Complaint that the post and hold regime in Connecticut authorizes the wholesalers to set and hold their own prices, and authorizes them to dictate minimum retail prices as well. Total Wine has claimed, and has offered evidence to show, that the system thus encourages horizontal price fixing at both the wholesale and retail levels, just like the evidence presented and reviewed by the Supreme Court in *Midcal*. The District Court thus plainly erred in failing to consider the challenged statutes as part of an integrated pricing regime, and in failing to consider the alleged horizontal impact of the statutes at both the wholesale and retail levels of the distribution chain. Moreover, the District Court's failure to consider the evidence of price collusion set forth in the Tables accompanying the Complaint simply cannot be squared with the unanimous decision of the Supreme Court in *Midcal*.

III. The Complaint States a Valid Preemption Claim Under *Rice*

The Appellees all insist that Total Wine's Complaint cannot meet the Supreme Court's test for a valid preemption claim challenging state statutes and regulations as preempted by the Sherman Act, as set forth in *Rice* v. *Norman Williams Co.*, 458 U.S. 654 (1982). The Appellees are wrong. In *Rice*, the Court held that a state statute "when considered in the abstract, may be condemned under the antitrust laws only 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." 458 U.S. at 661 (emphasis added). In other words, a preemption claim will be deemed valid under the Sherman Act only "when the conduct contemplated by the statute is in all cases a *per se* violation." *Id.* The allegations in the Total Wine Complaint readily meet that test.

First, the Complaint alleges that the Connecticut statutes both compel and authorize horizontal price fixing. *E.g.*, JA 19 (Complaint, ¶ 16). The price restraints operate horizontally at the wholesale level, where wholesalers are required to post prices from which they will not deviate for at least a month. And they operate horizontally at the retail level as well, in two respects. The statutes plainly authorize competing wholesalers to match their competitors' case prices for identical brands, so that the retailers have no alternative sources of supply for less expensive products. And the statutes also authorize the state's wholesalers to dictate minimum bottle prices that every retailer must adhere to as a floor for every product it sells. This system obviously creates, on its face, horizontal price restraints that are classic *per se* violations of the antitrust laws. *See, e.g.*, *Catalano, Inc.* v. *Target Sales, Inc.*, 446 U.S. 643, 649-50 (1980) (an agreement among competitors limiting their freedom to deviate from published prices is *per se* unlawful).

Second, the Complaint also alleges, just as the Supreme Court found in *Midcal*, that the unique form of "resale price maintenance" authorized by the Connecticut statutes has horizontal as well as vertical effects. The statutes not only require wholesalers to set and hold their own prices offered to retailers, but they also require the wholesalers to set minimum bottle prices as well for every product sold in the state. Connecticut retailers, in turn, are required to adopt those price floors and hold them in place until such time, if ever, that the wholesalers set a new minimum bottle price. *See* JA 18-20 (Complaint, ¶¶ 12-19). The allegations in the Complaint plainly satisfy the standards enunciated by the Supreme Court in *Rice*. It is only by ignoring the interplay of the statutes and the way that they operate in the marketplace, and the well-pleaded allegations of the Complaint, that the Appellees can contend otherwise.

IV. The Challenged Statutes Are Invalid Under *324 Liquor*

Only five years after its decision in *Rice*, the Supreme Court confronted another state statutory scheme governing liquor prices in *324 Liquor Corp*. v. *Duffy*, 479 U.S. 335 (1987). As the District Court observed, the New York statutory scheme invalidated in *324 Liquor* is nearly identical to the Connecticut price regime at issue in this case. *See* JA 150. Justice Powell wrote the decision for

the Court in *324 Liquor*. With respect to the issues presented in this appeal, the decision of the Supreme Court was unanimous.[7]

Significantly, the New York statutes invalidated in *324 Liquor* included a price posting statute that required wholesalers to "file, or 'post,' monthly price schedules with the State Liquor Authority (SLA)." 479 U.S. at 337. Those schedules were required to list with respect to every item offered for sale in a given month "the bottle and case price to retailers." *Id*. at 338 (internal quotation marks omitted). The Court observed that although the New York statutes did not require any relationship between posted case prices and posted bottle prices, for most products the implementing regulations dictated that "the posted bottle price must exceed the posted case price by a 'breakage' surcharge of $1.92." *Id.*

As is the case in Connecticut, pursuant to another section of the New York laws, "[r]etailers of liquor may not sell below 'cost,'" but the "statute defines 'cost' as 'the price of such item of liquor to the retailer plus twelve percentum of such price.'" *Id.* at 338-39. As in Connecticut, "price" under the New York statute was "defined as the posted bottle price in effect at the time the retailer sells or offers to

[7] Justice O'Connor and Chief Justice Rehnquist dissented only with respect to the Court's holding that the New York statute was not a valid exercise of the State's power to regulate the distribution of alcohol and thus protected by § 2 of the Twenty-first Amendment. Although Chief Justice Rehnquist was the author of *Rice*, he did not quarrel with the Supreme Court's holding in *324 Liquor* that the New York statutes at issue created a pricing scheme that was facially inconsistent with federal antitrust laws, and that constituted *per se* violations of the Sherman Act.

sell the item." *Id*. at 339. And as in Connecticut, the New York SLA "expressly has authorized wholesalers to reduce, or 'post off,' the case price of an item without reducing the posted bottle price of the item." *Id*. The Supreme Court observed, in words that are fully applicable to the Connecticut statutes at issue here, that "[b]y reducing the case price without reducing the bottle price, wholesalers can compel retailers to charge [consumers] more than 112 percent of the actual wholesale cost." *Id*. at 339-40. And, as is true in Connecticut, "wholesalers can sell retailers large quantities in a month when [posted case] prices are low and then require the retailers to sell at an abnormally high markup by raising the bottle price in succeeding months." *Id*. at 340. The result, also true in Connecticut, was that "[t]he New York retail pricing system … permits wholesalers to set retail prices, and retail markups, without regard to actual retail costs." *Id*.

The Supreme Court in *324 Liquor* also reviewed advertisements placed by New York wholesalers in which they guaranteed large retail markups to their customers through generous "post offs" and extra retail profits when bottle prices were raised. Contrary to the arguments of the State Defendants and the Intervenors in this appeal, the Supreme Court did not feel constrained when reviewing the facial validity of the challenged New York statutes and implementing regulations to ignore the actual impact of this system on the retail marketplace, nor did the Court feel constrained, as the District Court did here, to analyze separately each

statute and regulation contained within an integrated state-mandated pricing regime. To the contrary, the Court noted that "*[t]he effect of this complex of statutory provisions and regulations is to permit wholesalers to maintain retail prices at artificially high levels.*" *Id*. (emphasis added). The "complex" of Connecticut statutes and regulations at issue here, as alleged in Total Wine's Complaint, have precisely the same effect. *E.g*., JA 21 (Complaint, ¶ 22).

After reviewing the interplay of the statutes and regulations in question, and noting their obvious effect on retail prices for alcoholic beverages in New York, the *324 Liquor* Court observed that the framework for its preemption analysis was established by its earlier decision in *Midcal*. *Id.* at 341. And, "[t]he 'threshold question,' in this case as in *Midcal*, is whether the State's pricing system is inconsistent with the antitrust laws." *Id*. The Court had no difficulty in concluding that the New York statutes, taken together, created a "regime of resale price maintenance on all New York liquor retailers," *id*., and that such a regime of vertical price restraints, especially when it "applie[d] to *all* wholesalers and retailers of liquor," was "virtually certain to reduce interbrand competition as well as intrabrand competition, because it prevents manufacturers and wholesalers from allowing or requiring retail price competition." *Id*. at 342 (emphasis in original).

To be sure, the Supreme Court determined in *324 Liquor* that the challenged New York statutes were *per se* unlawful because, like the California statutes at

issue in *Midcal*, they "mandated resale price maintenance, an activity that has long been regarded as a *per se* violation of the Sherman Act." *Id*. at 343 (quoting *Rice* v. *Norman Williams Co*., *supra*, 458 U.S. at 659-60)). But it is also significant that the form of resale price maintenance condemned both in *Midcal* and *324 Liquor* was far different from private contractual price controls imposed on retailers by manufacturers within a single chain of distribution. To the contrary, the *per se* violations identified by the Court in *Midcal* and *324 Liquor*, and recognized by the Court as giving rise to valid Sherman Act preemption claims in *Rice*, were mandated statewide, and were applicable to *all* wholesalers and *all* retailers selling alcoholic beverages within California and New York.

Because the Connecticut statutes at issue here apply to all wholesalers, requiring them to post and hold both case prices that will be paid by all retailers, and to post and hold minimum bottle prices that must be adhered to by all retailers when making sales to consumers – and because those statutes effectively preclude any form of price competition at either the wholesale or retail levels of distribution – the statutes are facially inconsistent with the Sherman Act, and subject to preemption.

V. *Leegin* Did Not Overrule *Midcal* and *324 Liquor*

The Supreme Court's subsequent decision in *Leegin Creative Products, Inc.* v. *PSKS, Inc*., 551 U.S. 877 (2007), determined that vertical resale price

arrangements entered into by manufacturers, wholesalers and retailers in a single chain of product distribution were to be judged according to the "rule of reason" under the Sherman Act, because of their potential procompetitive effects in stimulating interbrand competition. *See, e.g.*, 551 U.S. at 900 ("there is now widespread agreement that resale price maintenance can have procompetitive effects."). But the *Leegin* Court did not question the continuing vitality of *Midcal* or *324 Liquor* in its ruling, let alone overrule those decisions, and it certainly did not authorize the states to contravene the federal policies favoring competition implemented in the Sherman Act by blessing state-mandated across-the-board retail price maintenance schemes throughout entire industries.

Unlike the procompetitive potential effects of private vertical resale price maintenance arrangements for certain goods, the clear impact of the Connecticut statutes at issue here is to preclude any form of price competition among competing wholesalers, eliminating both interbrand and intrabrand price competition, and to mandate fixed wholesale prices and fixed retail price floors (and resulting retail profit margins) for every alcohol product offered for sale in the state. *Leegin* expressly recognized that the federal "antitrust laws are designed primarily to protect interbrand competition, from which lower prices can later result." *Id*. at 895. As demonstrated above, there is no interbrand competition possible when competing wholesalers all post and hold their prices, and when

competing retailers are required to offer all their products at minimum bottle prices that have been fixed and artificially inflated by the wholesalers.

The District Court determined (JA 164-67), and the Appellees in this case have argued, that both *324 Liquor* and *Midcal* have lost their persuasive force after the Supreme Court's decision in *Leegin* holding that private vertical resale price maintenance agreements are not *per se* unlawful. They are wrong for several reasons.

First, even if *Leegin* had undercut the rationales of *324 Liquor* and *Midcal*, which Total Wine disputes for all the reasons set forth above, the Supreme Court has made it abundantly clear that the federal courts of appeal still must follow those of its decisions that have direct application to a given case. *See, e.g.*, *State Oil Co.* v. *Khan*, 522 U.S. 3, 20 (1997); *Agostini* v. *Felton*, 521 U.S. 203, 237 (1997); *Rodriguez de Quijas* v. *Shearson/American Express, Inc.*, 490 U.S. 477, 484 (1989) ("If a precedent of this Court has direct application in a case, yet appears to rest on reasons rejected in some other line of decisions, the Court of Appeals should follow the case which directly controls, leaving to this Court the prerogative of overruling its own decisions."). It cannot be gainsaid that the holding in *324 Liquor* and the reasoning in *Midcal* have direct application to Total Wine's preemption challenge to the Connecticut statutes at issue here. Those holdings should be followed by this Court, even if the Court were otherwise

inclined to believe, as the District Court apparently believed (and as Appellees strenuously contend), that *Leegin* overruled both *Midcal* and *324 Liquor sub silentio*, and dictated the application of "rule of reason" analysis to the vertical aspects of the Connecticut price regime.

Second, and more fundamentally, the District Court's principal error lay in its failure to recognize the *horizontal* aspects of the Connecticut statutes, and its decision to follow this Court's decision in *Battipaglia* v. *New York State Liquor Authority*, 745 F.2d 166 (2d Cir. 1984), rather than the Supreme Court's later opinion in *324 Liquor*. There is little question but that the critical analytical issue presented by this case is whether the pricing arrangements mandated by Connecticut law are "regarded by the [reviewing] court as fundamentally vertical or horizontal." Herbert Hovenkamp, PRINCIPLES OF ANTITRUST § 17.1, at 599 (2017). According to the leading antitrust scholars, statutory post and hold provisions in the liquor industry, like those at issue here, "look more like horizontal restraints and *Leegin*'s rule of reason for resale price maintenance did not apply to them." Instead:

> "These statutes require liquor resellers to 'post,' or publish, their resale prices and then promise not to deviate from those prices for a defined period of time such as thirty days. That kind of activity looks much more like a horizontal price fix than an act of resale price maintenance."

Id. (citing *TFWS, Inc*. v. *Schaefer*, 2007 WL 2917025 (D. Md. 2007), *aff'd*, 572 F.3d 186 (4th Cir. 2009)).

Finally, in this case, the horizontal price fix authorized by Connecticut law applies not only to the mandated adherence by all wholesalers to their posted case prices, but to the mandated adherence by all retailers to the wholesalers' posted minimum bottle prices as well, extending the impact of the horizontal price restraints to the retail level of the distribution chain, in such a fashion as to preclude any form of price competition, either within brands or between brands. In *Midcal* and *324 Liquor* it was the fact that the statutes at issue removed consumer pricing decisions from the retailers and had the effect of completely eliminating price competition throughout the industry that led the Supreme Court in each case to find that the statutory regimes were facially invalid under the Sherman Act. Nothing in *Leegin* even hints that state-mandated price posting requirements that eliminate all forms of price competition at both the wholesale and retail levels of industry-wide distribution channels should be viewed as anything other than unlawful *per se*, and thereby subject to Sherman Act preemption.

VI. *Battipaglia* Is Distinguishable And In Any Event Should Not Be Followed

Total Wine maintains its position that this Court's divided opinion in *Battipaglia* was wrongly decided, even if one were to accept the view, contrary to the criticisms of other federal appellate courts and leading commentators, that a post and hold law at the wholesale level does not necessarily mandate horizontal price fixing that is *per se* unlawful. *See* Br. for App'nt at 42-49. But this Court's

review of the New York statutes at issue in *Battipaglia*, some of which were later modified and then almost immediately invalidated by the Supreme Court in *324 Liquor*, was limited. Most critically, the *Battipaglia* Court noted that the mandated price schedules required of wholesalers had "no controlling effect on retail prices" because of an earlier ruling by the New York Court of Appeals that a section of the price control laws prohibiting retail sales at prices less than those established in a retail price schedule was itself unconstitutional under the Sherman Act. *See* 745 F.2d at 172 (describing *Mezzetti Associates, Inc*. v. *State Liquor Authority*, 51 N.Y. 2d 761 (1980)).[8] Thus, the *Battipaglia* majority distinguished *Midcal*, and was able to determine that the New York statute "merely requires wholesalers to post and adhere to their own unilaterally determined prices *and nothing more*." 745 F.2d at 172 (emphasis added).

Total Wine's challenge to the Connecticut pricing regime is not just a challenge to a requirement that the wholesalers post and adhere to unilaterally

[8] *Mezzetti* itself was an unusual decision. The challenged New York statutes had been upheld by a panel of the Appellate Division. *Mezzetti Associates, Inc*. v. *State Liquor Authority*, 66 A.D.2d 800 (2d Dep't 1978). A concurring judge indicated that he believed the New York statute in question should be struck down under the Sherman Act based on the reasoning of the California Supreme Court in *Rice* v. *Alcoholic Beverage Control Appeals Bd*., 21 Cal. 3d 431 (1978), although he conceded that *Rice* was itself inconsistent with a prior controlling decision of the Appellate Division. Following an appeal, and reargument in the New York Court of Appeals after the Supreme Court issued its decision in *Midcal*, that Court issued a brief, one sentence opinion reversing the judgment of the Appellate Division, "annulling" the determination of the State Liquor Authority, and citing only the Supreme Court's decision in *Midcal*.

determined prices "and nothing more." The Complaint here alleges much more – including a statutory scheme that authorizes the wholesalers to manipulate case and minimum bottle prices so as to fix retail price floors and profit margins across the entire industry, and that authorizes coordinated price postings by intrabrand wholesale competitors that magically track each other's posted and held case and minimum bottle prices every month down to the penny, and without deviation. *See, e.g.*,Note 4 *supra*. Even if it had been correctly decided, which it was not, *Battipaglia* did not mandate the District Court's dismissal of Total Wine's Complaint for failure to state a valid preemption claim.

In an effort to buttress their reliance on *Battipaglia* as a controlling precedent for this case, one group of Intervenors has engaged in an extensive discussion of this Court's later decision in *E.I. du Pont de Nemours & Co.* v. *F.T.C.*, 729 F.2d 128 (2d Cir. 1984). *See* Combined Br. of Int. App'ees, at 33-34. But that decision merely stands for the general proposition that price sharing among competitors, combined with "most favored nation" clauses in customer contracts, did not qualify as an "agreement" within the meaning of the Sherman Act. The *du Pont* decision has no relevance here, except to the extent that it supports Total Wine's argument, which may be why the case was not even cited by the State Defendants nor by Brescome Barton in their briefs.

The *du Pont* case was decided in 1984, three years before *324 Liquor* held that an agreement was *not* required to establish a violation of the Sherman Act *in the context of a challenge to hybrid statutory restraints against competition in the alcoholic beverage industry*. 479 U.S. at 345, n.8. The *du Pont* case addressed the *private* practices of four domestic sellers of lead antiknock additives to gasoline. This Court explained that at the time of the litigation, lead additives were being phased out and thus the entire industry was dying, which meant that price competition was essentially meaningless. *See* 729 F.2d at 141. Even then, however, the Court noted that the four participants competed on price through "secret" or "hidden" discounts, *see id.* at 132, 141 & n.12, and through other forms of nonprice competition that would not be permitted in Connecticut's alcoholic beverage market. For example, the Court observed that "the giving of … advance notice of a price increase did not preclude the initiator, upon finding that competitors did not follow, from rescinding or modifying the increase or extending its effective date at any time prior to the end of the 30-day period." *Id.* at 134 & n.6. That sort of flexibility is totally absent from the statutory regime at issue here.

Finally, the *du Pont* case was decided based on a full evidentiary record after trial before an ALJ, and this Court repeatedly observed that the record lacked *evidence* supporting "a causal connection between the challenged practices and market prices." *Id.* at 141. In this case, of course, undisputed evidence attached to

the Complaint supports exactly that connection – but all of the Appellees insist that this Court must ignore that evidence.

CONCLUSION

For all the reasons set forth herein, and those set forth in Total Wine's opening brief, the District Court's judgment dismissing the Complaint for failure to state a claim should be reversed, and the case remanded for further proceedings.

Dated: October 10, 2017

Respectfully submitted,

/s/ William J. Murphy

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CERTIFICATE OF COMPLIANCE

In conformance with Rule 32(a)(7)(C) of the Federal Rules of Appellate Procedure, the foregoing brief is in 14-point Times New Roman proportional font and contains 6,164 words. Accordingly, the brief complies with the type-volume limitation set forth in Rule 32(a)(7)(B) of the Federal Rules of Appellate Procedure and Local Rule 32.1(a)(4)(A).

Dated: October 10, 2017

/s/ William J. Murphy
William J. Murphy

Attorney for Plaintiff-Appellant

CERTIFICATE OF SERVICE

In conformance with Rule 25(d) of the Federal Rules of Appellate Procedure and Local Rule 25.1(h)(2), I hereby certify on this 10th day of October, 2017, I caused the foregoing Reply Brief of Plaintiff-Appellant Connecticut Fine Wine & Spirits, LLC to be filed electronically with the Clerk of the Court for the United States Court of Appeals for the Second Circuit through the appellate CM/ECF system, and through that filing to be served on all counsel of record.

/s/ William J. Murphy
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ADDENDUM

STATUTORY ADDENDUM

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Connecticut General Statutes

Sec. 30-63. Registration of brands, fees. Posting and notice of prices. Brand registration of fortified wine. When departmental approval prohibited.

(a) No holder of any manufacturer, wholesaler or out-of-state shipper's permit shall ship, transport or deliver within this state, or sell or offer for sale, any alcoholic liquors unless the name of the brand, trade name or other distinctive characteristic by which such alcoholic liquors are bought and sold, the name and address of the manufacturer thereof and the name and address of each wholesaler permittee who is authorized by the manufacturer or his authorized representative to sell such alcoholic liquors are registered with the Department of Consumer Protection and until such brand, trade name or other distinctive characteristic has been approved by the department. Such registration shall be valid for a period of three years. The fee for such registration, or renewal thereof, shall be two hundred dollars for out-of-state shippers and fifteen dollars for Connecticut manufacturers for each brand so registered, payable by the manufacturer or such manufacturer's authorized representative when such liquors are manufactured in the United States and by the importer or such importer's authorized representative when such liquors are imported into the United States. The department shall not approve the brand registration of any fortified wine, as defined in section 12-433, which is labeled, packaged or canned so as to appear to be a wine or liquor cooler, as defined in section 12-433.

(b) No manufacturer, wholesaler or out-of-state shipper permittee shall discriminate in any manner in price discounts between one permittee and another on sales or purchases of alcoholic liquors bearing the same brand or trade name and of like age, size and quality, nor shall such manufacturer, wholesaler or out-of-state shipper permittee allow in any form any discount, rebate, free goods, allowance or other inducement for the purpose of making sales or purchases. Nothing in this subsection shall be construed to prohibit beer manufacturers, beer wholesalers or beer out-of-state shipper permittees from differentiating in the manner in which their products are packaged on the basis of on-site or off-site consumption.

(c) For alcoholic liquor other than beer, each manufacturer, wholesaler and out-of-state shipper permittee shall post with the department, on a monthly basis, the bottle, can and case price of any brand of goods offered for sale in Connecticut, which price when so posted shall be the controlling price for such manufacturer, wholesaler or out-of-state permittee for the month following such posting. On and after July 1, 2005, for beer, each manufacturer, wholesaler and

out-of-state shipper permittee shall post with the department, on a monthly basis, the bottle, can and case price, and the price per keg or barrel or fractional unit thereof for any brand of goods offered for sale in Connecticut which price when so posted shall be the controlling price for such brand of goods offered for sale in this state for the month following such posting. Such manufacturer, wholesaler and out-of-state shipper permittee may also post additional prices for such bottle, can, case, keg or barrel or fractional unit thereof for a specified portion of the following month which prices when so posted shall be the controlling prices for such bottle, can, case, keg or barrel or fractional unit thereof for such specified portion of the following month. Notice of all manufacturer, wholesaler and out-of-state shipper permittee prices shall be given to permittee purchasers by direct mail, Internet web site or advertising in a trade publication having circulation among the retail permittees except a wholesaler permittee may give such notice by hand delivery. Price postings with the department setting forth wholesale prices to retailers shall be available for inspection during regular business hours at the offices of the department by manufacturers and wholesalers until three o'clock p.m. of the first business day after the last day for posting prices. A manufacturer or wholesaler may amend such manufacturer's or wholesaler's posted price for any month to meet a lower price posted by another manufacturer or wholesaler with respect to alcoholic liquor bearing the same brand or trade name and of like age, vintage, quality and unit container size; provided that any such amended price posting shall be filed before three o'clock p.m. of the fourth business day after the last day for posting prices; and provided further such amended posting shall not set forth prices lower than those being met. Any manufacturer or wholesaler posting an amended price shall, at the time of posting, identify in writing the specific posting being met. On and after July 1, 2005, all wholesaler postings, other than for beer, for the following month shall be provided to retail permittees not later than the twenty-seventh day of the month prior to such posting. All wholesaler postings for beer shall be provided to retail permittees not later than the twentieth day of the month prior to such posting.

Sec. 30-68k. Price discrimination prohibited.

No holder of any wholesaler's permit shall ship, transport or deliver within this state or any territory therein or sell or offer for sale, to a purchaser holding a permit for the sale of alcoholic liquor for on or off premises consumption, any brand of alcoholic liquor, including cordials, as defined in section 30-1, at a bottle, can or case price higher than the lowest price at which such item is then being sold or offered for sale or shipped, transported or delivered by such wholesaler to any

other such purchaser to which the wholesaler sells, offers for sale, ships, transports or delivers that brand of alcoholic liquor within this state.

Sec. 30-68m. Retail permittees; sales below cost prohibited; exception.

(a) For the purposes of this section:

(1) "Cost" for a retail permittee means (A) for alcoholic liquor other than beer, the posted bottle price from the wholesaler plus any charge for shipping or delivery to the retail permittee's place of business paid by the retail permittee in addition to the posted price, and (B) for beer, the lowest posted price during the month in which the retail permittee is selling plus any charge for shipping or delivery to the retail permittee's place of business paid by the retail permittee in addition to the price originally paid by the retail permittee;

(2) "Retail permittee" means the holder of a permit allowing the sale of alcoholic liquor for off-premises consumption; and

(3) "Bottle price" means the price per unit of the contents of any case of alcoholic liquor, other than beer, and shall be arrived at by dividing the case price by the number of units or bottles making up such case price and adding to the quotient an amount that is not less than the following: A unit or bottle one-half pint or two hundred milliliters or less, two cents; a unit or bottle more than one-half pint or two hundred milliliters but not more than one pint or five hundred milliliters, four cents; and a unit or bottle greater than one pint or five hundred milliliters, eight cents.

(b) No retail permittee shall sell alcoholic liquor at a price below his or her cost.

(c) Notwithstanding the provisions of subsection (b) of this section, a retail permittee may sell one beer item identified by a stock-keeping unit number or one item of alcoholic liquor other than beer identified by a stock-keeping unit number below his or her cost each month, provided the item is not sold at less than ninety per cent of such retail permittee's cost. A retail permittee who intends to sell an item below cost pursuant to this subsection shall notify the Department of Consumer Protection of such sale not later than the second day of the month such item will be offered for sale.

Sec. 30-94. Gifts, loans and discounts prohibited between permittees. Tie-in sales. Floor stock allowance. Depletion allowance.

(a) No permittee or group of permittees licensed under the provisions of this chapter, in any transaction with another permittee or group of permittees, shall directly or indirectly offer, furnish or receive any free goods, gratuities, gifts, prizes, coupons, premiums, combination items, quantity prices, cash returns, loans, discounts, guarantees, special prices or other inducements in connection with the sale of alcoholic beverages or liquors. No such permittee shall require any purchaser to accept additional alcoholic liquors in order to make a purchase of any other alcoholic liquor.

Connecticut Agencies Regulations

Sec. 30-6-B12. Manufacturer and wholesaler price lists to be filed.

(a) Each manufacturer and wholesaler permittee shall, annually, on or before the twelfth day of December, file with the department on forms prescribed by the department one copy of a complete schedule, with each page of such schedule numbered in numerical order, duly verified by the permittee and attested by the backer if an individual or, if the backer is a corporation, by an officer of such corporation, of all alcoholic liquors offered for sale in Connecticut. These lists shall contain with respect to each item: (1) The type of beverage and brand name; (2) the size of the container; (3) the age or per cent and type of neutral spirits; (4) the proof; (5) the number of bottles per case; (6) the bottle price and case price which shall include all customs, duties, federal taxes, state taxes and cost of delivery to the permittee. If a manufacturer or wholesaler sells to another manufacturer or wholesaler, the prices shall be submitted on a separate schedule; (7) the name of the publication or publications the prices will appear in. If not published, the affidavit required by subsection (g) shall be submitted. The following information shall be submitted only by manufacturer and wholesaler beer permittees: (1) The type of beverage; (2) the size of the container (barrel, half-barrel, quarter-barrel); (3) the number and size of bottles per case; (4) the container price and case price; (5) the name of the publication or publications the prices will appear in. If not published, the affidavit required by subsection (g) shall be submitted.

(b) Except in the case of still wines and sparkling wines, the case price shall be individual for each item and not in combination with another item. Schedules on multiple packages of still wines and sparkling wines shall contain the bottle price for each item contained in the multiple package, the unit price, and the

case price. The bottle price posted in such multiple package case must be the same as the bottle price posted in a case containing the one type and brand of wine. The price set forth therein shall become effective on the first day of the calendar month following the effective filing date thereof and, unless withdrawn or amended, shall be considered refiled and effective each month until the filing date of the next complete schedule.

(c) Price changes and prices on new items may be filed on supplemental price schedules, which schedules shall be filed on or before the twelfth day of any month, and the prices on such supplemental schedules shall become effective on the first day of the month following the effective filing date thereof. One copy of such supplemental price schedules showing amended prices shall be filed and only price changes and prices on new items should be listed.

(d) No changes, corrections or additions will be considered after the effective filing date, except in cases where obvious typographical errors have been made and except where otherwise allowed by statute.

(e) No manufacturer or wholesaler permittee may sell or offer for sale any brand of alcoholic liquor which does not appear on his price schedule. All items listed shall be bona fide offerings of the items set forth in the list and each manufacturer and wholesaler, upon request of the department, shall furnish the department with an inventory of any items that appear on his list. All liquor sold in less than case units at wholesale shall be sold at the per bottle price posted.

(f) All liquors shall be shipped and received by the purchaser in the same period for which the prices set forth in the invoices are in effect.

(g) Each manufacturer and wholesaler shall furnish each permittee customer with a copy of his price schedule, as amended, either by direct mail or by publishing his price schedule in any publication approved by the department of liquor control, provided, in accordance with the method used, the manufacturer, wholesaler or publication shall, on or before the tenth day of the month for which such schedule is effective, submit an affidavit that the provisions of this section have been complied with. If a manufacturer or wholesaler permittee solicits a new account, he shall, before making any sales, present a current price schedule to such account.

(h) A manufacturer or wholesaler posting prices on private labels shall submit those prices on separate sheets distinctly marked “Private Labels.”

(i) Each price schedule filed shall contain the statement that the manufacturer or wholesaler is a "present authorized distributor" of all brands on which prices are quoted. If for any reason a manufacturer or wholesaler files prices on any items or brands of which he is not an authorized distributor, such items or brands shall be listed as "close-outs."' Prices on so called "close-out" items shall be filed every month even though they remain the same. Such items shall be disposed of within three months and shall not be listed on more than three successive lists without permission of the department and the department will strike from the list those items unless the distributor presents the department with satisfactory reasons for not doing so.

(j) A violation of any of the provisions of this section shall be punishable by suspension or revocation