

REGIONAL LITIGATION SUMMARIES

Northeast Region

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Beer Supplier and Distributor Must Arbitrate Dispute Despite New York Law to the Contrary

In an issue of first impression in the Second Circuit, the Eastern District of New York recently held that a beer supplier and its distributor must arbitrate their dispute, pursuant to their agreement and federal law, despite the fact that a provision of the New York Alcoholic Beverages Control (“ABC”) Law prohibits such arbitrations.

In John G. Ryan Inc. v. Molson USA LLC, Case No. 05-CV-3984 (E.D.N.Y. Nov. 15, 2005), Molson USA LLC (“Molson”), a beer supplier, and John G. Ryan Inc. (“Ryan”), a beer distributor, entered into a distribution agreement that contained a mandatory arbitration clause. About a year later, Molson announced it was consolidating its distributors in the New York market into Coors distributors¹ and encouraged Ryan and other non-Coors distributors nationwide to sell their distribution rights to Coors distributors in their respective markets. When Ryan declined to do so, Molson commenced an arbitration proceeding pursuant to the agreement’s arbitration clause, seeking a determination that it had the legal right to terminate Ryan as a Molson distributor. Ryan responded by filing an action in New York state court seeking a dismissal or permanent stay of the arbitration proceeding, arguing that Section 55-c(7)(c) of the New York ABC Law (“Section 55-c”) prohibits the imposition of pre-dispute arbitration. Molson removed the case to federal court and moved to compel arbitration, arguing

¹ Molson and Coors were parties to a joint venture at this time and later merged.

that the Federal Arbitration Act (“FAA”) preempts Section 55-c pursuant to the Supremacy Clause of the United States Constitution.

Generally, under the Supremacy Clause, a federal law preempts any state law that conflicts with the federal law. The court noted that the parties did not dispute that New York’s prohibition of pre-dispute arbitration agreements between beer suppliers and distributors conflicts with “Congress’s intent to implement a national policy in favor of arbitration” as reflected in the FAA. Thus, the FAA should preempt Section 55-c. However, because Section 55-c governs the sale and distribution of alcoholic beverages in New York state, the Twenty-first Amendment to the Constitution -- which repealed Prohibition and granted states the power to regulate the sale and distribution of alcoholic beverages within their own borders -- comes into play.

To determine whether Section 55-c does indeed trump the FAA, the court analyzed whether the behavior regulated by that section falls within the “core” of powers reserved to the states by the Twenty-first Amendment. In North Dakota v. United States, 495 U.S. 423, 432 (1990), the Supreme Court held that that these core state concerns include: (1) promoting temperance; (2) ensuring orderly market conditions; and (3) raising revenue.

In earlier decisions that also affirm the states’ control over the importation, sale and distribution of alcohol within their borders, the Supreme Court acknowledged nonetheless that a state’s power to regulate alcohol is not absolute. The Court identified various state statutory schemes that did not sufficiently constitute core state interests to preclude federal preemption. For example, in California Retail Liquor Dealers Association v. Midcal Aluminum, Inc., 445 U.S. 97, 113-14 (1980), the court held a state’s wine-pricing regulations to be of insufficient state interest to prevent federal preemption by the Sherman Act. Similarly, a state’s

ban on advertising alcoholic beverages on cable television was preempted by federal communications regulations because the state advertising statute as applied “to the importation of distant signals by cable television operators” did not serve a core interest. Capital Cities Cable, Inc. v. Crisp, 467 U.S. 691, 715-16 (1984).

Guided by this trilogy of Supreme Court decisions, the Ryan court held that Section 55-c does not implicate a core New York state interest. Rather, it governs a purely “procedural matter affecting only the forum in which a dispute will be considered.” Having reached this determination, the court then proceeded to balance state and national interests “to harmonize state and federal powers” and “provide a thoughtful explanation as to why a state statute that has been enacted pursuant to a Constitutional Amendment will not prevail.” This analysis also tipped decisively in favor of federal preemption. Indeed, the court found “little, if any, evidence that would establish the state interest at stake,” and “no evidence . . . to support a finding that the statute actually serves the proffered interests” of maintaining the viability of a three-tier alcohol distribution system. “In contrast, the federal government has clearly articulated its interest in promoting a national policy in favor of arbitration.” Because “the State’s unsubstantiated interest . . . simply is not of the same stature as the goals of [the Federal Arbitration Act]” and “a ‘core’ power of the Twenty-first Amendment is not implicated,” the court held that the FAA preempts Section 55-c and granted Molson’s motion to compel arbitration.