SENATE BILL 688 TO AUTHORIZE SPORTS WAGERING IN NC WOULD VIOLATE THE ANTI-MONOPOLY CLAUSE OF THE NC CONSTITUTION

Jeanette Doran
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The Perpetuities and Monopolies Clause of the North Carolina Constitution restrains the General Assembly from legislating or conferring a legal monopoly, particularly where the legislation would have no factual, logical, or reasonable basis other than to eliminate future competition for the benefit of a favored few. Unfortunately, as currently written, SB 688 ("An Act to Authorize and Regulate Sports Wagering in North Carolina.") would violate this provision in the State Constitution and should not be enacted as written. The bill currently limits the number of interactive sports wagering licenses, a prerequisite to offering or accepting sports wagers under the bill, to not more than 12. That maximum is the principal portion of the bill at issue in this memorandum, but other portions of the bill raise concerns, including vagueness, which are beyond the scope of this memorandum.

A. The historical context of the Perpetuities and Monopolies Clause shows that it was designed precisely to prevent legislative acts that create or tend to create monopolies.

1. Text and definitions.

The North Carolina Constitution explicitly prohibits monopolies, declaring: "Perpetuities and monopolies are contrary to the genius of a free state and shall not be allowed." N.C. Const. art. I, Sec. 34. The North Carolina Supreme Court has set out a four-part definition of a monopoly:

> "(1) [C]ontrol of so large a portion of the market of a certain commodity that (2) competition is stifled, (3) freedom of commerce is restricted and (4) the monopolist controls prices."

American Motors Sales Corp. v. Peters, 311 N.C. 311, 316 (1984).

Two other relevant definitions are (1) "[c]ontrol or advantage obtained by one supplier or producer over the commercial market within a given region," and (2) "[t]he market condition existing when only one economic entity produces a particular

product or provides a particular service." Black's Law Dictionary 1098 (9th ed. 2009).

2. Similar monopoly language has been preserved in each successive state Constitution.

The language of the Perpetuities and Monopolies Clause is brief, but powerful. The text gives not only a strong prohibition against monopolies, but also provides a glimpse of the reason behind the imperative: monopolies "are contrary to the genius of a free state." N.C. Const. art. I, sec. 34.

Dating back to the State's first constitution in 1776, the North Carolina Constitution has always contained such a prohibition on monopolies. This first iteration of the ban found in the Declaration of Rights, which was incorporated into the 1776 Constitution, declared:

> "That perpetuities and monopolies are contrary to the genius of a free state and *ought not* to be allowed."

N.C. Const. 1776, Declaration of Rights, Art. XXIII (emphasis added).

The 1776 monopoly provision was later transferred nearly verbatim to the 1868 Constitution. N.C. Const. 1868, Art. I, section 31 ("Perpetuities and monopolies are contrary to the genius of a free State and ought not to be allowed."). When the Constitution underwent substantial revision and reorganization culminating in what is known as the 1971 Constitution, the provision was rendered as it is today: "Perpetuities and monopolies are contrary to the genius of a free state and shall not be allowed." N.C. Const. art. I, sec. 34. The language changed slightly from "ought not" to "shall not" as part of a general editorial revision made by the 1968 Study Committee that drafted the 1971 Constitution. Report of the North Carolina State Constitution Study Commission to the North Carolina State Board and the North Carolina Bar Association, Raleigh 1-5 (1968). The Study Committee explained, "In order to make it clear that the rights secured to the people by the Declaration of Rights are *commands and not merely admonitions* to proper conduct on the part of government, the words 'should' and 'ought' have been changed to read 'shall' throughout the Declaration." *Id.* (emphasis added). Thus, the prohibition on monopolies is not merely precatory but rather a strict, mandatory proscription.

3. Historical context for the 1776 Monopoly provision.

The minutes of the 5th Provincial Congress of North Carolina, which approved the 1776 Constitution, do not record any direct discussion about the Perpetuities and Monopolies Clause. A search of the minutes for the term "monopoly" or any of its variants yields only one result, one of little relevance, arising during discussion about the procurement of salt. Minutes of the Provincial Congress of North Carolina, Dec. 3, 1776, p. 951 (viewable at

http://docsouth.unc.edu/csr/index.html/document/csr10-0442.)[1]

The lack of recorded discussion does not end the inquiry, however. There is ample evidence that the drafters took a dim view of monopolies. The Perpetuities and Monopolies Clause must be viewed against the backdrop of the drafters' historical and political experience. According to noted state constitutional expert John Orth, "Monopolies still had political overtones at the time of the American Revolution." John V. Orth, Allowing Perpetuities In North Carolina, 31 Campbell L. Rev. 399, 401, n. 9 (2009). "English monarchs," Orth continues, "had used grants of monopolies to reward their political favorites, provoking parliament to adopt the Statute of Monopolies, 21 Jac. I, c. 3 (1624), which made all monopolies illegal except those authorized by parliament or those granted to protect inventions." *Id*. According to Orth, perpetuities and monopolies were considered by the 1776 drafters to be more than a threat to the free market; they were "a political threat" to the very values of the republic. *Id*. at 410. Perpetuities and monopolies were, in the plain words of the founders, "contrary to the genius of a free state." N.C. Const. 1776, Declaration of Rights, Art. XXIII.[2] Political favoritism remains a concern in the modern era. The Court of Appeals most recently considered this provision of the state constitution in *Rockford-Cohen Grp, LLC v. N.C. Dep't of Ins*. 230 N.C. App. 317 (2013) in which the Court struck down a statute restricting bailbondsman training to a single provider. The Court of Appeals described the statute as "foreclosing the possibility that others could provide this training." *Id*. at 323. Similarly, SB 688 would foreclose the possibility that others could provide sports wagering.

B. Case law confirms that legislative acts making a select group of companies or associations the sole legal provider of a good or service is the epitome of the evil that the Perpetuities and Monopolies Clause was designed to prevent.

Fundamentally, State-created monopolies "conflict with that fundamental democratic principle: 'Equal rights and opportunities to all, special privileges to none.'" *State v. Felton*, 239 N.C. 575, 587 (1954). For this reason, and as explained below, the General Assembly may not legislatively and artificially create a monopoly to benefit the few, by outlawing all other otherwise lawful competition. Yet, that is

[1] In this instance the delegates to the convention set up a committee "to inquire into the conduct of Mr. John Cooper, of Beaufort County, with respect to the monopoly of common Salt, and make report to the House." Numerous references to salt and shortages of salt can be found throughout the minutes of the convention.

[2] John Orth has noted that "genius" is "relevantly defined as a 'peculiar, distinctive, or identifying character' and 'an attendant spirit of a person or place.'" John V. Orth, Allowing Perpetuities In North Carolina, 31 Campbell L. Rev. 399, 401, n. 9 (2009).

precisely what SB 688 would do by authorizing sports wagering but capping the number of interactive sports wagering operators at merely 12.

1. Monopolies cannot be justified as an exercise of legitimate police power.

It is well established that "the police power of the State may be exercised to enact laws, *within constitutional limits*, to protect or promote the health, morals, order, safety, and general welfare of society." *Standley v. Town of Woodfin*, 362 N.C. 328, 333 (2008) (internal quotations omitted)(emphasis added). However, the North Carolina Supreme Court has also noted,

> [I]f a statute discloses no such purpose, has no real or substantial relation to these objects, or is a palpable invasion of rights secured by fundamental law*, it is the duty of the courts so to adjudge and thereby give effect to the Constitution.*

Palmer v. Smith, 229 N.C. 612, 616 (1948) (internal quotation omitted) (emphasis added).[3] This truism has been made explicitly applicable to monopolies: "the exercise of the police power will not be upheld where its use tends to create a monopoly or special privilege and does not tend to preserve the public health, safety or welfare." *Id* at 615. Further, a mere pretext of protecting the public health, safety, or welfare is insufficient to sustain a law that restricts liberty. *Roller v. Allen*, 245 N.C. 516, 525 (1957).

Any claim that the licensee cap of 12 is intended to protect the public from excessive numbers of sports wagering operators would be specious. The application fee is $500,000. That extraordinary fee would itself limit the number of applicants in practical terms, without the need for a statutory cap.

Further, if the justification for sports wagering legalization is revenue, the cap of 12 licensees means the state would receive only $6m in licenses fees from sports wagering operators (fees from unsuccessful applicants are to be refunded "minus any expenses the Commission incurs in reviewing the application."). It seems contrary to common sense to suspect that tax revenues from the wagering itself would be higher with *fewer* operators so tax-revenue would likewise provide an insufficient justification for the 12 license cap.

2. Unconstitutional monopolies are characterized by several features, including restrictions of the common right to engage in a lawful business or occupation, favoritism toward a particular class and exclusion of others, special privileges granted to private

[3] A different calculus might apply in the context of a public utility, given the need for such services. *See State v. Felton*, 239 N.C. 575, 585 (1954).

persons or corporations, and restraint on competition.

In *State v. Ballance*, the Court struck down a law requiring licensing for anyone engaging in professional photography because, among other things, the law violated the Perpetuities and Monopolies Clause. 229 N.C. 764, 772 (1949). The Court reasoned that the licensing requirement "unreasonably obstructs the common right of all men to choose and follow one of the ordinary lawful and harmless occupations of life as a means of livelihood[.]" *Id.* The *Ballance* Court determined that the licensing statute "bears no rational, real, or substantial relation to the public health, morals, order, or safety, or the general welfare." *Id.* Rather, the statue "is addressed to the interests of a particular class rather than the good of society as a whole and *tends to promote monopoly* in what is essentially a private business." *Id.* (emphasis added). "In so doing," the Court concluded, "it offends the additional constitutional guaranty that "Monopolies are contrary to the genius of a free state and ought not to be allowed." *Id.* (citing N.C. Const. 1776, Declaration of Rights, Art. XXIII; N.C. Const. 1868, Art. I, section 31).

In the case of *In re Certificate of Need for Aston Park Hosp., Inc.*, the Supreme Court struck down a statute conferring upon the state's Medical Care Commission the power to forbid construction of new medical facilities, through issuance or denial of certificates of need, ostensibly for the purpose of maintaining an efficient distribution of medical professionals. 282 N.C. 542 (1973). The Court's decision striking the law rested on two conclusions: (1) that the statute was a deprivation of due process of law in violation of N.C. Const. art. I, sec. 19, and (2) the statute created a monopoly in the existing hospitals and granted exclusive privileges in violation of N.C. Const. art. I, sec. 32 and 34. *Id.* at 551.[4] Moreover, the Court found no "reasonable relation" between the statute and the "promotion of the public health." *Id.*

In two notable cases, distinguishable from SB 688, challenges based on the Perpetuities and Monopolies Clause were unsuccessful, but the reasoning employed by the Court in both is instructive.

In *Madison Cablevision, Inc. v. Morganton*, the town of Morganton declined to renew a franchise agreement with the plaintiff cable company, deciding instead to provide cable service to the community itself. 325 N.C. 634 (1989). The Supreme Court addressed the plaintiff's claims that such action conferred a monopoly and exclusive emolument in violation of Sections 32. The Court disagreed, partly because the town "ha[d] not declared or established itself as the 'exclusive' supplier

[4] The courts often analyze together the monopolies and the exclusive emoluments provisions of the State Constitution. *See, e.g., State ex rel Taylor v. Carolina Racing Asso.*, 241 N.C. 80, 93-94 (1954); *State v. Felton*, 239 N.C. 575, 587 (1954).

of cable television service to its citizens." *Id.* at 654. Rather it "simply failed to renew Madison Cable's expired franchise or to grant a franchise to two other applicants for failure of their proposals to meet community needs." *Id.* Neither the plaintiff nor any other companies were foreclosed from future franchising opportunities by the town's action, and the town promised to revisit its decision in five years. *Id.* Factually, that is in stark contrast to SB 688 which would permit a state agency to select 10-12 interactive sports wagering operators as the *exclusive* providers of sports wagering and would *foreclose* licensure to all but 10 to 12 interactive sports wagering operators.

In *American Motors Sales Corp. v. Peters*, the Court upheld the state's franchise statute despite the plaintiff's claims that it granted monopolies to established car dealerships in a given local market. 311 N.C. 311 (1984). Plaintiff's automobile dealership franchise was revoked because another dealership of the same automobile make and models was already operating in the area. *Id.* The statute was designed to protect dealerships from abuse arising from "vertical integration" where manufacturers would grant multiple franchises in a given market. *Id.* at 319-20. The *Peters* Court characterized the scheme as a restriction on intra-brand competition and concluded that it did not amount to the creation of a monopoly. *Id.* at 313-14. "Of central importance to the validity of this legislation" the Court wrote, "is the recognition that if it restrains trade, it does so vertically rather than horizontally. *Id.* at 318. The Court explained:

> A vertical restraint runs from the manufacturer down through the distributer, ending ultimately with the retailer. Horizontal restraints, on the other hand, run between dealers and dealers or retailers and retailers, all operating on the same level. *Id.*

Had the challenged arrangement been a horizontal rather than vertical restraint on trade, it would have "run contrary to the public interest because they stifle competition[.]" *Id.* (citing *Bulova Watch Co., Inc. v. Brand Distributors of North Wilkesboro, Inc.*, 285 N.C. 467, 480 (1974)). The Court concluded that the restraints on competition and the increased prices resulting from horizontal restraints were "the evil which the anti-monopoly provision seeks to prevent." *Id.* (internal citations omitted); *see also* Charles Noel Anderson, Jr., Survey of Developments In North Carolina Law, 1984: III. Commercial Law: *American Motors Sales Corp. v. Peters*: Green Light to Territorial Security for Automobile Dealers, 63 N.C.L. Rev. 1080, 1082-83 (1985). Although the *Peters* Court upheld the franchise statute as a permissible vertical restraint on trade, SB 688 would create a statutory scheme more analogous to the type of horizontal restraint that *Peters* condemns as monopolistic. SB 688 would prohibit non-licensed interactive sports wagering operators from providing

the same sports wagering services as licensed operators, yet the bill would authorize the Commission to select only 10 to 12 operators as the exclusive permissible suppliers of those services, and thereby outlaw all other competition.

3. By permitting no more than 12 interactive sports wagering operators the exclusive right to sports wagering, SB 688 would fall squarely within the meaning and prohibition of the Perpetuities and Monopolies Clause.

As explained above, legislation such as SB 688 must have a "real or substantial relation" to the "prevent[ion of] some offense or evil or to preserve public health, morals, safety and welfare," if it is to survive. *Palmer v. Smith,* 229 N.C. at 616. Mere pretense or "the guise of protecting the public" simply will not suffice. *Roller v. Allen*, 245 N.C. 516, 525 (1957). In the present case, there has been no evidence of a "real or substantial relation" to any legitimate governmental interest. The purported justification for SB 688 is tax revenue. Indeed, in the event more than 12 applicants apply for an interactive sports wagering operator license, the Commission may consider the "amount of adjusted gross revenue and associated tax revenue that an applicant projected to generate." There can be no factual, logical, or reasonable basis to conclude that *limiting* the number of operators would promote greater tax revenue. Rather, far from addressing a legitimate interest of the State, SB 688 addresses the interests of a handful of wagering operators by limiting the number of interactive sports wagering operators.

Unlike the decision not to renew a franchise contract in *Madison Cablevision, Inc. v. Morganton*, SB 688 would make a select few the exclusive providers of a service, and it forecloses any possibility that other companies will be allowed to enter sports wagering market. SB 688 would not only restrict healthy and beneficial horizontal competition, as described in *American Motors Sales Corp. v. Peters,* 311 N.C. 311 (1984), but it effectively eliminates it by imposing a shockingly low cap on the number of available licenses. This type of restriction or elimination of competition is "the evil which the anti-monopoly provision seeks to prevent." *Id*

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About the Author

Jeanette Doran has served as President and General Counsel of the North Carolina Institute for Constitutional Law since returning to the Institute to reorganize and restart the organization in July 2019.

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PO Box 30601
Raleigh, NC 27622
984.884.7451
www.ncicl.org