

SOME THINGS DON'T AGE WELL: HOW THE LEGACY OF PROHIBITION HURTS CONSUMERS AND SMALL BUSINESSES IN THE MODERN ALCOHOL INDUSTRY

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ABSTRACT

The United States alcohol industry, its production, distribution, and consumption, lies below one of the most complex regulatory structures in the nation, which has diminished competition, undermined small businesses, and diluted consumer buying power. Although the Prohibition era's ban on alcohol distribution and production is a thing of the past, the legal ramifications of its repeal exists today. States have the power to regulate the sale of alcohol in their jurisdiction, with states adopting a three-tier structure to regulate the industry: the tiers separate production and retail by requiring that beverage alcohol be sold through a distributor, effectively forbidding businesses licensed in one tier from operating or holding financial stakes in another.

The effect is an industry that still feels the purposes of Prohibition today; temperance movements created restraints on the system, states can more easily tax alcohol at a higher rate, and economic power is taken from small and mid-sized producers. As a result of the three-tier system, anti-competitiveness between the large businesses festers, consumer prices increase, and local alcohol producers and distributors are inhibited from growing.

This Note describes the changing American drinking culture and the

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underlying role that the federal government played in shaping the alcohol industry before, during, and after Prohibition. Where the growth of the domestic industry led to overconsumption of alcohol and underscored the impetus for the temperance movement and Prohibition, the hasty passage of the Eighteenth Amendment and its rapid repeal in the Twenty-First Amendment has laid the foundation for the current misconceived regulatory structure of the alcohol industry today. Instead of diluting the power of businesses and consumers alike through the three-tiered structure that post-dates Prohibition, the federal government should adopt a standardized system through the Spending Clause where consumers experience a variety of alcohol to choose from and producers, wholesalers, and retailers experience reduced market barriers to grow their businesses. Specifically, allowing a direct small producer-to-retailer sales route and taxing it to correspond with wholesaler markups would be beneficial to the industry and consumer. As the beverage alcohol industry continues to feel the effects of Prohibition and the temperance movement, the regulatory structure of this industry should favor small businesses, local producers, wholesalers, and consumers that make the backbone of this industry.

INTRODUCTION

In the United States, only one consumer product has been regulated by the constitution twice: alcohol.¹ The country has a varied and conflicting relationship with fermentation. Prohibition is the most visceral example of the interchange between government power and sugar-alcohol conversion. The Prohibition period was shaped by the culture of American drinking that dominated the 19th century. In turn, that period has altered our regulatory system today.

The modern alcohol industry is exceedingly vibrant. In 2021, the national industry was valued at 1.9 trillion in total.² Federal revenue from

1. See Mark Edward Blankenship Jr., *A Horse Walks Into a Bar: Comparing Easterbook's Criticized Cyberlaw Analogy of the Study of Alcoholic Beverage Laws & Regulation*, 25 ILL. BUS. L.J. 41, 92 (2020).

2. *Alcoholic Beverages Market Size, Share & Industry Analysis, By Type (Beer, Wine, Distilled Spirits, and Others), By Distribution Channel (Retail [Mass Merchandisers, Specialty Stores/Liquor Stores, Convenience Stores, and Online Retail] and Food Service), and Regional Forecast, 2025–2032*, FORTUNE BUS. INSIGHTS (Aug. 7, 2025), <https://www.fortunebusinessinsights.com/alcoholic-beverages-market-107439> [https://perma.cc/5HTK-CFCF].

alcohol sales reached ten billion dollars in 2019.³ State government alcohol taxes raised over seven billion dollars in 2018.⁴ The Distilled Spirits Council of the United States estimates the industry provides the nation roughly four million jobs in production, distribution, and retail.⁵ Overall, this economic picture shows a lively and expanding industry. Yet, it could do better. The current regulatory structure of the industry is diminishing competition, harming consumers and small businesses, and assisting the largest powers in the industry.

After Prohibition, the federal government granted the individual states powers to regulate the sale of alcohol within their jurisdiction.⁶ Most states adopted a three-tier structure to regulate the industry.⁷ The tiers separate production and retail by requiring that beverage alcohol be sold through a distributor.⁸ With few exceptions in certain states, a business licensed in one tier is forbidden from operating, or holding any financial stake in another.⁹

This forced separation exists for multiple reasons. Stemming from the period after Prohibition, these tiers aim to prevent vertical integration within the industry,¹⁰ advance temperance movements by creating restraints on the system,¹¹ and assist states in taxing beverage alcohol.¹²

The focus on avoiding vertical integration has caused negative repercussions. It has created anticompetitive incentives for large businesses

3. *What are the Major Federal Excise Taxes, and How Much Money do they Raise?*, TAX POL'Y CTR. (Jan. 2024), <https://www.taxpolicycenter.org/briefing-book/what-are-major-federal-excise-taxes-and-how-much-money-do-they-raise> [https://perma.cc/YN8R-ZHM9].

4. *Statistics: State and Local Alcohol Tax Revenue 1977 to 2021*, TAX POL'Y CTR. (July 6, 2023), <https://taxpolicycenter.org/statistics/state-and-local-alcohol-tax-revenue> [https://perma.cc/YE9E-5HYB].

5. *Understanding Jobs in the Alcohol Industry*, OVERPROOF (Mar. 20, 2023), <https://overproof.com/2023/03/20/jobs-in-the-alcohol-industry/> [https://perma.cc/22PY-9H4D].

6. U.S. CONST. amend. XXI.

7. Drew Thornley, *Opening the Taps of Freedom to Distribute Alcohol: An Overview of State Alcohol Regulation in the United States and Recommendations for Reform*, 52 U. PAC. L. REV. 821, 823 (2021).

8. *Id.* at 824.

9. *Id.*

10. Michael B. Newman & Jason H. Barker, *Retying the House: How the Evolution of Prohibition Era Alcohol Beverage Laws Has Facilitated a Generation of Independent Craft Brewers*, 12 BUFF. INTELL. PROP. L.J. 159, 163 (2018).

11. David H. Jernigan, *Economic Competition in the Alcohol Industry Should Not Trump Public Health*, 83 J. STUD. ON ALCOHOL & DRUGS 637, 638 (2022).

12. James C. Cooper & Joshua D. Wright, *Alcohol, Antitrust, and the 21st Amendment: An Empirical Examination of Post and Hold Laws*, 32 INT'L REV. L. & ECON. 379 (2012).

by encouraging horizontal integration within the tiers.¹³ It has increased consumer prices and limited growth opportunities for small to midsized alcohol producers and distributors that add the most dynamism to the alcohol industry, limiting consumer choices and increasing prices.¹⁴

This Note first describes the American drinking culture and the historic role of government policies in shaping the alcohol industry before, during, and after Prohibition. Second, it examines the results of these policies today, with a focus on how the states and federal government can better support small businesses and consumers within the three-tier system and restore competitive balance to the industry.

I. HISTORY

A. *Pre-Prohibition*

Fermentation has been a part of human history since the beginning of civilization.¹⁵ Its production, use, and sale been inextricably linked to state power and policies.¹⁶ Moreover, the consumption of alcohol played a major role in the early history of the United States. The Mayflower landed in Cape Cod, Massachusetts instead of its original target, Virginia, partially due to a fear that the ship's limited beer supply would vanish during a longer voyage.¹⁷

American enjoyment of beer, wine, and spirits between the Revolutionary War and Prohibition had outsized ramifications that directly influenced social and economic life within the country. Up to the Second Industrial Revolution, distilled spirits were the drink of choice within the nation.¹⁸ Prior to the Revolution, rum was the most commonly consumed alcoholic beverage.¹⁹ The American Colonies imported both processed rum

13. U.S. DEP'T TREASURY, COMPETITION IN THE MARKETS FOR BEER, WINE, AND SPIRITS (2022) [Hereinafter Competition Report].

14. *Id.* at 3.

15. Bert L. Vallee, *The Conflicted History of Alcohol in Western Civilization*, SCI. AM. (June 1, 2015), <https://www.scientificamerican.com/article/the-conflicted-history-of-alcohol-in-western-civilization/> [https://perma.cc/QJ5E-G8R8].

16. *Id.*

17. Andrew J. Miller, *Crafting A Better Industry: Addressing Problems of Regulation in the Craft Beer Industry*, 2019 U. ILL. L. REV. 1353, 1357 (2019).

18. W. J. Rorabaugh, *Estimated U.S. Alcohol Beverage Consumption, 1790–1860*, 37 J. STUD. ON ALCOHOL & DRUGS 357, 360 (1976).

19. Livia Gershon, *A Brief History of US Drinking*, JSTOR DAILY (Aug. 12, 2016),

or the ingredients for distillation from British Colonies in the Caribbean.²⁰ The English Prohibitory Acts of 1775, enacted during the Revolutionary War, severely diminished the availability of West Indies sugar products for distillation and finished product rum within the colonies.²¹ The war changed the economies of the United States and the British Colonies. Imports from the West Indies, including sugar products like rum, dramatically decreased.²² The nation's grain exports to the West Indies similarly declined.²³ The westward expansion of the United States brought more farmland to be cultivated, especially for grains like corn.²⁴ The result was a diminished appetite for rum and a surplus of cheap grains that took the place of sugar in the nation's stills. Corn-based whiskey thus arose as a uniquely popular American drink.²⁵

Whiskey became the most popular drink in the United States at a point when consumption as a whole rose.²⁶ The harsh lifestyle of the western frontier made distilling an economic necessity for many farmers.²⁷ Solid grains were expensive and cumbersome to transport. However, a horse would be able to transport six times the amount of produce as whiskey than as grain or meal.²⁸ In 1790, the yearly per capita consumption of absolute alcohol was 5.8 gallons, 2.3 gallons of which were consumed as spirits.²⁹ By 1840, distilled spirit consumption grew to 4.3 absolute gallons, and total consumption rose to 7.1 absolute gallons per capita.³⁰

The rise in spirit consumption did not go unnoticed by the young federal government. Severely in debt from the war, the nation undertook "one of [its] earliest fiscal measures," a whiskey excise tax.³¹ The tax burden fell

<https://daily.jstor.org/a-brief-history-of-drinking-alcohol/> [https://perma.cc/YFH5-QTQ8].

20. W. J. RORABAUGH, *THE ALCOHOL REPUBLIC: AN AMERICAN TRADITION* 225 (1st ed. 1979).

21. Selwyn H. H. Carrington, *The American Revolution and the British West Indies Economy*, 17 J. INTERDISC. HIST. 823, 824 (1987).

22. *Id.* at 827.

23. *Id.*

24. Patrick J. Kiger, *When Whiskey Was the Backbone of the US Economy*, HISTORY (Oct. 7, 2019), <https://www.history.com/news/whiskey-america-economy> [https://perma.cc/J72B-8YYX].

25. *Id.*

26. Rorabaugh, *supra* note 18, at 361.

27. Paul Aaron & David Musto, *Temperance and Prohibition in America: A Historical Overview*, ALCOHOL AND PUB. POL'Y: BEYOND THE SHADOW OF PROHIBITION 127, 135 (Mark H. Moore & Dean R. Gerstein eds., 1981).

28. *Id.*

29. Rorabaugh, *supra* note 18, at 361.

30. *Id.*

31. THOMAS P. SLAUGHTER, *THE WHISKEY REBELLION: FRONTIER EPILOGUE TO THE*

most heavily on areas west of the Appalachian Mountains, where grain surpluses and distillation were most prevalent.³² In a written appeal to Congress, one western farmer wrote “[d]istant from a permanent market, and separate from the Eastern coasts by mountains, we have no means of bringing the produce of our lands to sale either in grain or meal. We are therefore distillers by necessity, not choice.”³³ The federalist Congress passed the tax over these objections. The Whiskey Rebellion started soon after.³⁴ This event was a key test of the new federal government.³⁵ In a show of federal strength, President Washington commanded troops to enforce the new tax in the western regions.³⁶ Alternatively, Thomas Jefferson’s 1800 presidential campaign promised to repeal the tax upon election.³⁷ Jefferson upheld this promise when he repealed the unpopular tax in 1801 during his first year as President.³⁸

After the mid-19th century, spirit consumption and distillation declined as urbanization, population growth, and industrialization limited surplus grain,³⁹ beer and wine became more cheaply available,⁴⁰ and the nascent temperance movement encouraged individuals to switch to lower-strength beverages.⁴¹

Historically, beer was a local production with a short shelf life, and it did not ship well.⁴² Americans rarely produced beer prior to the Second Industrial Revolution. Beer accounted for only 0.1 gallons of absolute alcohol consumed per capita of the population over fifteen at the time.⁴³ The Second Industrial Revolution caused the American population to

AMERICAN REVOLUTION 27 (1st ed. 1988).

32. *Id.* at 73.

33. Aaron & Musto, *supra* note 27, at 135.

34. SLAUGHTER, *supra* note 31.

35. Aaron & Musto, *supra* note 27, at 135.

36. SLAUGHTER, *supra* note 31, at 216 (Interestingly and ironically, after his presidency Washington’s Mount Vernon distillery was one of the nation’s largest in operation).

37. Cynthia L. Krom & Stephanie Krom, *The Whiskey Tax of 1791 and The Consequent Insurrection: “A Wicked and Happy Tumult”*, 40 ACCT. HIST. J. 91, 110 (2013).

38. *Id.*

39. Lara Cockx, Guilia Meloni, & Johan Swinnen, *The Water of Life and Death: A Brief Economic History of Spirits*, 16 J. WINE ECON. 355, 365 (2021).

40. ELINE POELMANS & JOHAN SWINNEN, A BRIEF ECONOMIC HISTORY OF BEER 15 (2012).

41. Aaron & Musto, *supra* note 27, at 140.

42. Martin H. Stack, *A Concise History of America’s Brewing Industry*, ECON. HIST. ASS’N (2003), <https://eh.net/encyclopedia/a-concise-history-of-americas-brewing-industry/> [<https://perma.cc/S3DS-YMG7>].

43. Rorabaugh, *supra* note 18, at 361.

concentrate into urban centers, where more work opportunities were available compared to rural areas.⁴⁴ New immigrants arrived in cities from European regions that favored beer.⁴⁵ At the same time, the new technology of pasteurization extended beer's shelf life.⁴⁶ Additionally, the rise of factory work made it easier to quaff the lower alcohol beverage before, during, and after shifts.⁴⁷ In 1865, Americans were drinking 3.5 gallons of beer per person per year.⁴⁸ By 1910, they were drinking nearly 20 gallons per person each year.⁴⁹

The alcohol industry of the late 1800s was stronger than any other time in the nation's history besides the present day.⁵⁰ The number of licensed breweries peaked in the 1870s at more than 3,200 nationwide.⁵¹ Distilleries were equally vibrant in this period, numbering roughly 6,000 throughout the country.⁵² In the decades before Prohibition, the beer and spirits industries experienced rapid consolidation and conglomeration.⁵³ By 1910, American beer consumption was at its apogee.⁵⁴ By then, the number of breweries in the nation had declined to 1,300, a collapse of nearly 60% compared to forty years prior.⁵⁵ During the 1870s, an average brewery produced two million gallons of beer per year.⁵⁶ By 1910, an average brewery produced forty-four million gallons of beer per year.⁵⁷ An age of massive breweries had arrived! Pasteurization kept beer fresh longer and it was now distributed by a nationwide shipping network connected by railroad.⁵⁸

Local beer production and consumption diminished. Spirit production fared similarly to beer. The number of distilleries contracted to 500 nationwide by 1916, with a similar total production and consumption

44. Stack, *supra* note 42.

45. *Id.*

46. *Id.*

47. *Id.*

48. Rorabaugh, *supra* note 18, at 360.

49. *Id.*

50. David F. Musto, *Alcohol in American History*, 274 *SCI. AM.* 78, 81 (1996).

51. Stack, *supra* note 42.

52. Cockx, Meloni & Swinnen., *supra* note 39, at 386.

53. Stack, *supra* note 42; Cockx, Meloni & Swinnen., *supra* note 39, at 392.

54. Rorabaugh, *supra* note 18, at 360.

55. Stack, *supra* note 42.

56. *Id.*

57. *Id.*

58. *Id.*

compared to forty years early.⁵⁹ The federal government worked closely with these large alcohol companies to expedite tax collection.⁶⁰ Between 1873 and 1916, alcohol taxes accounted for up to 41% of federal tax revenues.

B. Temperance and Prohibition Movements Prior to the Eighteenth Amendment

The Eighteenth Amendment was proposed by congress in 1917, ratified in 1919, and brought into force in 1920.⁶¹ The amendment prohibited the “manufacture, sale, or transportation of intoxicating liquors within, and the importation thereof into, or exportation thereof” all intoxicating liquors within the United States.⁶² Its passage was accompanied by the Volstead Act, passed over a presidential veto.⁶³ The Volstead Act defined intoxicating beverages as anything that contained more than one half percent alcohol. For the next thirteen years, the United States began a “Noble Experiment” as a dry nation.⁶⁴

While the Eighteenth Amendment may have been the start of nationwide prohibition, it was simultaneously the culmination of a century long crusade by various groups with far ranging and dynamic purposes. Temperance began as a reactionary movement against consumption of alcohol in the early 1800s when demand for alcoholic drinks had skyrocketed.⁶⁵ Alcohol consumption was changing just as the country did. The few regulations and laws regarding alcohol consumption were routinely ignored in this period.⁶⁶ As public intoxication became more common, the nascent temperance movement grew in popularity.⁶⁷ Temperance societies appeared across the nation, such as The Union Temperance Society of Moreau and Northumberland in 1808 and The American Society of

59. Cockx, Meloni & Swinnen, *supra* note 39, at 386.

60. John Slack, Goodnight Moonshine: The Lasting Effects of Prohibition on the United States 6 (May 2015) (B.A. thesis, University of Louisville) (on file with ThinkIR, the University of Louisville’s Institutional Repository).

61. Thornley, *supra* note 7, at 845.

62. U.S. CONST. amend. XVIII (repealed 1933).

63. Slack, *supra* note 60, at 11.

64. Jesse D.H. Snyder, *Watering Down the Exceptionalism of the Twenty-First Amendment*, 36 J.L. & POL. 31, 45 (2021).

65. Stack, *supra* note 42.

66. Aaron & Musto, *supra* note 27, at 137.

67. *Id.* at 137–38.

Temperance in 1826.⁶⁸ By 1835, over 1.5 million citizens committed themselves to the mission of temperance.⁶⁹

The temperance movement of the early 19th century had a key difference with its later progeny. These temperance movements were against ardent spirits and actively encouraged the consumption of beer and wine instead.⁷⁰ Those committing to the temperance societies would only swear off distilled spirits.⁷¹

Later, public opinion on temperance and spirits began to correlate with political affiliation. The Democratic-Republicans promoted rural agrarian interests that coincided with distilling.⁷² It was common knowledge that “[t]he whiskey drinkers made Jefferson president.”⁷³ James Madison, the second Democratic-Republican president, was known to drink a pint of whiskey a day.⁷⁴ Founding Father Benjamin Rush, a signer of the Declaration of Independence and head of the U.S. Mint under Federalist John Adams, was a leader of the temperance movement. He stated that “spirits are anti-Federal . . . companions of all those vices calculated to dishonor and enslave our country.”⁷⁵

Temperance movements found meaningful connections in protestant religious organizations, as well as family, women's rights, and anti-immigration movements.⁷⁶ Previously, drinking in the 19th century United States had been a domestic endeavor, enjoyed on the farmstead while at work.⁷⁷ As the national population expanded and urban centers grew, the American lifestyle shifted. Employment outside the home removed men from the domestic sphere for large periods of the day. Drinking was no longer an at home endeavor. Instead, it occurred in pubs, saloons, and

68. *Id.* at 139–40.

69. *Id.* at 140.

70. *Id.*

71. *Id.*

72. Krom & Krom, *supra* note 37, at 110.

73. *Id.*

74. David Von Drehle, *The Demon Drink*, TIME (May 24, 2010), <https://content.time.com/time/magazine/article/0,9171,1989146,00.html> [<https://perma.cc/CGF6-C4UE>].

75. Aaron & Musto, *supra* note 27, at 139.

76. Jed Dannenbaum, *The Origins of Temperance Activism and Militancy Among American Women*, 15 J. SOC. HIST. 235, 235 (1981).

77. Allan M. Winkler, *Drinking on the American Frontier*, 62 Q. J. STUD. ON ALCOHOL 413, 421 (1968).

grogshops.⁷⁸ At the time, these were mainly male spaces.⁷⁹ Many began to link alcohol to the decline in the domestic sphere and family life.⁸⁰ A higher percentage of individual wages would be spent on drinking instead of the family needs.⁸¹ Eventually, as Americans' desire for distilled spirits slowed, the "temperance drinks" of beer and wine became more popular and routinely consumed. However, the social ills that were blamed on alcohol continued. New forms of alcohol and drinking cultures were associated with migrant populations who arrived during the second and third waves of immigration from European countries.⁸² Immigrants from places like Ireland, Italy, and Germany brought with them new libations such as lager beer, malt whiskey, and various wine cultivars. With this new influx, the Protestant-backed temperance movement began to view immigrants' drinking and religious habits as a threat to the country's moral fiber.⁸³

By 1840, the temperance movement had yet to succeed at rectifying the moral ills of the country. This caused a reckoning and recalibration within the temperance cause. Instead of advocating for "temperance drinks," the movement began to encourage abstention from all alcohol. The strategy to attain diminished drinking nationwide adjusted as well. Previously, the temperance movement had advocated for individual changes in consumption. The new prohibition movement, aware of the previous failures of temperance, advocated for legislative changes to achieve their goal.⁸⁴ This reorientation coincided with the first appeals to legislatures.⁸⁵ In 1838, appeals to six state governments were made from temperance groups.⁸⁶ The success of the prohibition movement quickly emerged. In 1827, Maine had a population of 360,000 and manufactured 1,333,160 gallons of distilled spirits.⁸⁷ Maine became the nation's first fully dry state just over twenty years later.⁸⁸ By 1855, numerous states had passed some

78. Aaron & Musto, *supra* note 27, at 137.

79. *Id.* at 142.

80. *Id.*

81. See generally Benson Y. Landis, *Estimated Consumer Expenditures for Alcoholic Beverages in the United States 1890-1943*, 6 Q. J. STUD. ON ALCOHOL 92 (1945).

82. Marie Sarita Gaytan, *Drinking Difference: Race, Consumption, and Alcohol Prohibition in Mexico and the United States*, 14 ETHNICITIES 436, 441 (2013).

83. *Id.* at 442.

84. Aaron & Musto, *supra* note 27, at 140.

85. *Id.*

86. *Id.*

87. L. Ames Brown, *Prohibition*, 202 N. AM. REV. 702, 704 (1915).

88. *Id.* at 715.

form of temperance or high punitive tax on alcohol.⁸⁹ These laws were nearly all retracted or invalidated within a decade.⁹⁰

The force of the prohibitionist movement remained, even if state laws did not. Organized into a political party, the Prohibition Party's 1872 presidential ticket garnered 0.05% of the vote.⁹¹ By 1892, the ticket received 2.25% of the national vote.⁹² The prohibitionist movement continued to connect with Protestantism, women's suffrage, anti-immigration backlash, and progressive political reform.⁹³ The largest prohibitionist organizations in the United States began to target nationwide legislation.⁹⁴ "The evil is a national evil, the sin of perpetuating it is a national sin; God deals with nations as nations, and accepts no expiation for that nation's sin."⁹⁵

The prohibition movement promised that national prohibition would fix the social problems of the day and usher in a utopian society. The many problems at issue included overfilled prisons, poverty, and a decaying family unit. Prohibitionists believed in the idea that national prohibition would create the basis of a new 20th century society: one that was industrious, efficient, and morally upstanding.⁹⁶ The Anti-Saloon League (ASL), founded in 1893, was the leading organization supporting federal reform. The ASL was funded by well-heeled supporters, including the Rockefeller family, who gave over \$800,000 to the ASL by the time Prohibition ended.⁹⁷

The prohibition movement of the 20th century was diverse and motivated by a wide range of ideals. Industrialists desired a more focused working class.⁹⁸ Women's movements were motivated by family values.⁹⁹ Anti-immigrant sentiments associated alcohol with new cultures arriving to the

89. *Id.* at 708–09.

90. *Id.* at 709.

91. Slack, *supra* note 60, at 5.

92. *Id.*

93. Julia Walsh, *The Women's Christian Temperance Union: Demanding Rights and Oppressing Immigrants*, 9 *HISTS.* 48, 51 (2019).

94. Aaron & Musto, *supra* note 27, at 140.

95. Slack, *supra* note 60, at 5.

96. Harry G. Levine, *The Birth of American Alcohol Control: Prohibition, the Power Elite, and the Problem of Lawlessness*, 12 *CONTEMP. DRUG PROBS.* 63, 64 (1985).

97. *Id.* at 72.

98. *Id.* at 63.

99. Walsh, *supra* note 93, at 51. See generally LISA MCGIRR, *THE WAR ON ALCOHOL: PROHIBITION AND THE RISE OF THE AMERICAN STATE* (2015).

country during this period.¹⁰⁰ Finally, protestant religious organization were strong supporters of Prohibition.¹⁰¹

While each group brought different reasons for supporting the prohibition movement, certain grievances were nearly universal. Most prohibitionists distained “Tied-House” saloons.¹⁰² At the time, many saloons across the country were “tied” to an alcohol producer or supplier. A Tied-house is owned or contractually obligated to serve only a specific alcohol supplier’s products.¹⁰³ As most tied-houses were connected with the largest alcohol producers, these businesses were viewed as corporate overreach into a community space.¹⁰⁴ The fear was that tied-houses would be only motivated by profit, without regard for any expense or damage that they caused to a community.¹⁰⁵ In economic terms, these arrangements made the business of running a saloon cheaper. The savings were passed onto the consumers, who would utilize the lower cost to buy more alcohol.¹⁰⁶ Tied-houses were one of the most animating issues to the prohibition movement.¹⁰⁷

One reason state regulations failed in the previous wave of temperance legislation was the Commerce Clause.¹⁰⁸ In the late 1800s and early 1900s the Supreme Court would regularly halt temperance reform or prohibition legislation by a state, asserting such laws to be discriminatory to out of state commerce.¹⁰⁹ The Wilson Act was the first federal reform by the prohibition movement. The act aimed to negate the courts “original packaging” doctrine, that states could not prevent alcohol from being imported if it was

100. See generally Gaytan, *supra* note 82.

101. John Frendreis & Raymond Tatalovich, “A Hundred Miles of Dry”: Religion and the Persistence of Prohibition in the U.S. States, 10 STATE POL. & POL’Y. Q. 302, 306 (2010) (finding strong correlation for ‘dry’ counties with Protestantism and rurality). See generally Lionel Benavidez, Prohibition and Religion: William H. Anderson, the Anti-Saloon League, and The Rise and Fall of a Protestant Evangelical Crusade Against Alcohol in New York (2020) (Master’s Thesis, The City University of New York).

102. Michael B. Newman & Jason H. Barker, *Retying the House: How the Evolution of Prohibition Era Alcohol Beverage Laws Has Facilitated a Generation of Independent Brewers*, 12 BUFF. INTELL. PROP. L.J. 159, 162 (2018).

103. Newman & Barker, *supra* note 10, at 162.

104. *Id.* at 165.

105. *Id.* at 162.

106. *Id.* at 161.

107. *Id.*

108. Alice Vagun, *A Seat at the Bar: Modernizing Alcohol Laws to Meet the Demands of Responsible Consumers*, 54 UIC L. REV. 1011, 1014 (2021).

109. *Id.*

in its original packaging.¹¹⁰ The Wilson Act read, “[a]ll fermented, distilled, or other intoxicating liquors or liquids transported into any State or Territory . . . upon arrival in such State or Territory be subject to the operation and effect of the laws of such State or Territory.”¹¹¹ The court chose to read this law narrowly, constructing it to only take effect once the product was delivered to the person who ordered it.¹¹² In effect, the original packaging doctrine continued past the Wilson Act.

The next federal legislation supported by prohibitionists came in 1910, The Webb-Kenyon Act. Passed over President Taft’s veto, the Act was more explicit than its predecessor.¹¹³ It permitted states to bypass the Commerce Clause by adopting state-wide prohibition.¹¹⁴ The passage of these two acts broadened the perspective and goals of the prohibition movement. Nationwide prohibition became a plausible legislative goal.¹¹⁵

Moreover, outside factors helped broaden the possibilities of the prohibition movement. Alcohol taxes had been the main source of federal government revenue from 1873 to 1915.¹¹⁶ These taxes provided over 50% of federal internal revenue during that period.¹¹⁷ In half of those years, alcohol taxes accounted for 75% of all federal income.¹¹⁸ The Sixteenth Amendment, ratified in 1913, allowed Congress to exercise an income tax as a new way to generate revenue.¹¹⁹ In 1919, the final full year before Prohibition took effect, federal tax revenue from distilled spirits alone was 365 million dollars.¹²⁰ The Sixteenth Amendment was followed by The Income Tax Act of 1913, The Revenue Act of 1916, and the War Revenue

110. Evan W. Saunders, Note, *It’s 1919 Somewhere: What Tennessee Wine & Spirits Retailers Association v. Thomas Means for The National Hangover of The Twenty-First Amendment, The Dormant Commerce Clause, and Federal Legalization of Intoxicating Substances*, 86 BROOK. L. REV. 261, 268 (2020).

111. 27 U.S.C.A. § 121 (West).

112. See generally *Rhodes v. Iowa*, 170 U.S. 412 (1898); *In re Rahrer*, 140 U.S. 545 (1891).

113. Bradley R. Greenman, Note, *The Intemperate Regulation of Alcohol*, 15 J. BUS. ENTREPRENEURSHIP & L. 173, 179 (2022).

114. *Id.*

115. RICHARD F. HAMM, *SHAPING THE EIGHTEENTH AMENDMENT: TEMPERANCE REFORM, LEGAL CULTURE, AND THE POLITY, 1880–1920* 26 (1995).

116. Adam Gifford, Jr., *Whiskey, Margarine, and Newspapers*, in *TAXING CHOICE* 64 (1997).

117. *Id.*

118. *Id.*

119. U.S. CONST. amend. XVI.

120. Farrell Evans, *Why Ice Cream Soared in Popularity During Prohibition*, HISTORY (Jan. 28, 2021), <https://www.history.com/news/ice-cream-boom-1920s-prohibition> [https://perma.cc/7AJ5-F6XZ].

Act of 1917. These legislative accomplishments meant by 1920 over 95% of internal government revenue came from internal tax receipts.¹²¹ Therefore, national prohibition would no longer decimate the federal budget.

C. *The Eighteenth Amendment and Prohibition*

The Eighteenth Amendment was ratified in 1919. At the time, it was the fastest an amendment had gone from proposal to ratification. Prohibition began one year later with the Volstead Act. Prohibition might be viewed as a failure. At the very least, it can be viewed in terms of its unintended consequences and the challenges of legislating behavior.¹²²

Many of the goals sought by Prohibition were never accomplished. Negative effects were widespread. The promised utopia never arrived.¹²³ During this period, alcohol consumption did not decrease and possibly increased.¹²⁴ Underground speakeasies replaced saloons as the centers of social life. New York City had more than 30,000 speakeasies active during Prohibition.¹²⁵ Alcohol laws were routinely violated.¹²⁶ Lawlessness proliferated beyond drinking to a general disregard for the rule of law.¹²⁷ Prison populations increased.¹²⁸ Alternatively, various states were uninterested in enforcing Prohibition. This obliged the federal government to shoulder the enforcement and massive cost of maintaining Prohibition.¹²⁹

Prohibition increased the cost of illegal alcohol, which disproportionately affected the drinking poor and redirected possible government income to criminal enterprise.¹³⁰ The underground alcohol

121. Mark Norris, Note, *From Craft Brews to Craft Booze: It's Time for Home Distillation*, 64 CASE W. RESV. L. REV. 1341, 1352 (2014).

122. MCGIRR, *supra* note 99, at 7.

123. Harry G. Levine & Craig Reinerman, *From Prohibition to Regulation: Lessons from Alcohol Policy for Drug Policy*, 69 MILBANK Q. 461, 464 (1991).

124. Jeffrey A. Miron, *The Effect of Alcohol Prohibition on Alcohol Consumption* 21 (Nat'l Bureau of Econ. Rsch., Working Paper No. 7130, 1999).

125. Snyder, *supra* note 64, at 51.

126. *Id.*

127. *Id.*

128. Mark Thornton, *Alcohol Prohibition Was a Failure*, CATO INST. (July 17, 1991), <https://www.cato.org/policy-analysis/alcohol-prohibition-was-failure> [<https://perma.cc/ADV7-697R>].

129. J.C. Burnham, *New Perspectives on the Prohibition "Experiment" of the 1920's*, 2 J. SOC. HIST. 51, 58 (1968).

130. *Id.* at 62–63.

industry in Detroit was the second largest economic contributor to the city, behind its auto industry.¹³¹ Prohibition changed individual consumption habits as well.¹³² Beer consumption collapsed nationwide. The beverage's bulk and short shelf life were two significant challenges in the underground market.¹³³ Alcohol consumption swung back towards distilled spirits for their discreet nature, ease of transport, and potency.¹³⁴ Consumption of spirits rose dramatically.¹³⁵ Wine consumption also rose in this time.¹³⁶

Prohibition also forced a "democratization and decentralization" in the illegal alcohol industry.¹³⁷ Underground alcohol producers supplied middlemen who transported their products into the hands of speakeasies and consumers.¹³⁸ The majority of legitimate producers within the beer, wine, spirits industries shut down during Prohibition. Some businesses moved underground and began catering to the burgeoning illegal market. The savviest companies were able to pivot to new ventures or markets. The largest breweries were able to use their equipment and land for new purposes.¹³⁹ Anheuser-Busch and Yuengling used their refrigeration and pasteurization equipment for products like milk and ice cream. Coors Brewery entered the ceramics industry using clay deposits near the brewery.¹⁴⁰ Pabst produced over eight million pounds of Pabst-ett brand cheese during Prohibition.¹⁴¹

Distilled spirits were still legal as a prescription medication. The largest

131. Snyder, *supra* note 64, at 51.

132. Levine & Reinerman, *supra* note 123, at 467.

133. *Id.* at 471.

134. *Id.*

135. *Id.* at 467.

136. *Id.*

137. *Id.* at 472.

138. *Id.*

139. Carlos Eduardo Hernandez Castillo, *Technology Adoption and Product Diversification in the Brewing Industry over the Nineteenth and Twentieth Centuries* (2016) (Ph.D. dissertation, University of California, Los Angeles).

140. Christopher Klein, *How America's Iconic Breweries Survived Prohibition*, HISTORY (2019), <https://www.history.com/news/brewers-under-prohibition-miller-coors-busch-yuengling-pabst> [<https://perma.cc/Z2MT-4YUD>]. CoorsTek, the largest laboratory ceramics company in the world, has generated more revenue than the brewery. *Id.*; Dan Alexander, *Inside the Coors Family's Secretive Ceramics Business Worth Billions*, FORBES (Nov. 25, 2015) <https://www.forbes.com/sites/danalexander/2015/11/04/inside-the-coors-family-secretive-ceramics-business-worth-billions/> [<https://perma.cc/CEP8-UUBF>].

141. Levine & Reinerman, *supra* note 123, at 472.

distilleries had the means to get the medical production licensing.¹⁴² During the first years of prohibition, vineyards saw an increase in the value of their farmland.¹⁴³ Some wineries made medicinal or sacramental wine, whose production was still permitted.¹⁴⁴ Other vineyards began to grow thick skinned and hardy wine varieties that could be shipped to large cities for home winemaking.¹⁴⁵

Numerous reasons contributed to the downfall of Prohibition. Many were self-inflicted, while others were fortuitous. The Great Depression was a major factor in Prohibition's repeal.¹⁴⁶ The movement became stratified along party lines.¹⁴⁷ Finally, by 1932, Prohibition had been abandoned by many of elites that once supported it.¹⁴⁸

Pivotaly, the United States' economic depression began in 1929.¹⁴⁹ By 1932, one in four members of the workforce were unemployed.¹⁵⁰ Urban cities felt the crisis deeply, with higher unemployment rates than the nation as a whole.¹⁵¹ These urban centers also held the largest concentration of immigrants and anti-prohibitionists. Agriculture prices were heavily depreciated.¹⁵² The depression shattered the idea that banning alcohol would bring a prosperous utopia.¹⁵³ Instead, many saw the massive cost of upkeeping Prohibition as an unaffordable waste.¹⁵⁴ There was widespread belief that Prohibition took away a potential source of jobs that could help to stimulate the economy.¹⁵⁵ In the middle and upper classes, the depression intensified the belief that Prohibition undermined all laws.¹⁵⁶ One politician argued that ending Prohibition and providing beer to the working class

142. *What Distilleries Were Allowed to Produce During Prohibition?*, SIPPING HISTORY (Jan. 18, 2022), <https://sippinghistory.com/2022/01/18/what-distilleries-were-allowed-to-produce-during-prohibition/> [<https://perma.cc/9Q5A-NT7D>].

143. Levine & Reinerman, *supra* note 123, at 472.

144. *Id.*

145. *Id.*

146. Levine, *supra* note 96, at 70.

147. *Id.* at 71.

148. *Id.* at 77.

149. *Id.* at 68.

150. MCGIRR, *supra* note 99, at 278.

151. *Id.*

152. *Id.* at 277.

153. Levine, *supra* note 96, at 70.

154. Snyder, *supra* note 64, at 51.

155. Levine, *supra* note 96, at 69.

156. *Id.* at 70.

would ease the stress of mass unemployment.¹⁵⁷

Public sentiments against Prohibition meant fertile political terrain for the opposing party. Prohibition gained association with the Republican Party, and many Democrats ran on a repeal platform.¹⁵⁸ Al Smith, the 1928 Democrat nominee, placed repeal front and center in his campaign.¹⁵⁹ This attracted urban workers and immigrant communities to the Democratic Party.¹⁶⁰ Smith lost the election to Herbert Hoover but formed a coalition that future democrats could build on.¹⁶¹

As president, Hoover was trapped between the generally popular repeal movement and his prohibitionist base.¹⁶² Hoover appointed a commission under Attorney General Wickersham with a stated focus on law enforcement and observance, but clearly targeted at the Prohibition issue.¹⁶³ The Commission supported continuing Prohibition, yet the report also mentioned that commissioners were not “convinced that Prohibition under the Eighteenth Amendment is enforceable.”¹⁶⁴ The 1932 election brought a Democratic romp. The party platform explicitly focused on repealing Prohibition.¹⁶⁵ The 72nd Congress was the first to have democratic control in over ten years. The Democratic Party would go on to control the House of Representatives for all but two terms until the 1990s.

Concurrent to the political shift against Prohibition was its rejection by former elite supporters. William Randolph Hearst, a proponent of Prohibition and the Eighteenth Amendment, publicly changed his mind by the mid-1920s.¹⁶⁶ He would later use his editorial strength to run prize contests for alternatives to Prohibition.¹⁶⁷ Perhaps the largest and most influential change came from John Rockefeller, a lifelong teetotaler, when he declared his opposition to the law at the 1932 Republican Convention.¹⁶⁸ Rockefeller's stance was in direct opposition to President Hoover. His

157. *Id.*

158. MCGIRR, *supra* note 99, at 275.

159. *Id.* at 216.

160. *Id.* at 224.

161. *Id.*

162. *Id.* at 280.

163. Levine, *supra* note 96, at 70–71.

164. *Id.* at 70.

165. MCGIRR, *supra* note 99, at 288.

166. Levine, *supra* note 96, at 67.

167. *Id.*

168. MCGIRR, *supra* note 99, at 280.

announcement gave new momentum to repeal, given that he was one of Prohibition's most prominent financial donors. While he supported repealing the Eighteenth Amendment, Rockefeller did not support a return to the Pre-Prohibition system. He commissioned a report to find plausible future solutions. *Towards Liquor Control*, also known as the Rockefeller Report, contained suggestions for state-level regulation that would be adopted across the country.¹⁶⁹

Prohibition came to an end after the 1932 election. However, its influence and legacy did not disappear. The state-level regulations that came after Prohibition are still in place today. The structure and laws governing the alcohol industry are directly influenced by Prohibition and its repeal. The expansion of federal power necessary to enforce Prohibition became a model of federal influence in the mid-20th century and onwards.¹⁷⁰

D. Repeal, The Twenty-First Amendment, and The Modern Industry

The Twenty-First Amendment went from proposed to ratified faster than any other amendment, including the Eighteenth Amendment.¹⁷¹ The amendment echoed the Webb-Kenyon Act by giving regulatory power to the states. In the span of twenty years, alcohol regulation had gone from a local issue, to a federal issue, and finally was given to the power of each state.¹⁷² The repeal movement gained legislative momentum so quickly that outside of the Rockefeller Report, there was little forethought to what state-level regulation might look like.¹⁷³ This meant *Toward Liquor Control* had a premier place in crafting the new policies that would come after Prohibition.

The chief goals of *Toward Liquor Control* were to check the disregard for the law prevalent during Prohibition and provide an active government role in regulating alcohol.¹⁷⁴ If alcohol laws were too restrictive or difficult, the public would ignore them, as they did during Prohibition.¹⁷⁵ The report

169. Levine & Reinerman, *supra* note 123, at 475.

170. MCGIRR, *supra* note 99.

171. Levine, *supra* note 96, at 75.

172. Levine & Reinerman, *supra* note 123, at 475.

173. Pamela E Pennock & K. Austin Kerr, *In the Shadow of Prohibition: Domestic American Alcohol Policy Since 1933*, 47 BUS. HIST. 383, 386 (2005).

174. Levine & Reinerman, *supra* note 123, at 476.

175. *Id.*

gave two main suggestions for state level regulation, retail control or license regulation.¹⁷⁶ Either option would ensure active government oversight of the industry, minimal interruptions to consumer access, and shield consumers from the regulatory interplay between the state and suppliers.¹⁷⁷ In a “control” system, the report’s preferred option, the state would take over all off-premises retail alcohol sales. In this system, the profit motive would be eliminated from the consumer transaction.¹⁷⁸ The control plan was adopted by fifteen states. The licensing plan was the more widely adopted of the two, as many states did not want to own and operate liquor stores. The plans created three tiers, producers, distributors, and retailers.¹⁷⁹ Both the control and the licensing plan provided a mechanism for state regulation at each stage of the process. The plans would minimally impact consumers and co-opting the illegal distribution systems that existed during Prohibition.¹⁸⁰ Tied houses would be prevented, as no license holder in one tier could be connected to another tier.¹⁸¹ Ultimately, nearly every state adopted a regulatory suggestion contained within *Towards Liquor Control*.¹⁸²

The changes in the industry caused by Prohibition and repeal were predictably extreme. Of the 1,300 nationwide breweries at the start of Prohibition, less than 100 survived. These breweries are familiar names today. Anheuser-Busch, Coors, Pabst, Miller, and Yuengling were all breweries able to weather Prohibition. By 2021, Molson Coors and AB-InBev would account for close to 70% of all beer sales revenue in the country.¹⁸³

The diffused and decentralized distilling industry of Prohibition disappeared under the weight of regulatory scrutiny. Within five years of repeal, four distillery corporations would account for up to 90% of all liquor sold in the country.¹⁸⁴ In the California wine industry there were over 700

176. *Id.*

177. Levine, *supra* note 96, at 88.

178. Levine & Reinerman, *supra* note 123, at 476 (“Only as the profit motive is eliminated is there any hope of controlling the liquor traffic in the interests of a decent society. To approach the problem from any other angle is only to tinker with it and ensure failure.” (quoting Rockefeller)).

179. Newman & Barker, *supra* note 10, at 163.

180. Levine & Reinerman, *supra* note 123, at 480.

181. *Id.* at 476.

182. *Id.* at 477.

183. Competition Report, *supra* note 13, at 30.

184. Levine, *supra* note 96, at 86.

wineries statewide prior to Prohibition. By 1932, less than 200 remained.¹⁸⁵ In anticipation of repeal, a number of wineries restarted operations. By 1933, there were 277 wineries licensed in California.¹⁸⁶ E&J Gallo, one of the three largest wine corporations in the United States today, began their first harvest during this wave.¹⁸⁷

The regulatory structures from *Towards Liquor Control* worked surprisingly well at curbing illegal activity and instituting state oversight.¹⁸⁸ The alcohol industry gave the nation a significant new source of needed tax revenue,¹⁸⁹ another market for grains and other agricultural products whose prices had declined during the Depression,¹⁹⁰ and a source of new jobs.¹⁹¹ State oversight became easier if the industry was more consolidated.¹⁹² Along with state-level regulation, the federal government worked concurrently to promote self-regulation in the industry.¹⁹³ In nearly every state and federal regulatory decision, there was a contradiction between promoting public health through temperance and the desire for an expanded source of jobs and tax revenue.¹⁹⁴ The separation of the consumer from the state-industry regulatory scheme meant there was very little popular desire for public oversight of the system. Beer and spirits both experienced rapid consolidations after repeal.¹⁹⁵ The basic regulatory structure of the alcohol industry remains largely the same today.¹⁹⁶

States were successful in preventing tied houses and separating the consumer from production. Meanwhile, in each tier, the market has become less competitive and more conglomerated.¹⁹⁷ The effect was contradictory state action, intense enforcement of tier separation, and vertical integration with a state benefit for consolidation within the mandated tiers. The

185. Julian Hitner, *California and Prohibition: Collateral Damage*, DECANTER (July 21, 2019), <https://www.decanter.com/learn/california-and-prohibition-419995/> [<https://perma.cc/YQ7R-FYQU>].

186. *Id.*

187. *Id.*

188. Levine & Reinerman, *supra* note 123, at 479.

189. Pennock & Kerr, *supra* note 173, at 383.

190. MCGIRR, *supra* note 99, at 279.

191. *Id.*

192. Levine & Reinerman, *supra* note 123, at 478.

193. Pennock & Kerr, *supra* note 173, at 384.

194. Levine & Reinerman, *supra* note 123, at 480.

195. Pennock & Kerr, *supra* note 173, at 390.

196. *See id.*

197. See Jay Brooks, *The Beer Monopoly*, BROOKSTONE BEER BULL. (Feb. 29, 2024), <https://brookstonbeerbulletin.com/the-beer-monopoly/> [<https://perma.cc/5393-9NLX>].

consumer continues to feel these effects indirectly today. Horizontal integration without opportunities to reach the market vertically negatively impacts the modern market, especially for the smallest businesses within each tier.

The beer industry reached its nadir during the 1980s when fewer than 100 breweries were in operation. At the time, the five largest breweries controlled roughly 75% of the market by revenue.¹⁹⁸ The two largest breweries from the 1980s continue to dominate market today. AB-InBev controls 42.4% of the market by revenue. Molson Coors has a market share of 22.4%. Together these two behemoths control roughly 65% of the national beer market.¹⁹⁹ While market concentration has remained static, the number of breweries has grown exponentially since the 1980s. There are over 6,000 breweries currently in operation.²⁰⁰ Of these breweries, 90% make less than 15,000 barrels annually.²⁰¹ The top-heavy concentration is the same for wine and spirits. The top fifteen distilleries produce two thirds of the nation's spirits by proof gallon, close to 300 million gallons per year.²⁰² The smallest 1,500 distilleries produce less than two million total proof gallons per year.²⁰³ As of 2010, the three largest wine producers E&J Gallo, Constellation Brands, and The Wine Group, account for 50% of the total wine market by revenue in the US.²⁰⁴

The distribution tier is similarly concentrated. Wine and spirits are typically distributed together and by separate entities than beer. Each state has slightly different laws, and because of this, many smaller distributors are limited by geographic area. Many states' legislation aims to protect distributors from coercive large suppliers.²⁰⁵ This is seen in multiple ways. First, most states permit a producer to work with only a single distributor.²⁰⁶ Second, the ability to change distributors, even for contractual violations, can be limited and challenging.²⁰⁷ These restrictions harm small alcohol

198. *See id.*

199. Competition Report, *supra* note 13, at 20.

200. *Id.*

201. *Id.*

202. *Id.* at 22.

203. *Id.*

204. Hilary Lipoff & Gina Scurich, Consolidation and Label Acquisition in the California Wine Industry (June 2011) (B.S. thesis, California Polytechnical State University).

205. *See* Thornley, *supra* note 7, at 847.

206. *See* Competition Report, *supra* note 13, at 13.

207. *See* Thornley, *supra* note 7, at 828.

producers and assist the brands with the largest market shares.²⁰⁸ The largest wine and spirits distributors are currently expanding and consolidating as a result. Southern Glazer's Wine and Spirits, the largest distributor by volume, now operates in forty-four states.²⁰⁹ The next largest distributor, Republic National Distribution Company, operates in thirty-five states with plans to operate in five more as of 2021.²¹⁰

In the beer industry, some states allow vertical integration between producers and distributors.²¹¹ For these states, their largest beer distributors are likely either AB-InBev or Molson Coors. In states without this arrangement, the largest beer companies might be able to "affiliate" with independent distributors. These arrangements force the smallest breweries to go through distributors whose business is overwhelmingly focused on major brands.²¹² The current state of the production and distribution tier exhibits massive horizontal integration, with vertical integration existing explicitly, implicitly, or through extreme market leverage. This means competition in the industry today is stifled, the largest companies are entrenched, and finally, the ability for small businesses to enter or expand into new or existing markets is greatly diminished.

II. ANALYSIS

A. Overview

The current state of alcohol regulation is unnecessarily burdensome for all parties involved. The three-tier system is no longer serving the original goals it was created for. Reforms to the three-tier system could encourage better competition and accomplish better policy goals. Businesses in the industry vary greatly in size. Due to this, the equal information cost to understand state regulation or enter a new market unfairly burdens small businesses with less revenue and market leverage. Federal intervention under the Spending Clause could alleviate this imbalance by incentivizing a single, standard, regulatory structure for alcohol sales. Current Supreme Court precedent would permit a federal role like this if the *Dole* test for the

208. *Id.* at 821.

209. Competition Report, *supra* note 13, at 24.

210. *Id.*

211. *See id.* at 25.

212. *Id.* at 26.

Spending Power could be met. A second reform, on the state or federal level, is a direct-to-market exception from three-tier distribution for alcohol producers up to a certain size. Small producers would be able to sell directly to retailers for up to certain percentages of production based on total barrelage. Sales under this exception would be taxed at a similar rate to a distributor markup. This allows distributors to retain a competitive position in the industry. These reforms would ensure that small alcohol producers have better opportunities to compete in the industry and grow their businesses.

B. The Three-Tier System is Failing to Achieve its Goals

Forty-eight states have enacted a three-tier system (TTS) with varying characteristics. These regulatory structures separate alcohol manufacturers, distributors and retailers from one another within the alcohol industry. TTS's aimed to prevent vertical integration, something that had existed profusely prior to Prohibition. The laws advanced three main goals: diminishing alcohol consumption, legitimizing the underground market, and effectively levying taxes through oversight of the industry.²¹³ These aims are inapplicable to, or greatly diminished by, today's alcohol market. Instead of achieving these goals, the current legal structure protects the largest businesses at the expense of industry newcomers, small businesses, and consumers. The current three-tier system is deeply ingrained and does create benefits, such as increased access to disparate markets.²¹⁴ Nonetheless, structural changes could better serve the entire industry and increase consumer welfare.

The goal of integrating an underground alcohol market is no longer applicable today. The country largely follows alcohol laws and rarely resorts to an underground or black markets. States continue to have an interest in the public health benefits of reducing alcohol consumption. Yet, artificially increasing the price of alcohol through the three-tier system is not an efficient or viable means of reducing consumption. Firstly, utilizing private companies to artificially inflate prices instead of applying higher tax

213. See Vagun, *supra* note 108, at 1022.

214. See *The Three-Tier System: A Modern View*, NAT'L ALCOHOL BEVERAGE CONTROL ASS'N (Mar. 1 2024), <https://www.nabca.org/three-tier-system-modern-view-0> [https://perma.cc/7RTD-NT7X].

rates is not intelligent policy.²¹⁵ Cost increases of 10% have been shown to reduce alcohol consumption by roughly 5%.²¹⁶ Yet, cost increases would disproportionately harm craft and small alcohol producers that usually charge more for their products. Cost increases drive consumers to cheaper beer, which is usually made by the largest producers.²¹⁷ Thus, increasing the cost of alcohol would only increase the market share of large producers.²¹⁸ There are better ways for the government to promote alcohol moderation than to disproportionately harm small businesses with price increases. The growth of the administrative state since the end of Prohibition means that the need to co-opt private enterprise to collect taxes is diminished. Multiple states have created taxable exceptions to the three-tier system, such as brewpubs, self-distribution, or direct to consumer shipping. These arrangements have not diminished the state's ability to collect taxes.

The current three-tier system is no longer accomplishing the goals it was originally created to.²¹⁹ Instead, the system reinforces itself and protects the corporate interests that it serves best. The largest companies in each tier can afford state-level lobbying to protect their interests. Alcohol wholesalers are one of the largest industry donors to state legislature campaigns.²²⁰ In some states, breweries have successfully lobbied to obtain distributor licenses. This has benefited only the largest breweries who can afford to operate their own distributor.²²¹ In other states, distributors can choose to align themselves with one of the largest breweries. In some markets, the Molson Coors and AB-InBev aligned distributor controls 90% of beer distribution.²²² This limits the access that local producers can

215. See Thornley, *supra* note 7, at 852.

216. Miller, *supra* note 17, at 1374.

217. See *id.*

218. See *id.*

219. See Greenman, *supra* note 113, at 202.

220. See Phil Williams, *Revealed Extra: Who's Funding Tennessee's Political Campaigns? Liquor Distributors, Realtors top list*, NEWS CHANNEL 5 NASHVILLE (Mar. 15, 2022, 2:11 PM), <https://www.newschannel5.com/news/newschannel-5-investigates/revealed-whos-funding-tennessees-political-campaigns-liquor-distributors-realtors-top-list> [<https://perma.cc/7PV8-F6S9>]; *Wholesale Protection 2018: A Report on Alcohol Wholesaler State Campaign Contributions*, NAT'L ASS'N WINE RETAILERS (Jan. 8, 2018), <https://nawr.org/wp-content/uploads/2018/01/Wholesale-Contribution-Report.pdf> [<https://perma.cc/J8DX-8DP9>] (finding that distributors spent multiple times more than any other sector of the alcohol industry on state congressional campaigns between 2007 and 2016).

221. Miller, *supra* note 17, at 1368.

222. Competition Report, *supra* note 13, at 26.

achieve in their market.²²³

In 2015, AB-InBev announced a “distributor incentive” reimbursement program that could provide up to \$200,000 to distributors, if 98% of their sales were AB-InBev labels.²²⁴ Meanwhile, franchise agreement laws limit how small breweries can, or cannot, terminate agreements with wholesalers. These laws are widely recognized as overly protective of distributors, requiring ‘good faith’ when terminating a distribution agreement. However, failure to sell product or match sale projections is not considered a ‘good faith’ reason to terminate.²²⁵ Many states simultaneously limit distribution rights to only a single entity at a time.²²⁶ Small producers can be obligated to remain with a distributor who is aligned with their competition, who does not attempt to sell their product, and retain no rights to terminate the agreement.

C. A Federal Role

The Twenty-First Amendment was originally considered to leave alcohol regulation to states. Over time, this interpretation has changed. The Supreme Court’s decision in *Granholm v. Heald*, aligned with a more “federalist” view of the Twenty-First Amendment.²²⁷ *Granholm* held that state alcohol regulation under the Twenty-First Amendment had to comply with the Commerce Clause.²²⁸ Earlier, in *South Dakota v. Dole*, the Supreme Court ruled that conditioning highway funds on states adopting a minimum drinking age was an acceptable use of the Spending Clause. The Court decided that the National Minimum Drinking Age Act did not violate the Twenty-First Amendment’s allotment of alcohol regulation to the states. Utilizing the Spending Clause and the current Supreme Court interpretation of the Twenty-First Amendment, Congress should create a standardized regulatory structure for the three-tier system. States should then be encouraged to adopt this system through conditioned spending. Federal

223. Miller, *supra* note 17, at 1368.

224. Tripp Mickle, *Craft Brewers Take Issue With AB InBev Distribution Plan*, WALL ST. J. (Dec. 4, 2015), <https://www.wsj.com/articles/craft-brewers-take-issue-with-ab-inbev-distribution-plan-1449227668> [<https://perma.cc/5QGJ-MBSH>].

225. Daniel Croxall, *Independent Craft Breweries Struggle Under Distribution Laws that Create a Power Imbalance in Favor of Wholesalers*, 12 WM. & MARY BUS. L. REV. 401, 416 (2021).

226. Competition Report, *supra* note 13, at 13.

227. See Greenman, *supra* note 113, at 188.

228. *Id.*

legislation would ease the asymmetrical cost burden of regulatory knowledge between large and small alcohol producers, decrease barriers to enter new markets for the small producers, and increase consumer welfare by alleviating the cost of state-by-state legal and regulatory guidance.

In *Granholm v. Heald*, the Court was presented with a challenge to the regulation of direct-to-consumer wine shipment in New York and Michigan.²²⁹ The state laws at issue allowed in-state wineries to sell directly to in-state consumers without allowing out-of-state wineries to do the same. The key question was how the Twenty-First Amendment interacted with the Dormant Commerce Clause requirement that states shall not discriminate against interstate commerce.²³⁰ The Court found that state alcohol regulation is still subject to other constitutional provisions.²³¹ Thus, the Twenty-First Amendment gives states the abilities to outright ban alcohol sales, but the grant of regulatory power is not unlimited and is subject to federal constraints.²³²

In *South Dakota v. Dole*, the Court faced the outer limits of the Spending Clause and how it relates to the Twenty-First Amendment.²³³ The issue hinged upon the Federal Minimum Drinking Age Act, which conditioned five percent of federal highway funds on state adoption of twenty-one as the minimum drinking age. Ten states brought a challenge to the withholding, arguing that the law was an invalid use of the Spending Clause and violated the Twenty-First Amendment.²³⁴ The Court ruled against the states on both points.²³⁵ Ultimately, the Court concluded the law did not induce states to act unconstitutionally and did not violate the Twenty-First Amendment. The Court crafted a four-part test to determine the validity of conditioned federal funds. To pass a constitutional challenge, 1) the Spending Clause must be used for the general welfare,²³⁶ 2) with clearly stated conditions.²³⁷ The withheld funds 3) must be in relation to the federal interest being promoted²³⁸ and 4) cannot require states to act

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

230. *Id.*

231. *Id.*

232. Greenman, *supra* note 113, at 188.

233. *South Dakota v. Dole*, 483 U.S. 203 (1987).

234. *Id.*

235. *Id.*

236. *Id.* at 207.

237. *Id.* at 208.

238. *Id.* at 207.

unconstitutionally.²³⁹ The Court decided the National Minimum Drinking Age Act advanced the general welfare because of its aim to prevent drunk driving by underage citizens of one state travelling to another where they are of age.²⁴⁰ It also reasoned that the use of highway funds was reasonably related to this goal.

In the grand scheme of these cases, the Court found that state alcohol regulation interests did not outweigh other constitutional provisions. However, crafting a federal regulatory scheme and using the Spending Clause to incentivize states to adopt it is a valid use of federal power. Small producers and consumers would be major beneficiaries of this change. Producers would only need to deal with a single regulatory system, instead of one for each state that they want to do business in. This would indirectly reduce prices for consumers by lowering the legal and information costs to expand to new states. The total information cost burden to enter each state market is consistent between large and small producers. As the small producers have less employees, revenue, and profits than large alcohol corporations, the cost of understanding multiple state systems is a barrier to entry that unfairly disadvantages small producers wanting to expand to new markets.

Principally, the Spending Clause must be used in conjunction with new or existing federal grants that relate to the interests being advanced by the legislation.²⁴¹ Fortunately, multiple options exist for federal funds that could reasonably relate to the welfare promoted by standardizing alcohol regulation. Alcohol producers, such as breweries, are one of the most efficient ways to revitalize post-industrial neighborhoods and rural cities.²⁴² Some federal infrastructure funds could be withheld from states that do not standardize their alcohol regulatory and distribution laws to a set federal guideline. Focusing on the community nature of spaces like breweries, Congress could use existing grants such as the Community Development

239. *Id.* at 210.

240. *Id.* at 214.

241. *Id.* at 207.

242. See, e.g., Neil Reid, *Craft Breweries, adaptive reuse, and neighborhood revitalization*, 57 URB. DEV. ISSUES 5 (2018); Geoff Boening, Jesus Barajas & Julie Wartell, *Neighborhood Change, One Pint as a Time*, in UNTAPPED: EXPLORING THE CULTURAL DIMENSIONS OF CRAFT BEER (2017); Geoff Boening, *Craft Beer, Urban Planning, and Gentrification* (June 30, 2017), [https://geoffboening.com/2017/06/craft-beer-planning-gentrification/#:~:text=There's%20a%20strong%20narrative%20\(and,urban%20centers%20and%20residential%20districts](https://geoffboening.com/2017/06/craft-beer-planning-gentrification/#:~:text=There's%20a%20strong%20narrative%20(and,urban%20centers%20and%20residential%20districts) [https://perma.cc/6PMZ-69CE].

Block Grant program or new federal funding focused on neighborhood revitalization to encourage state harmonization of alcohol laws.

A standardized system within each state is most beneficial for small businesses and would lower consumer prices. The advantages of a standardized regulatory system across the nation are not related to any specific policy within the regulation. Savings and advantages would stem from the lower barrier to entry for each state market.

D. Direct to Market Exception

The outsized influence that the largest producers, wholesalers, and retailers are able to wield against businesses within the other tiers diminishes the efficacy of the three-tier system. Consolidation within each tier has hurt small businesses in all tiers. The mandatory structure of the three-tier system has additionally inflated the market power the largest businesses wield.

Distributors play a key role in the system by moving product between suppliers and retailers. Their role efficiently organizing and pooling sales as well as product storage plays a crucial role in the industry. Yet, wholesalers can also serve as an anti-competitive force when the wholesale market in a region exhibits monopolist or oligopolistic traits.²⁴³ Refinements in the three-tier system can create competition within the distributor tier that would be a net positive for all players in the industry.

Allowing a direct to retailer route for alcohol producers up to a specific volume would add pressure to distributors to create value in their sales services. By limiting the exception according to production volume, distributors are protected from losing their largest clients and encouraged to serve small producers more efficiently. To prevent large price disparities between distributor and direct sales, these transactions should be given an additional state tax comparable to a standard distribution markup. This policy would properly incentivize distributors without harming the industry, increase state tax revenues, and give an independent sales route for small producers.

243. Competition Report, *supra* note 13, at 26.

CONCLUSION

Alcohol regulation in the United States today is deeply related to, and directly shaped by, the trends that have existed since the founding of the nation. The growth of the domestic industry after the Revolution led to a culture of overindulgence. This continued into the turn of the 20th century when the market underwent rapid consolidation and the largest companies wielded great influence. The reaction to the overconsumption and large market forces came through the temperance movement and Prohibition. The hasty passage of the Eighteenth Amendment and its rapid repeal in the Twenty-First Amendment laid the foundation for our regulatory structure for alcohol today. This structure prevented the vertical integration that was a significant feature of the pre-Prohibition market. Yet, the focus on vertical integration prevention allowed horizontal integration in each of the three tiers that negatively impacts consumers and small businesses in the market. The fractured regulatory system exacerbates the power imbalance between large and small businesses. Incentivizing states to adopt a standardized system through the Spending Clause would positively influence consumer experience and price, as well as reduce market barriers for small producers, wholesalers, and retailers. Allowing a limited producer-to-retailer sales route and taxing it at roughly the same price as a wholesaler markup would be beneficial to the industry as a whole. This would give new opportunities for small business growth, properly incentivize distributors to give beneficial services, and increase state tax revenue. Small businesses, local producers, wholesaler, and individuals have been the backbone of the industry since the founding era, and our laws can do better to protect and support these industry players.

