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R STREET POLICY STUDY NO. 98
June 2017

COULD ECONOMIC LIBERTY LITIGATION 'FREE THE BOOZE?'

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EXECUTIVE SUMMARY

The South Carolina Supreme Court recently struck down a state law limiting how many liquor retail outlets an individual or business could own within the Palmetto State.[1] According to the court, the only justification for the law was economic protectionism, an improper basis for economic regulation. The case may be a portent for the end of oppressive and protectionist alcohol-regulation regimes across the country, and a sign that the recent revival in economic liberty jurisprudence could be coming to the world of booze.

SOUTH CAROLINA'S RETAIL SERVICES CASE

The court's decision in *Retail Services & Systems v. S.C. Dep't of Revenue and ABC Stores*[2] concerned a several-decades-old state law that limited individual owners to operating no more than three liquor retail stores in South Carolina. Total Wine & More, an alcohol chain-store retailer, applied to open a fourth store in the state but was rejected under the statute, which prompted the lawsuit.

Total Wine argued the statute was unconstitutional under the South Carolina Constitution because: 1) it exceeded the scope of the legislature's police powers; and 2) it violated the state's equal protection and due process protections.[3] Ultimately, the South Carolina Supreme Court agreed on the first point: arbitrarily limiting the number of retail outlets that one could operate inside the state exceeded the scope of the state's police powers.[4]

The court acknowledged the South Carolina General Assembly has broad leeway under the state constitution to regulate alcohol. The constitution states that "[i]n the exercise of the police powers the General Assembly has the right to prohibit and to regulate the manufacture, sale, and retail of alcoholic liquors or beverages," and permits the legislature to "license persons or corporations to manufacture, sell, and retail alcoholic liquors or beverages . . . under the rules and restrictions as it considers proper."[5]

But despite this broad language, the court's majority held the state's grant of power was not unlimited. While the government could use its police powers to "regulate any trade, occupation or business," it must have a proper reason to do so, such as to protect "public health, morals, safety or comfort."[6] Therefore, the state law limiting liquor retail outlets could only be permissible if it was enacted to advance those core police power objectives.

1. Roddie Burris, "SC high court overturns liquor license limit," *The State*, Mar. 29, 2017. http://www.thestate.com/news/business/article141494319.html.

2. Retail Services & Systems v. S.C. Dep't of Revenue and ABC Stores, Case No. 2014-002728, Opinion No. 27709 (2017).

3. Ibid., 2-3.

4. Ibid., 4. The court declined to address the equal protection and due process arguments.

5. S.C. Const. art. VIII-A, § 1.

6. *Retail Services*, Case No. 2014-002728, 4.

It was here that the law faltered. Rather than protecting health, safety, or morals, the court found the law's only justification to be raw economic protectionism. It advantaged smaller, incumbent liquor retail stores over larger chain stores that sought to establish a presence in the state. For this reason, the court held: "Without any other supportable police power justification present, economic protectionism for a certain class of retailers is not a constitutionally sound basis for regulating liquor."[7]

Further, the majority found that there was no indication in the record that the law was motivated by traditional police power concerns like health, safety, or morals because it did not specifically limit the number of liquor stores in a certain area or forbid their geographical placement (such as next to a church or school). Whereas these more limited restrictions could potentially have been justified on health and safety grounds—for example, by keeping alcohol away from minors in school zones—the state law instead set an arbitrary cap on the number of stores that one owner could operate statewide.[8] This, they argued, was a clear indication of economic protectionism.

The dissent conceded that, were economic protectionism the *only* justification, it "might be inclined to join the majority."[9] But the dissent argued that South Carolina had identified other rationales for the law, including that it promoted "trade stability and temperance."[10] Most importantly, according to the dissent, "virtually every other" state court to consider similar laws in other states had upheld them, citing justifications as varied as maintaining trade stability, promoting temperance, preventing monopolies, and protecting against indiscriminate price cutting and excessive advertising.[11]

Rather than closely scrutinize the justifications the state proffered for the law, the dissent argued that courts should seek out "any reasonable hypothesis" for why the legislature might want to cap liquor store ownership—even including rationales that appeared in cases from other states.[12] The dissent concluded by accusing the majority of sitting as a "superlegislature," seeking to turn a mere policy disagreement into a matter of constitutional law.[13]

As close observers of constitutional law will recognize, the approaches taken by the majority and dissent highlight a longstanding and contentious debate about the level of judicial scrutiny that should apply in constitutional lawsuits that involve economic regulations.

RATIONAL BASIS 'WITH BITE'

The fight over how to treat economic liberty under the Constitution has been as lengthy as it has been acrimonious. Under current constitutional jurisprudence, certain types of recognized rights—so-called "fundamental rights"—receive more robust judicial protection (known as "strict scrutiny") than other rights. In order for a government to infringe upon these "fundamental" rights, it must have a compelling interest and adopt the least intrusive means to advance that interest.[14] This requires an inquiry into both the goals of the infringing law and the means the law adopts to achieve those goals.

In contrast, other rights—like economic liberty rights—are accorded a lesser level of protection known as "rational basis" review, which merely asks whether a law is "rationally related" to a "legitimate" government interest.[15] In practice, rational basis review is even more watered down than it appears on paper. In the words of professor Randy Barnett, infringements on economic liberty are routinely upheld so long as a court can "identify any hypothetical reason for why a legislature might have enacted the restriction."[16]

However, Barnett and others have argued this multitiered approach to rights protection was not always predominant in constitutional jurisprudence.[17] Traditionally, courts would engage in an in-depth analysis of the objective and justification of challenged laws to determine whether their purpose was a proper one. If the law in question was enacted "genuinely to serve the public welfare," then it would be deemed legitimate, but if the court found the law to be "arbitrary, unreasonable, or discriminatory," the law could be struck down as beyond the proper scope of the government's powers.[18]

Determining whether a certain state law was proper or "arbitrary, unreasonable, or discriminatory" depended upon how broad one considered a state's "police powers." In his book *Restoring the Lost Constitution*, Barnett retraces the historical meaning of the term "police powers," finding that it generally was taken to mean that states could protect the

7. Ibid., 5.

8. Ibid., 5-6.

9. Ibid., 11.

10. Ibid., 11-13.

11. Ibid., 14.

12. Ibid., 15.

13. Ibid., 14.

14. See, e.g., Washington v. Glucksberg, 521 U.S. 702, 719-22 (1997).

15. See, e.g., Williamson v. Lee Optical of Oklahoma Inc., 348 U.S. 483 (1955); Powers v. Harris, 379 F.3d 1208, 1221-22 (10th Cir. 2004).

16. Randy E. Barnett, "Judicial Engagement Through the Lens of Lee Optical," 19 *Geo. Mason L. Rev.*, 845, 856 (2012).

17. Ibid.; See also, Paul J. Larkin, et al., "Economic Liberty and the Constitution: An Introduction," Heritage Foundation, Special Report. No. 157, Oct. 1, 2014. http://www1.heritage.org/research/reports/2014/10/economic-liberty-and-the-constitution-an-introduction.

18. Barnett, 847, 852.

general public's health, safety and, in some instances, morals.[19] Laws that could not be justified on these grounds were deemed beyond the scope of a state's authority. Before the New Deal, economic regulations were treated no differently than laws abridging other liberties, which meant they could not arbitrarily benefit certain classes of individuals (or economic actors) over others.[20] Such favoritism often amounted to nothing more than discriminatory economic protectionism, which was viewed as outside of a state's police powers, since it had no obvious health or safety rationale.

The most famous example of a court striking down economic-based legislation was of course the Supreme Court's decision in *Lochner v. New York*,[21] which ruled unconstitutional a New York law that limited how many hours bakers could work. While the State of New York argued its baking-hour restrictions were justified on health and safety grounds—*i.e.*, that limiting the number of hours bakers worked could improve their health—the court found this rationale unconvincing and likely a pretext for what it referred to as "other motives" (such as economic protectionism).[22]

Lochner was a highly controversial decision that drew ire from many legal scholars.[23] Despite the fact that the Supreme Court ultimately repudiated *Lochner*, legal observers today are still quick to invoke the "Ghost of *Lochner*," accusing some libertarians and conservatives of trying to engender a return to the "*Lochner* Era" of increased judicial scrutiny of economic regulations.[24]

In modern times, courts frequently uphold economic legislation that arbitrarily benefits certain economic actors over others,[25] with some courts even going so far as to hold that economic protectionism is a proper purpose of governmental action that sits squarely within a state's police powers.[26] The switch from scrutinizing economic regulations to ensure they were not "arbitrary, unreasonable, or discriminatory," to rubber-stamping such infringements for "any hypothetical reason" occurred during the U.S. Supreme Court's New Deal era.[27]

Specifically, in the case of *Williamson v. Lee Optical*, the U.S. Supreme Court "withd[rew] from policing economic legislation," reversing what Barnett characterizes as "150 years" of "traditional police powers jurisprudence."[28] Barnett has summarized the switch as follows:

> [W]here does modern "anything goes" rational basis scrutiny come from? . . . [It comes from] the 1955 Warren Court case of *Williamson v. Lee Optical* in which Justice Douglas replaces the realistic *actual* rational basis scrutiny that was employed by the lower court with a formalist *hypothetical* rational basis that is satisfied so long as a judge can imagine any possible rational basis for a statute.[29]

Recently, however, there has been renewed legal scholarship critiquing the move away from more rigorous scrutiny of economic regulations,[30] along with several recent judicial opinions that have resuscitated this pre-New Deal variety of economic liberty jurisprudence.

For example, in the D.C. Circuit case of *Hettinga v. United States*,[31] which involved the regulation of milk under federal law, Judges Janice Rogers Brown and David Sentelle issued a concurring opinion that criticized the judiciary's abdication of even modest scrutiny of economic regulations. They summarized the history of economic liberty jurisprudence as follows:

> [T]he judiciary's [modern] refusal to consider the wisdom of legislative acts—at least to inquire whether its purpose and the means proposed are "within legislative power"—[would] lead to only one result: "[R]ights guaranteed by the Constitution [would] exist only so long as supposed public interest does not require their extinction." . . . [T]he [Supreme C]ourt ratified minimalist review of economic regulations, holding that a rational basis for economic legislation would be presumed and more searching inquiry would be reserved for intrusions on political rights.[32]

19. Randy E. Barnett, *Restoring the Lost Constitution: The Presumption of Liberty* (Princeton: Princeton University Press, 2014), pp. 322-37.

20. Ibid., pp. 334-35.

21. Lochner v. New York, 198 U.S. 45 (1905).

22. Ibid., 64.

23. See, e.g., David A. Strauss, "Why Was Lochner Wrong?," 70 *U. Chi. L. Rev*. 373 (2003); Jack M. Balkin, "'Wrong the Day It Was Decided': Lochner and Constitutional Historicism," 85 *B.U. L. Rev*. 677 (2005); and Victoria F. Nourse, "A Tale of Two Lochners: The Untold History of Substantive Due Process and the Idea of Fundamental Rights," 97 *Calif. L. Rev.* 751, 753 (2009).

24. See, e.g., Jamin Raskin, "The Ghost of Lochner Sits on the Supreme Court and Haunts the Land," *Huffington Post*, June 2, 2012. http://www.huffingtonpost.com/jamie-raskin/the-ghost-of-lochner-sits_b_1398073.html

25. See, e.g., Locke v. Shore, 634 F.3d 1185 (11th Cir. 2011).

26. See, e.g., Powers v. Harris, 379 F.3d 1208 (10th Cir. 2004).

27. Barnett, "Judicial Engagement Through the Lens of Lee Optical," 856-58.

28. Ibid., 847-48.

29. Randy Barnett, "Strict Scrutiny for Every Law? Remembering the Real Carolene Products," Volokh Conspiracy, Apr. 20, 2012.

30. See, e.g., David E. Bernstein, "Rehabilitating Lochner: Defending Individual Rights Against Progressive Reform" (2011); Larkin et. al, "Economic Liberty and the Constitution: An Introduction," Heritage Foundation, Special Report. No. 157, Oct. 1, 2014; and Thomas Colby and Peter J. Smith, "The Return of Lochner," 100 *Cornell L. Rev*. 527 (2015).

31. Hettinga v. United States, 677 F.3d 471 (D.C. Cir. 2012).

32. Ibid., 481.

This resuscitation has happened in state courts, as well. In *Patel v. Texas Dep't of Licensing and Regulation*,[33] the Supreme Court of Texas, in an opinion authored by Justice Don Willett, struck down a protectionist licensing scheme for eyebrow threaders. After recounting the judicial history that led to the current anything-goes version of the rational basis test for economic liberty concerns, the court adopted what it termed "rational basis with bite," which demands "actual *rationality*, scrutinizing the law's actual *basis*, and applying an actual *test*."[34]

Like the South Carolina Supreme Court in *Retail Services*, the Texas Supreme Court rejected economic protectionism as a proper end of government:

> Government's conception of its own power as limitless is hard-wired. But under the Texas Constitution, government may only pursue constitutionally permissible ends. Naked economic protectionism, strangling hopes and dreams with bureaucratic red tape, is not one of them."[35]

In other words, the Texas Supreme Court restored at least some constitutional safeguards against arbitrary and discriminatory economic regulations, and held that the state's police powers were not unlimited.

The South Carolina Supreme Court's majority and dissenting opinions reflect the fissure between the currently dominant anything-goes version of rational basis and the growing support to restore a rational basis "with bite" test for economic legislation. The *Retail Services* majority simply extended this recent trend of heightened scrutiny for economic regulations into the realm of alcohol, holding that promoting raw economic protectionism is not a legitimate objective of government.

Rather than a straightforward application of this revived economic liberty jurisprudence, however, the *Retail Services* opinion raises novel legal questions, given the long-accepted role of states in regulating and controlling alcoholic beverages.

HEIGHTENED SCRUTINY FOR PROTECTIONIST ALCOHOL LAWS

While protectionist alcohol laws might appear to be nothing more than garden variety restrictions on economic liberty, the role of Prohibition and its subsequent repeal add an additional constitutional dimension when it comes to regulating booze.

Today, nearly every state has a three-tiered alcohol distribution system that maintains a strict wall of separation between alcohol producers, distributors and retailers.[36] Even more stringent are the numerous states in which the government still controls alcohol distribution.[37] In addition to these structural restrictions, close observers would have no difficulty finding arbitrary, bizarre, and overtly protectionist alcohol laws in nearly every state in the union.[38] From Virginia's food-beverage ratio law, which arbitrarily mandates how much booze versus food a restaurant can sell,[39] to Indiana's cold beer law, which only allows liquor stores (but not gas stations or grocery stores) to sell refrigerated beer,[40] the examples are legion.

In many ways, state and local alcohol laws are ground zero for cronyist and protectionist legal regimes, which makes this area ripe for a more robust application of economic liberty-based constitutional litigation. However, whether more courts will adopt South Carolina's approach and start rigorously scrutinizing booze laws is an open question, given the broad power states are recognized to possess over alcohol.

While many present-day Americans celebrate Repeal Day and the ratification of the 21st Amendment, which repealed the 18th Amendment and thus ended nation's 13-year experiment with Prohibition, few appreciate the broad authority the 21st Amendment transferred to state governments to control and regulate alcohol within their borders.[41]

In fact, the language of the 18th Amendment is remarkably similar to that of the 21st, except that the 21st Amendment

33. Patel v. Texas Dep't of Licensing and Regulation, 469 S.W.3d 69 (Tex. 2015).

34. Ibid., 98.

35. Ibid., 122.

36. Kevin Kosar, "Finding a 21st Century System for Booze," *American Spectator*, Nov. 3, 2016. https://spectator.org/finding-a-21st-century-system-for-booze/.

37. Matthew Brouillette, "For Separation of Booze and State," *National Review*, Sep. 3, 2015. http://www.nationalreview.com/article/423463/separation-booze-and-state-matthew-brouillette.

38. C. Jarrett Dieterle, "Think Prohibition Is Over? Nope. It's Still Making Booze Pricy And Hard To Get," *The Federalist*, Oct. 19, 2016. https://thefederalist.com/2016/10/19/think-prohibition-nope-still-making-booze-pricy-hard-get/.

39. C. Jarrett Dieterle, "Welcome to Virginia, Where the whiskey is strong and the government's stronger," *American Spectator,* Aug. 15, 2016. https://spectator.org/welcome-to-virginia-where-the-whiskeys-strong-and-the-governments-stronger/.

40. Brian Slodysko, "Indiana Senate committee advances bill to close cold beer sales loophole," Chicago Tribune, Mar. 29, 2017. http://www.chicagotribune.com/news/nationworld/midwest/indiana/ct-indiana-cold-beer-sales-loophole-20170329-story.html.

41. John Foust, "State Power to Regulate Alcohol Under the Twenty-First Amendment: The Constitutional Implications of the Twenty-First Amendment Enforcement Act," 41 *B.C.L. Rev*. 659, 678 (2000) ("In addition to repealing national prohibition, the Twenty-first Amendment of the Constitution grants the states broad authority to regulate the subject of alcoholic beverages."); Sidney J. Spaeth, "The Twenty-First Amendment and State Control over Intoxicating Liquor: Accommodating the Federal Interest," 79 *Cal. L. Rev.* 161 (1991) ("The hard lesson learned from nationwide prohibition was formalized into the twenty-first amendment, which gives states vast power to regulate the importation, distribution, and transportation of alcoholic beverages within their borders").

gave prohibitory powers over alcohol to *states* rather than to the federal government. The 18th Amendment prohibited the "manufacture, sale, or transportation," as well as the importation and exportation of "intoxicating liquors" within the United States,[42] whereas the 21st Amendment prohibits the "transportation or importation into any state" of "intoxicating liquors" if doing so is "in violation of the laws thereof."[43]

As legal scholars like Baylen Linnekin have noted, the 21st Amendment "basically transferred the language from federal prohibition and made it essentially state prohibition," giving states near plenary power over alcohol.[44] Unsurprisingly, state governments rushed to fill the gap left by Prohibition's repeal, which resulted in a dizzying array of state laws concerning spirits. Many state constitutions mirror South Carolina's in explicitly laying out the state's comprehensive ability to legislate and regulate liquor, underscoring the broad powers enjoyed by states in this area.[45]

Furthermore, given alcohol's intoxicating tendencies, it's rarely difficult for states to justify their restrictions over the alcohol trade based on legitimate public health and safety concerns. As the U.S. Supreme Court has put it:

> The police power of the state is fully competent to regulate the [alcohol] business, to mitigate its evils, or to suppress it entirely. There is no inherent right in a citizen to thus sell intoxicating liquors by retail. It is not a privilege of a citizen of the state or of a citizen of the United States. As it is a business attended with danger to the community, it may, as already said, be entirely prohibited or be permitted under such conditions as will limit to the utmost its evils. The manner and extent of regulation rest in the discretion of the governing authority.[46]

As the dissent in *Retail Services* was also quick to point out, "virtually every other court" that has considered state alcohol-licensing laws similar to South Carolina's has upheld them against constitutional challenges.[47]

To be sure, the Supreme Court has found at least some limits on state power under the 21st Amendment. For example, in *Granholm v. Heald*,[48] the Court struck down state laws banning out-of-state wineries from directly shipping their products to consumers. *Granholm*, however, relied on Dormant Commerce Clause reasoning to hold that the 21st Amendment did not permit states to discriminate against out-of-state producers in favor of in-state ones. The Court was careful to note that states still had "virtually complete control" over the liquor trade within their borders.[49]

CONCLUSION

Although state powers are at an apogee in the realm of alcohol regulation, *Retail Services* has shown how, in at least some states, the government's power over booze may still be subject to some limitations. If more courts begin to conclude that some ends—such as promoting economic protectionism—remain beyond state governments' proper police powers, it could usher in an era of booze-related economic liberty litigation.

Whether more courts follow the South Carolina Supreme Court's lead remains to be seen, but many state booze laws across the country would certainly provide ripe targets for challenge.

This policy study originated as a three-part blog post series for the Federalist Society for Law and Public Policy

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42. U.S. Const. amend. XVIII, § 1.

43. U.S. Const. amend. XXI, § 2.

44. C. Jarrett Dieterle, "So Many Drinks Laws: An Interview with Food Policy Expert Baylen Linnekin," *American Spectator*, Feb. 28, 2017. https://spectator.org/so-many-drinks-laws-an-interview-with-food-policy-expert-baylen-linnekin/.

45. See, e.g., Idaho Const. art. III, § 26 ("From and after the thirty-first day of December in the year 1934, the legislature of the state of Idaho shall have full power and authority to permit, control and regulate or prohibit the manufacture, sale, keeping for sale, and transportation for sale, of intoxicating liquors for beverage purposes."); Mich. Const. art. IV, § 40 ("[T]he legislature may by law establish a liquor control commission which, subject to statutory limitations, shall exercise complete control of the alcoholic beverage traffic within this state, including the retail sales thereof."); and Tex. Const. art. XVI, § 20(a) ("The Legislature shall also have the power to regulate the manufacture, sale, possession and transportation of intoxicating liquors, including the power to establish a State Monopoly on the sale of distilled liquors").

46. Crowley v. Christensen, 137 U.S. 86, 91 (1890).

47. *Retail Services*, 8.

48. Granholm v. Heald, 544 U.S. 460 (2005).

49. Ibid., 488.