
No. 07-2108

**IN THE UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT**

TFWS, INC.,
T/A Beltway Fine Wine & Spirits,
Plaintiff-Appellee,

versus

PETER FRANCHOT, et al.,
Defendants-Appellants,

On Appeal from the United States District Court
for the District of Maryland
(William D. Charles, District Judge)

REPLY BRIEF OF APPELLANTS

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1 reserved to the state under the 21st Amendment and the
2 state amply substantiated those interests.

3 Let me begin, if I may, with the second of
4 those grounds, because, as I recall, that's roughly where
5 we left off three and a half years ago.

6 At that time TFWS urged this Court as it has in
7 this round to affirm on any plausible ground that appears
8 anywhere in the record. That's the standard the Court
9 actually did apply and it was left at the end with a
10 definite firm conviction a mistake had been committed.

11 So this Court went through and having examined
12 all the evidence in this case, as it said, and as TFWS
13 asked it to, concluded the only evidence in the record
14 aside from two exhibits submitted post-trial by TFWS, and
15 I'll come to those, showed that the evidence was to the
16 contrary of what TFWS claimed; namely; that Maryland
17 prices were not raised and elevated as they claimed in
18 their complaint and as the rest of the records showed,
19 which would have, of course, a consumption reducing
20 effect and thereby promote the state's interest in
21 fostering temperance.

22 The Court nevertheless offered TFWS an
23 opportunity to go back to the District Court and let the
24 District Court explain why it might be that one of the

1 errors we had identified in that late analysis was, could
2 be rectified.

3 JUDGE: But remand was limited to the one area,
4 wasn't it, that was the effect of excise taxes?

5 MR. BROCKMAN: That was the, the one that the
6 Court identified in its opinion.

7 JUDGE: Yes.

8 MR. BROCKMAN: We had pointed out several
9 problems, both evidentiary and procedural in nature and
10 methodological.

11 JUDGE: My recollection is the only thing we've
12 found wrong was the failure to take into account excise
13 taxes.

14 MR. BROCKMAN: Your recollection, of course, is
15 better than mine. The way I would have --

16 JUDGE: No, it seems to me that Judge Michael's
17 question points out a concern that I have and that is the
18 remand was limited and for a limited purpose and what you
19 seem to want to do is to re-litigate the case from square
20 one as if the previous decisions of the Court really had
21 no affect. I mean, what about the law of the case?
22 Aren't we precluded from re-litigating the ban on volume
23 discounts and the price schedule filing or hybrid or
24 unilateral restraints? I mean, isn't that water over the

1 dam; hasn't that been settled?

2 MR. BROCKMAN: Well, there are two ways in
3 which the law of the case enters into this case. I was
4 actually trying to talk about the second way, which is
5 what TFWSIII held and what the terms of the remand were
6 and what the effects of those remand proceedings were.

7 You're right, our brief also asked the Court to
8 take a closer look at some of the determinations that
9 were made when we came up here after having one of our
10 motions dismissed and those include --

11 JUDGE: But to be pointed about it, you seem to
12 say, well, this Leegin case in 2007 should cause us to
13 re-examine the earlier holding that these were unilateral
14 restraint. And but if Leegin really on point? That
15 dealt with a variable price maintenance and what we're
16 dealing with here is something different?

17 MR. BROCKMAN: I think Leegin has very
18 tangential relevance to the, to our call for the Court to
19 go back and look at some of those prior determinations.

20 JUDGE: And what authority do we have to re-
21 examine those earlier holdings just as a matter of
22 Circuit precedent?

23 MR. BROCKMAN: Well, I don't agree that it's
24 Circuit precedent. We're talking about law of the case

1 here.

2 JUDGE: That's probably even stronger.

3 MR. BROCKMAN: Oh, well, that's not my
4 understanding, the doctrine, what the Supreme Court has
5 said about law of the case is that a Court has the power
6 to re-visit prior decisions of its own of a Court in any
7 circumstance and should readily do so where, when that's
8 in Christianson versus Polk Industries.

9 JUDGE: What would that do to the District
10 Court who examined, who went through a four-day trial
11 under one set of instructions and we just, and then the
12 thing comes up on appeal and we way, well, that was all
13 for naught, we're going to go back and --

14 MR. BROCKMAN: Well, I sure hope we don't have
15 to go back. I think Mr. Murphy probably agrees with me.
16 And I think the reliance interest that law of the case
17 recognizes are here relatively minimal. I think most of
18 the people who have an interest in perpetuating the rules
19 that were laid out in that interlocutory appeal in TFWSI
20 were, are represented in this courtroom.

21 And my understanding of the law of the case
22 doctrine is not anywhere near, it's not as confining as
23 say stare decisis or intervening done by a higher Court.
24 It's, the Supreme Court in another case says it simply

1 expresses the common judicial practice. It does not
2 limit the Court's power and that's Castro versus the
3 United States.

4 So we don't have to have you revisit all of
5 TFWSI in order to win this case. We've won it now
6 several times in the District Court where the District
7 Court followed what it thought were the TFWSI
8 instructions.

9 We think that revisiting TFWSI would produce
10 better law of the Circuit and we'd welcome that. But if
11 I can I'll explain why we did win even under the approach
12 that TFWS has urged here.

13 And so where we left off was that this Court
14 had concluded the record as a whole supported the state's
15 position that prices were elevated by the, as an effect
16 of these regulations with the exception of two exhibits
17 that they submitted, which had all of these defects that
18 we'd identified.

19 And getting back to your question, Judge
20 Michael, yes, the opinion rested only on one, which was
21 the exclusion of an omitted variable, a very important
22 one. The District Judge had not been asked to control
23 for excise taxes because this all happened after trial.

24 So and I think the question this Court posed

1 was, well, we're not really sure is 100 percent of excise
2 taxes imposed at the wholesale level then passed on to
3 the retail level where it would affect consumers and
4 therefore affect consumption.

5 The answer to that was resolved very quickly on
6 remand. It was undisputed. The economic literature with
7 which the state's expert, Professor Tuluca, was in at
8 least Miller demonstrates that 100 percent or more likely
9 slightly more than 100 percent of the excise tax is
10 passed on into the retail price.

11 Both sides in the re-analysis of the disputed
12 exhibits by TFWS used a more conservative 100 percent
13 figure. And so that's the excise tax differential that
14 was used to recalculate the figures.

15 So the only thing that was done to those two
16 exhibits was an additional column was added that adjusted
17 for the excise tax differential.

18 When that was done, the effects that they
19 touted three years ago were reversed. It used to say
20 they said that Delaware prices were lower than Maryland's
21 and that therefore the regulations weren't serving their
22 purpose. Now it says they're higher. And that simply
23 cannot overcome the abundant evidence elsewhere in the
24 record.

1 If I may, let me just briefly review some of
2 that abundant evidence, which should satisfy any standard
3 of a review under any assignment of the burden of proof.
4 The better question, we believe is whether the Maryland
5 legislature could rationally believe that this type of
6 proof which support its belief that the means they had
7 chosen to effectuate their stated purpose would be
8 effective.

9 This is by no means an exhaustive list, but
10 TFWS alleged in its complaint that the laws artificially
11 inflate wholesale prices. They stabilize and raise those
12 prices and that the higher wholesale prices lead to
13 retails sales, of course, finally higher prices as the
14 pages 23 to 26 of the joint appendix.

15 Basic economic theory is both parties and their
16 experts agree indicates that raising prices will reduce
17 sales and consumption levels. The elasticities of demand
18 that are understood in modern economics for alcoholic
19 beverages show that there is a price elasticity of demand
20 for these types of products. And so raising prices does
21 reduce consumption.

22 The District Court could have stopped there
23 having confirmed the theoretical predictions, or having
24 confirmed what the legislature thought and what the

1 plaintiffs had alleged then having that substantiated by
2 the common understanding of supply and demand.

3 We went further, though, and I should say, Dr.
4 Overstreet did posit three counter veiling effects. He
5 said well yeah, it raises prices, but there are other
6 ways in which the regulatory system might somehow have
7 counter veiling effects that produce higher consumption.
8 That's where we were in TFWSII when this Court told the
9 District Court it should not have converted cross motions
10 for summary judgment into a bench trial and resolved
11 those theoretical disputes, the one between orthodox
12 economic principles of supply and demand and what Dr.
13 Overstreet had posited.

14 But when we came back on remand Dr. Overstreet
15 admitted he had not done any work to test those
16 hypotheses much less substantiate them.

17 So we went back to trial and then the record
18 went still deeper. Some of it is sitting over there.
19 The state adduced empirical evidence then in addition to
20 the theoretical predictions of economic theory and it
21 tended to confirm, it did confirm the allegations of
22 higher prices in their complaint. It also confirmed the
23 predictions of economic theory.

24 JUDGE: But did the trial judge accept that

1 testimony?

2 MR. BROCKMAN: He accepted it in TFWS, in the
3 proceedings leading to TFWSIII.

4 JUDGE: Okay.

5 MR. BROCKMAN: Okay.

6 JUDGE: I was getting, which TFWS case we were
7 in, you were in.

8 MR. BROCKMAN: I'm now in four standing here.
9 This was in 2003, 2004 that --

10 JUDGE: I'm the only one left here --

11 MR. BROCKMAN: You're the last judge standing,
12 sitting. Mr. Murphy shares that distinction with Mr.
13 Sullivan. I'm a Johnny come lately. I've only been here
14 for like five years. So --

15 JUDGE: The underlying question of import is
16 whether these are unilateral or hybrid restraints.

17 MR. BROCKMAN: Well, that could resolve the
18 entire case.

19 JUDGE: Yeah.

20 MR. BROCKMAN: But even under this Court's
21 analysis in TFWSI and the general principles of which we
22 have no quarrel with, the next step would then be, if you
23 found that there were hybrid restraints, the next step
24 would be to say are they nevertheless valid under the

1 21st Amendment.

2 JUDGE: Do you want to very briefly review of
3 why they're hybrid or why they're --

4 MR. BROCKMAN: Why they're unilateral?

5 JUDGE: Excuse me, why they're unilateral.

6 MR. BROCKMAN: Sure. Let me start with the
7 volume discount ban, which, as the Costco Court in the
8 Ninth Circuit recently recognized is in Washington state
9 as it is in Maryland really the center of the solar
10 system around which a lot of these other regulations
11 revolve and rotate. And that volume discount ban says --

12 JUDGE: Which of these restraints do you think
13 is the most unilateral? I realize you think they're both
14 unilateral.

15 MR. BROCKMAN: I think it's easiest to
16 demonstrate with the volume discount ban.

17 JUDGE: I agree with you.

18 MR. BROCKMAN: Thank you. Because, what that
19 law says to wholesalers here is pick a price and then
20 offer that uniform price to all your purchasers whether
21 they're large or small, whether they're buying in small
22 quantities or in large quantities. It doesn't say
23 anything more than that. And anything more than that --

24 JUDGE: You think the price schedule was much

1 more difficult to defend as a unilateral restraint?

2 MR. BROCKMAN: Well, no, I feel like I can
3 defend that one.

4 JUDGE: Well no, I know you feel like you can,
5 but I just thought, and I'm talking to you in terms of
6 relative difficulty.

7 MR. BROCKMAN: Well, I think it's relatively
8 difficult to explain. And let me explain, I'll move on
9 to the post and hold or price filing system.

10 JUDGE: But your view is of the two, the volume
11 discount ban is more cleanly unilateral?

12 MR. BROCKMAN: I think they're both equally
13 unilateral.

14 JUDGE: I'm not asking you to give up anything,
15 I'm just asking you --

16 MR. BROCKMAN: I think it's harder to explain
17 because of the precedents that this Court relied on in
18 TFWSI. I think a closer examination of those precedents
19 allows a fuller understanding of why post and hold is
20 unilateral.

21 I think volume discount is more important
22 because the entire article to the regime is built around
23 a general prohibition on price discrimination and I see,
24 I'm into my rebuttal time, but the, as a general

1 prohibition on price discrimination and then we have an
2 elaboration of that with respect to volume discounts and
3 we have a post and hold system that not only puts a brake
4 on price wars, as the legislature intended and expressly
5 stated, but also works to enforce --

6 JUDGE: Well, price wars, doesn't that
7 statement itself reveal a price schedule's hybrid nature?

8 MR. BROCKMAN: May I answer? No. It, what it
9 shows is --

10 JUDGE: You're facilitating Sherman Act
11 violations on the part of private parties, which is the
12 very definition of a hybrid restraint.

13 MR. BROCKMAN: No, that's the very definition
14 of a private collusion, that's done notwithstanding the
15 restraint that the state imposes.

16 JUDGE: If you're an aider and the state is an
17 aider and abetter, or if the state is facilitating it.

18 MR. BROCKMAN: No, we don't engage in private
19 conspiracies. All we do is we require that these private
20 parties --

21 JUDGE: (Inaudible).

22 MR. BROCKMAN: I'm sure Mr. Murphy has a
23 different view. I can pick this up later. I'm happy to
24 continue now. But we just tell private parties don't do

1 that and if they go beyond what's actually required by
2 the statutes and do engage in the kinds of price fixing
3 that would be per se illegal, then they're breaking
4 Maryland law, federal law and they're violating the terms
5 of a consent decree to which they are bound.

6 JUDGE: Okay, thank you.

7 MR. BROCKMAN: Thank you.

8 JUDGE: Mr. Murphy?

9 MR. MURPHY: Thank you, Your Honor. May it
10 please the Court, I'm William Murphy. I represent TFWS
11 and TFWSIV. Why don't we start with a quick statement
12 that I think is important to understand this case.

13 In Maryland there are now two wholesale
14 distributors that filed an amicus brief in this case.
15 They filed it as an association of the licensed
16 distributors of Maryland. There are only two of them
17 that control 90 percent of the products that are
18 distributed.

19 So there are, they control 95 percent of the
20 liquor and about 80 percent of the wine, just the two of
21 them. And they post their prices every month. They're
22 required by the statute to do that and they have to hold
23 those prices for a month.

24 And this Court correctly found in TFWSI that

1 that is a classic hybrid restraint. What this Court also
2 found in TFWSI is that the quantity discount ban makes it
3 easier to enforce the prospect of collusion. We've cited
4 a lot of the law review articles that talk about
5 cartelization and if you're going to have a cartel and
6 affect prices and a price regime, it's good to have a
7 policy that says you can't offer any discounts.

8 JUDGE: Let me just to play devil's advocate
9 for a second, isn't the volume discount ban a classic,
10 present a classic example of state immunity? It's simply
11 a unilateral command that the private sector has to obey.

12 I mean, all I'm asking you, just as I asked the
13 previous counsel, isn't there, just for the purposes of
14 argument, isn't there a real difference between the price
15 schedule, which seems to me to be a fairly classic
16 example of a hybrid restraint which facilitates private
17 collusion, and the volume discount ban which seems to me,
18 you know, just a straight out economic regulation, much
19 in the nature of rent control?

20 MR. MURPHY: But --

21 JUDGE: Which, you know, is thought to be an
22 exercise of sovereignty in a more unilateral fashion.

23 MR. MURPHY: I would agree, Your Honor, that
24 it's a tougher case in the abstract. And certainly in

1 Costo, the ninth circuit had that problem.

2 Maryland statute is different. Maryland
3 statute does --

4 JUDGE: From the one in Costco?

5 MR. MURPHY: Yes. Maryland statute does not
6 prohibit volume discounts. It gives to the controller of
7 the state, the ability to decide what the level of
8 discounts will be and the controller decided through a
9 regulation that the level of discounts will be none.
10 There will be none. That's a regulation of the state,
11 it's not part of the statute.

12 We didn't challenge the statute that says in
13 general there should be no discrimination in pricing
14 among the wholesalers. We didn't challenge that. We
15 challenged the regulation that the controller enacted in
16 1948, which the Maryland Court of Appeals initially held
17 was invalid, and then in 1951, when the statute was
18 changed and gave the controller authority, and this is in
19 our statutory addendum, which is attached to our brief.

20 The original 1948 statute actually dictated
21 that there will be discounts, quantity discounts were in
22 effect for a couple of years. Then the price filing was
23 held to be unauthorized by statute. Then the Maryland
24 legislature when back to the drawing boards and passed a

1 new statute, which gave the, which created price filing
2 as a statutory mandate and a general non-discrimination
3 provision --

4 JUDGE: I thought the real question is whether
5 the volume the discount ban in and of itself was
6 unilateral.

7 MR. MURPHY: Well, you could ask that question.
8 But what I'm saying is, that since it's in a regulation,
9 in our case, unlike the Costco case, the centerpiece of
10 this constellation of regulations is not a regulation
11 that the controller enacted on its own authority with the
12 authorization of the legislature, it's the legislative
13 provision that says that there will be price filing in
14 this state and a mandate that there will be no deviation
15 from those prices for whatever reason.

16 JUDGE: Now you're back to the price schedule.

17 MR. MURPHY: That's right, because they work
18 together. And Judge Michael's decision in TFWSI, he
19 concluded that they work together. And I think that's
20 the right way to view it.

21 JUDGE: I went back and read that and I
22 concluded that without much explanation and wish I had
23 said more.

24 MR. MURPHY: If you had said more --

1 JUDGE: With Mr. Brockman's new brief.

2 MR. MURPHY: If you had said more, Judge
3 Michael, maybe Costco would have come out the other way
4 on that issue because the Costco Court was really, I mean
5 they were puzzling about it themselves. They said this
6 is not free from doubt and they certainly had no trouble
7 finding as this Court has found that the price schedule
8 is a hybrid restrain per se violation.

9 JUDGE: It's easier.

10 MR. MURPHY: It's easier.

11 JUDGE: A lot easier.

12 MR. MURPHY: But they work together. And we
13 tried this case.

14 JUDGE: Well, I want you to explain why they
15 work together. I think that, I mean, if they do, I mean
16 maybe I was completely wrong. And I think, I mean, isn't
17 the theory at least that the ban against volume discounts
18 supports post and hold for one reason I guess, if you
19 don't have volume discounts, it's easier to --

20 MR. MURPHY: Here's one way that it works
21 together. I mean, if I'm a retail and I look at the
22 prices of my competitor for a product and I know what I
23 paid for it at wholesale and he's offering it at a price
24 that's lower than my wholesale cost and I think well he

1 must be in violation of the statute, I'm going to turn
2 him in, but he says oh, I got a volume discount. That's
3 why I was able to price it a little lower than your
4 wholesale cost.

5 That upsets the ability of people in the
6 marketplace to enforce the mandate that there be one
7 price. If you allow volume discounts --

8 JUDGE: If you break down the post and hold,
9 then they won't work together, the volume discount would
10 stand on its own, would it not?

11 MR. MURPHY: The regulation, I guess would
12 still be there.

13 JUDGE: But I mean if you struck the post and
14 hold as a hybrid restraint, then the volume discount,
15 then the argument that they work together would no longer
16 be there to condemn the volume discount ban.

17 MR. MURPHY: And I would still argue that it's
18 a hybrid restraint. It creates a situation where you
19 have what would otherwise be a per se violation of the
20 antitrust laws under Catalano versus Target Sales.

21 I mean, the Supreme Court's recent decision in
22 Leegin, as Your Honor has mentioned, it didn't touch at
23 all the fundamentals of the horizontal price restraints
24 that this Court relied upon.

1 JUDGE: And if didn't touch at all, your
2 argument has to be that on this question of hybrid
3 restraint, that we're bound by the law of the case.

4 MR. MURPHY: Yes, I do argue that.

5 JUDGE: What are the prudential reasons and
6 others that you would argue way in favor of just letting
7 that rest?

8 MR. MURPHY: Well, the Court should let it rest
9 because it is decided, it's a decision of a panel of this
10 Court which has been reaffirmed now twice. And hopefully
11 it will be reaffirmed a third time.

12 The parties have litigated the case under the
13 assumption that these two regulations work together. The
14 expert witnesses, none of them were able to separate out
15 what the impact of one of the regulations is separate and
16 apart from the other because they have worked together
17 since 1951 to create a system in Maryland of pricing,
18 which is anti-competitive.

19 JUDGE: Was there any dormant commerce clause
20 challenge --

21 MR. MURPHY: No.

22 JUDGE: Raised against these regulations?

23 MR. MURPHY: No.

24 JUDGE: Why did you go at it, just for my own

1 information, why did you go at through the Sherman Act
2 rather than the dormant commerce clause?

3 MR. MURPHY: Because there is precedent, there
4 was precedent to suggest that both of these types of
5 restrictions were per se violations and hybrid
6 restraints.

7 JUDGE: But do these same, I mean a lot of
8 times you can have a Sherman Act violation and a dormant
9 commerce clause violation, aren't there a number of cases
10 that find both?

11 MR. MURPHY: I don't view this as really a
12 dormant commerce clause case. There is --

13 JUDGE: Why wouldn't this be a dormant, why
14 wouldn't this be an impermissible burden on interstate
15 commerce?

16 MR. MURPHY: Well, there's no discrimination
17 that I see between in state and out of state, which is
18 kind of the classic dormant commerce clause.

19 JUDGE: Then the ban on volume discounts
20 applies to wholesalers in state, wholesalers out of state
21 and the price and hold system applies equally to instate
22 and out of state?

23 MR. MURPHY: All the wholesalers are licensed
24 in Maryland they're all Maryland corporations. We are a

1 Maryland corporation, my client is a Maryland licenced --

2 JUDGE: So at least it's neutral on its face.

3 MR. MURPHY: Right, there's no, on its face
4 there's nothing you can say well this is discriminating
5 against an out of stater. So we've litigated that way
6 and there's a substantial precedent from Miller versus
7 Headland on.

8 The other point I want to raise before I run
9 out of time is, the state is attempting to argue here
10 that in TFWSIII there was a determination that we had
11 lost this case. But for the excise tax issue and it was
12 remanded back on that issue alone.

13 I agree that it was remanded back on excise
14 taxes alone. But there was no determination in this
15 Court's opinion that we had lost at the trial court
16 level. A trial judge had found for us following a trial
17 that we had over five days. And his decision was
18 supported by ample evidence from a lot of different
19 sources, which the state tends to disregard.

20 But the state would like to pretend that if
21 there's some shred of evidence anywhere in the record to
22 support what the state rationally might have thought,
23 that the state should prevail. But that was not the
24 directive that this Court gave to the District Court and

1 it's not the directive that the Supreme Court gave to the
2 Courts reviewing these types of antitrust challenges in
3 Midcal and in 324 Liquor. I mean, the burden was clearly
4 upon the state, once there was a finding that this was a
5 hybrid restraint that was constituted per se violations
6 of the antitrust laws and then the state proffers a 21st
7 Amendment defense, the burden then shifts to the state to
8 prove as this Court says, was this done for some
9 temperance purpose and does the regulation or the
10 statutory scheme work? Is it effective? Is it doing
11 something to actually support a temperance effect.

12 There's been, our position is that the state,
13 in this case, has never presented any reliable evidence
14 that these regulations are doing anything across the
15 state to increase prices. That's only the first step of
16 what they'd have to prove.

17 JUDGE: Or they decreased consumption.

18 MR. MURPHY: Well, that's the second step. I
19 mean, they really can't get to the decrease in
20 consumption argument until they first get to some proof
21 that they're raising prices.

22 And our position is, in the complaint, as the
23 state constantly says, we allege that this affects
24 prices. It does to my client. My client would like to

1 get the advantage of a quantity discount. He'd like to
2 have the ability to bargain for a price that wasn't on
3 the price schedule.

4 He'd like to do both of those things in a full
5 economic system. In most states he could. But in
6 Maryland he can't. It's affecting him.

7 But when you look at the effect of the
8 regulation across the board, which is what the state has
9 to do to prove a temperance effect, if you think about
10 it, if there was suddenly quantity discounts available in
11 the state of Maryland some smaller retailers would see
12 their prices go up from what they used to pay and some
13 larger retailers would see their prices go down.

14 Because, the wholesalers overall are going to
15 try to maintain their profit margins. That's what
16 economic theory teaches us.

17 So if you now have quantity discounts, some
18 people, some retailers are going to get the advantage
19 because they can afford it and they'll get the discount,
20 they'll buy more to get the discount. Other retailers
21 will not.

22 Overall, and this is one of the things that Dr.
23 Overstreet talked about. Overall you don't know what the
24 impact on prices would be statewide. And so when we go

1 into these comparisons of Maryland versus Delaware, we
2 find that there's a confounding effect. These
3 regulations do not have a consistent affect of causing
4 price increases in Maryland.

5 After we took out the excise taxes, which I
6 didn't necessarily think we should have to do, because
7 after all, people buy based on the price that they see in
8 the store. The excise taxes are in there. It's a little
9 hard for Maryland to say that we are trying to decrease
10 consumption by raising prices when they have the lowest
11 excise taxes in the country, bar none on liquor and they
12 haven't changed the tax since 1955.

13 And every time there is a proposal to change
14 the tax the controller files something with the general
15 assembly saying don't do it, we'll lose sales.

16 Now, that's a little hard to equate with their
17 temperance motive. But even putting that to the side,
18 when you look at the whole effect of this --

19 JUDGE: That's okay, but isn't that a policy
20 question? A state kind of has, you know, maybe they're
21 being sort of, maybe they're not facing up to the hard
22 political choices by having a volume discount ban and a
23 post and hold. But wouldn't the state be --

24 MR. MURPHY: Maryland is --

1 JUDGE: Able to do that in order to avoid
2 raising taxes on it.

3 MR. MURPHY: Maryland is in a budgetary crisis
4 again. This has happened now twice. And every time that
5 we're in this budgetary crisis they have raised taxes and
6 licensing fees on every conceivable product. Our sales
7 tax went from five to six percent. But do not touch
8 those excise taxes on liquor. And the reason is, they
9 have the most powerful and effective lobby in the General
10 Assembly.

11 Now, the taxes, put them aside. Let's just
12 look at them without the taxes. What happens with these
13 regulations? The wholesalers have a very elaborate
14 system of discounts. They don't call them quantity
15 discounts, but they call post off and post on. And so
16 the two big wholesalers that sell 95 percent of the
17 liquor brands that you're familiar with, one guy's got
18 Jim Beam and he'll sell that to a retailer for \$192 a
19 case one month and then the next month he drops it down
20 to \$160 a case. And then the following month it's up to
21 \$192, then it's down to \$160. And it goes like that in a
22 cycle, all throughout the year.

23 JUDGE: Why?

24 MR. MURPHY: It helps them sell what they want

1 to sell when they want to sell it. That wholesaler has
2 Jim Beam and he might have Jack Daniels too, he's got
3 competitive products. And he's got several vodkas and
4 he's got several gins. And he's got them all moving up
5 and down at different times.

6 The net effect, when you look at it, and Dr.
7 Overstreet did some wonderful charts, when you look at
8 that effect, compare the prices in Maryland to the prices
9 in Delaware, overall, often times the Maryland products
10 are cheaper even when you take out the excise tax impact.

11 Often times they're not cheaper. But there's
12 no consistent pattern. And people, people when they buy,
13 I can go to a liquor store and I might want to buy
14 Tanqueray or Beefeater. If I see that my retailer got a
15 deal last month and so his retail price to me on
16 Beefeater is cheaper, I'll buy that. And I can buy it in
17 a big bottle and I can save it for a while and then I'll
18 wait for the Tanqueray price to come down in two months
19 and I'll go buy it then.

20 JUDGE: You know, all this discussion, at the
21 end of the road, aren't we here on a fairly limited
22 question, and that is, there was a four day trial or a
23 five day trial and it was designed to answer the basic
24 question of whether these regulations are related to the

1 asserted stated interest of promoting (inaudible).

2 Now, you know, you can make arguments as the
3 state has, that the state shouldn't be required to
4 justify its enactments empirically and that this
5 restraint is hybrid or this restraint is unilateral.

6 But we're here on something much more finite, much
7 more limited and that is whether there is something wrong
8 with the District Court's holdings that these particular
9 regulations are not related to the whole question of
10 temperance, both in its pricing aspect and in its
11 consumption aspect.

12 MR. MURPHY: There is no question, if you look
13 at the record in this case, all this effect that I talked
14 about boiled down to two cents a bottle. That's what the
15 bottom line conclusion was, for looking at all the
16 products.

17 JUDGE: I mean, what's before us is a very
18 discreet matter.

19 MR. MURPHY: Right. And if the conclusion is
20 that this scheme of regulation, including both the volume
21 discount ban and the price filing, may have caused prices
22 in Maryland to go up on 2637 products by an average of
23 two cents a bottle, how can you possibly conclude that
24 that's going to have an effect on consumers and cause

1 consumers to buy less.

2 I mean, the average price of one of these big
3 bottles of liquor is about \$30 and when you're talking
4 two or three cents a bottle, would the consumer even
5 notice that the price went from \$29.97 to \$29.94? I
6 don't think so. And I don't think the state could
7 possibly contend otherwise.

8 And their expert who crossed with us about
9 which monthly average you should be looking at, which
10 comparison you should make with Delaware and which one
11 with Maryland prices, his conclusion was 30 cents a
12 bottle.

13 And my conclusion on that is the same. Even if
14 it's 30 cents a bottle, it's not enough to cause a real
15 drop in consumption. And in fact, in all of these cases,
16 and if you go back to the Supreme Court opinions from the
17 70's, some state Court opinions from the 60's, when
18 Courts have looked at these issues, there has never been
19 a determination made that one of these regulations
20 actually affects price enough to affect consumption.

21 No Court has ever reached that conclusion
22 because the state has never been able to prove it. These
23 regulations were enacted, initially back in the 30's,
24 40's and 50's as part of the design to protect small

1 retailers and to protect wholesale profit margins and to
2 protect the distillers and the vineyards as well.

3 And all these regulations have had that effect.
4 They have protected high profit margins in this industry
5 and they have prevented competition from being able to --

6 JUDGE: We kind of decided that issue against
7 it, didn't we? We took the legislature at its word.

8 MR. MURPHY: You know, we've had this
9 discussion before, Judge Michael, I don't think so. I
10 mean, the state did throw in, in 1951, for the first time
11 they threw in something into the legislative purposes to
12 say this is a, we're trying to have a temperance effect
13 here.

14 But you know, the reality is, that they never
15 tested it, there were no legislative findings to do that.
16 The statutes stay on the book for 40 or 50 years, they
17 never test it. The first time anybody ever tried to test
18 it was when Dr. Overstreet, our expert tried to test it
19 and then the state hires an expert to sort of counteract
20 what Dr. Overstreet had done. That's the first time they
21 ever tried to look at these issues in any kind of a
22 meaningful way.

23 Because, throughout recorded time and recorded
24 history in Maryland the controller's office always said

1 we are against raising liquor prices because we want to
2 keep local sales of liquor.

3 JUDGE: Okay, thank you, Sir.

4 MR. MURPHY: Thank you, Your Honor.

5 JUDGE: All right, Mr. Brockman, do you have
6 some rebuttal?

7 MR. BROCKMAN: Thank you, Your Honor. Let me
8 pick up on a couple of things Mr. Murphy just said.
9 First, he said that there are two wholesalers who control
10 90 percent of the market. There's a third that actually
11 does a whole lot of business with Mr. Trone with TFWS.
12 Those two though, are under the consent agreement,
13 consent decree that I mentioned earlier and when he
14 starts talking about consolidation of the market and
15 differences between Maryland and Washington, he's all in
16 the world of per se speak. And once you get into the
17 world of per se speak, you're out of the world of
18 preemption under Rice. So that's one point.

19 Another point, we, he talked about Dr.
20 Overstreet's wonderful charts. We reproduced them in our
21 reply brief because we think they are wonderful. Dr.
22 Chaluka had studied the empirical evidence, and this is
23 not price, but consumption. We don't even have to make
24 inferences about the effect of price on consumption.

1 This is consumption data and it's on pages, we've
2 produced it on pages 23 and 24 of our reply brief. The
3 previous page provides the record citations.

4 This is TFWS's chart, this is the state's, the
5 same thing on the following page.

6 JUDGE: You introduced that before Judge
7 (inaudible)?

8 MR. BROCKMAN: We did, at trial.

9 JUDGE: Right, and he --

10 MR. BROCKMAN: It was at trial.

11 JUDGE: And he credited one set of experts over
12 another.

13 MR. BROCKMAN: He did not. He did not credit
14 one set of experts over another. He credited some lay
15 testimony that was introduced post trial over both
16 experts' accord on this question. This is not a
17 divergence of opinion. These two experts agreed that the
18 marvelous social experiment that Delaware performed on
19 our behalf, not so marvelous necessarily for their own
20 temperance interests, but they did what Brandice called,
21 you know, acted as a laboratory of democracy and they
22 abandoned their regulations at the same time that they
23 raised their excise taxes.

24 And nevertheless, where the two states' trends

1 had been roughly parallel, they diverged at that point
2 and Maryland's consumption trends continued to decline
3 while Delaware's began to increase. So we had an accord
4 of experts, not a battle of experts there.

5 The, another point Mr. Murphy made, I think he
6 provided a very cogent explanation of why, in trying to
7 explain why these two regulations have to be bundled and
8 looked at. The explanation he gave was for why the post
9 and hold enforces volume discount, not the other way
10 around.

11 And that not only tells us the could be
12 severed, and volume discount could be left alone. It
13 also tells us how easy it would be to circumvent volume
14 discount if post and hold is removed. And since post
15 and hold is a unilateral restraint, there is no reason to
16 deprive the state of the opportunity to use that very
17 effective enforcement mechanism.

18 So let me just make one last, two last points.
19 If this had been a dormant commerce clause case, where
20 there was interstate discrimination against out of state
21 interests, then we would actually have a standard of
22 review that approximates the one that TFWS has urged the
23 District Court was permitted to apply here, strict
24 scrutiny. We don't have that and no Court, the Supreme

1 Court has never, in any of these cases required that as
2 their definition of what it means to substantiate a state
3 interest on the 21st Amendment.

4 Instead, we've got a problem where the word
5 substantiate, in TFWSI, which it comes from 324 Liquor
6 and Midcal where they talk about unsubstantiated state
7 concerns, unsubstantiated because the state didn't really
8 bother or their state's highest court said they don't
9 matter. Here we have our state's highest court saying
10 they do matter and we do care, as we've shown in this
11 litigation.

12 But if substantiate means that you have to
13 compile a record like that, and if it means that the
14 burden is assigned to the states rather than to the
15 person who is trying to preempt the law, who ought to
16 have to show both that it's in conflict with the
17 antitrust laws, and that it's not, doesn't further 21st
18 Amendment interests.

19 Nevertheless, if it's assigned to us, imagine
20 what the burden of production would look like. Imagine
21 if this challenge were brought on the day after the
22 statutes were enacted. We wouldn't have wouldn't have
23 empirical evidence. Imagine if Delaware hadn't done us
24 the favor of doing this experiment. Again, we wouldn't

1 have a comparison to do, we wouldn't have the 16 year
2 comparison that the experts did at trial and we wouldn't
3 have the one year comparison done based on self selected
4 data from TFWS's own store 12 years later where they
5 didn't supply us with the information and didn't supply
6 their own expert with the information although he agreed
7 that it would have made for a more robust analysis,
8 information about when those products were purchased,
9 which would have allowed them to show whether their
10 heroic assumption about bridge buying was actually a
11 reasonable assumption. Unless there are further
12 questions I know I'm out of time. Thank you, Your Honor.

13 JUDGE: We'll adjourn Court and come down and
14 greet counsel.

CERTIFICATE OF TRANSCRIPTIONIST

I, CAROLYN J. TIMKO, a Verbatim Reporter, do hereby certify that the notes of the foregoing hearing were reduced to typewriting under my direction; that the foregoing is a true record of said hearing to the best of my knowledge and ability; that I am neither related to nor employed by any attorney or counsel employed by the parties thereto; nor financially or otherwise interested in the action.

CAROLYN J. TIMKO
Transcriptionist