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E-Commerce in Wine

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E-COMMERCE IN WINE

*James Alexander Tanford**

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I. INTRODUCTION

The first major battle of the wine war is now history. The rebels unexpectedly routed the States' forces and their powerful wholesaler allies and won a convincing victory in *Granholt v. Heald*.¹ Trade barriers blocking e-commerce in wine that once seemed invincible have been torn down, or at least damaged.

The assault on wine trade barriers began in 1998 in Indiana, of all places. Two lawyers from the Hoosier state and a handful of wine consumers declared war on laws that prohibited ordering wine over the Internet and denied them access to hundreds of small producers. Somewhat unexpectedly, the plaintiffs won the initial battle.² News of the victory spread through the wine world, and new recruits began arriving. Cases were filed in Florida, Michigan, North Carolina, Texas, Virginia and New York. The wine industry, which had at first been reluctant to get involved, joined the fray.

The intoxicating feeling of victory was quickly replaced by the hangover of three defeats in a row. The plaintiffs lost in Florida³ and Michigan,⁴ and suffered a devastating defeat as the Seventh Circuit reversed and va-

* Professor of Law, Indiana University-Bloomington, and Counsel of Record for the plaintiffs in *Granholt v. Heald*. My co-counsel in *Granholt* was Robert D. Epstein, who helped develop every one of these issues over nearly eight years of litigation. I also owe debts of gratitude to Clint Bolick, Ken Starr, Jim Seff, Kathleen Sullivan, and Tracy Genesen, all of whom participated with us in crafting the Supreme Court argument, and to the army of legal scholars and lawyers who wrote a total of 26 briefs in the case—including Paul Bender, Susan Estrich, Stuart Banner, Steven Diamond, Drew Days, Miquel Estrada, Carter Phillips, Viet Dinh, and the firms of Dickstein Shapiro, Gibson Dunn & Crutcher, Morrison & Foerster, Jenner & Block, Sidley & Austin, Patton Boggs, Pillsbury Winthrop, King & Spalding, and Kirkland & Ellis. As counsel of record, I read every one of those briefs. It is inevitable that some of the ideas, citations, and phrases used in this Article should properly be attributed to them but are not because I have misplaced the mental citation. Finally, special thanks to Dean Lauren Robel who supported my work on the *Granholt* case and defended me when I was attacked personally by the wine wholesalers.

¹ *Granholt v. Heald*, 544 U.S. 460 (2005).

² *Bridenbaugh v. O'Bannon*, 78 F. Supp. 2d 828 (N.D. Ind. 1999).

³ *Bainbridge v. Bush*, 148 F. Supp. 2d 1306 (M.D. Fla. 2001).

⁴ *Heald v. Engler*, 2001 U.S. Dist. LEXIS 24826 (E.D. Mich. 2001).

cated the plaintiffs' initial victory in Indiana.⁵ The trade barriers held. Momentum shifted to the states. Wine industry support faltered, and rebel supplies ran low—one more defeat, and the revolution would be over.

That one additional defeat never happened. The rebels won the next eight decisions—in the district courts of Virginia,⁶ North Carolina,⁷ Texas,⁸ and New York,⁹ and in the courts of appeals for the Fourth,¹⁰ Fifth,¹¹ Sixth,¹² and Eleventh¹³ Circuits. State officials in Texas and North Carolina surrendered, but others fought on. Then, the Second Circuit surprisingly upheld New York's law to set up a split in the Circuits,¹⁴ and the battleground shifted to the Supreme Court. Fighting in the Supreme Court is unlike any other kind of litigation. It is covered on the front pages of the *New York Times* and *Wall Street Journal*. It is fought behind the scenes at the highest levels of government. Alliances must be formed because you need all the friends you can get to support you with amicus briefs.¹⁵ It is politics writ large. Luckily for the rebels, former Solicitor-General Kenneth Starr arrived in the nick of time, bringing with him his small band of Washington troops who were experienced in this kind of in-fighting.¹⁶ The Federal Trade Commission (FTC) also supplied much-needed ammunition in the form of a strong, and judicially noticeable, report on the anti-competitive effects of state barriers to e-commerce in wine and the availability of non-discriminatory regulatory alternatives.¹⁷ The forces converged on the Supreme Court, filing 26 briefs. Then, on May 16, 2005, the Court released its decision. The rebels had won a decisive and unequivocal victory for consumers and the free market. In a broad and sweeping decision, the Su-

⁵ *Bridenbaugh v. Freeman-Wilson*, 227 F.3d 848 (7th Cir. 2000). Ironically, this anti-free market opinion was written by J. Frank Easterbrook, who was one of the founding scholars of the law and economics movement.

⁶ *Bolick v. Roberts*, 199 F. Supp. 2d 401 (E.D. Va. 2002).

⁷ *Beskind v. Easley*, 197 F. Supp. 2d 464 (W.D.N.C. 2002).

⁸ *Dickerson v. Bailey*, 212 F. Supp. 2d 673 (S.D. Tex. 2002).

⁹ *Swedenburg v. Kelly*, 232 F. Supp. 2d 135 (S.D.N.Y. 2002).

¹⁰ *Beskind v. Easley*, 325 F.3d 506 (4th Cir. 2003).

¹¹ *Dickerson v. Bailey*, 336 F.3d 388 (5th Cir. 2003).

¹² *Heald v. Engler*, 342 F.3d 517 (6th Cir. 2003).

¹³ *Bainbridge v. Turner*, 311 F.3d 1104 (11th Cir. 2002).

¹⁴ *Swedenburg v. Kelly*, 358 F.3d 223 (2d Cir. 2004) (the court acknowledged that it was taking the disfavored position and setting up a split in the Circuits).

¹⁵ Perhaps the oddest allies in this case were the liquor dealers, evangelists, and high school principals who supported the states.

¹⁶ Kenneth Starr is now the Dean of the Pepperdine Law School. In 2004, he was in the Washington office of Kirkland & Ellis. His associates were Kannon Shanmugam (now a deputy Solicitor-General), Susan Kearns Engel, Steven Engel, and Jennifer Atkins.

¹⁷ Staff of the Federal Trade Commission, *Possible Anticompetitive Barriers to E-commerce: Wine* (July 2003), available at www.ftc.gov/os/2003/07/winereport2.pdf (last visited Aug. 21, 2007) [hereinafter *FTC Report*]. It is based on "testimony from all sides of the wine issue, including wineries, wholesalers, state regulators, and a Nobel laureate in economics." *Id.* at 2.

preme Court held that trade barriers banning direct shipment of wine ordered through e-commerce are unconstitutional.

Now what? The Supreme Court had knocked down trade barriers in Michigan and New York. Ohio,¹⁸ Pennsylvania,¹⁹ Massachusetts,²⁰ and Florida²¹ surrendered. But, in New Jersey,²² Indiana,²³ Kentucky,²⁴ Maryland,²⁵ Arkansas,²⁶ Arizona,²⁷ Maine,²⁸ and Delaware,²⁹ the fighting continued as lawmakers and their wholesaler allies scurried to shore up their defenses, adopted new strategies, and vowed to fight to the death against opening the wine market to e-commerce. After all, what state would want the terrible consequences of an open market—free trade, competition, increased product availability, lower prices, and a diminution in the power currently held by the cartel of oligopolist wholesalers?

This article will look at the history of wine regulation in the United States, and what difference *Granholm v. Heald* makes. Based on the continued resistance to open markets in a dozen states, it assumes that *Granholm* was not the end of the fight. Consequently, the article looks ahead and wonders where the next battles are likely to take place. It will conclude with thoughts about the continued stability of the underlying structure that led to the wine wars—the three-tier distribution system that gives so much power to the wholesalers.

II. BACKGROUND

A. *The Commerce Clause*

The Commerce Clause provides that “Congress shall have Power . . . to regulate Commerce . . . among the several States”³⁰ Although the Constitution says nothing about whether states have power to regulate interstate commerce simultaneously, the Supreme Court has always held that this provision grants exclusive power to Congress. The states may not in-

¹⁸ *Stahl v. Taft*, No. 2:03CV597, 2006 U.S. Dist. LEXIS 17014 (S.D. Ohio 2006).

¹⁹ *Cutner v. Newman*, 398 F. Supp. 2d 389 (E.D. Pa. 2005).

²⁰ *Stonington Vineyards v. Jenkins*, No. 1:05CV10982 (D. Mass. 2005).

²¹ *Bainbridge v. Bush*, 148 F. Supp. 2d 1306 (M.D. Fla. 2001).

²² *Freeman v. McGreevey*, No. 2:03CV03140 (D.N.J. filed 2003).

²³ *Baude v. Heath*, No. 1:05CV0735, 2005 U.S. Dist. LEXIS 43947 (S.D. Ind. 2005).

²⁴ *Huber Winery v. Wilcher*, No. 3:05CV289, 2006 U.S. Dist. LEXIS 43947 (W.D. Ky. 2006).

²⁵ *Bushnell v. Ehrlich*, No. 1:05CV03128 (D. Md., case dropped in 2006).

²⁶ *Beau v. Moore*, No. 4:05CV903 (E.D. Ark. 2005, stayed Sept. 28, 2006).

²⁷ *Black Star Farms, LLC v. Morrison*, No. 2:05CV02620 (D. Ariz. filed 2005).

²⁸ *Cherry Hill Vineyard v. Baldacci*, No. 1:05CV153, 2006 U.S. Dist. LEXIS 51657 (D. Me. 2006).

²⁹ *Hurley v. Minner*, No. 1:05CV00826, 2006 U.S. Dist. LEXIS 69090 (D. Del. 2006).

³⁰ U.S. CONST. art. I, § 8.

terfere with it.³¹ This is known as the “dormant” Commerce Clause principle, first articulated in *Gibbons v. Ogden*.³² Simply put, states cannot discriminate against interstate commerce, provide economic protection to in-state businesses, erect tariffs or trade barriers to the products of other states, or otherwise impose significant burdens upon interstate commerce.

The reason is historically obvious. The Framers denied states the power to erect local trade barriers in “the conviction that in order to succeed, the new Union would have to avoid the tendencies toward economic Balkanization that had plagued relations among the Colonies and later among the States under the Articles of Confederation.”³³ The new country must be made a single economic unit. This was the “one object riding over every other in the adoption of the Constitution.”³⁴ In an oft-quoted passage, the Court summarized this historical guiding principle as follows:

Our system, fostered by the Commerce Clause, is that every farmer and every craftsman shall be encouraged to produce by the certainty that he will have free access to every market in the Nation, that no home embargoes will withhold his exports, and no foreign state will by customs duties or regulations exclude them. Likewise, every consumer may look to the free competition from every producing area in the Nation to protect him from exploitation by any. Such was the vision of the Founders; such has been the doctrine of this Court which has given it reality.³⁵

The Founders believed that, to succeed as a new nation, the “peoples of the several states must sink or swim” together as a single national economic unit.³⁶ This guiding philosophy has evolved into several specific jurisprudential principles relevant to state efforts to restrict buying wine over the Internet.

1. States may not discriminate against interstate commerce

The most obvious principle derived from the dormant Commerce Clause is that a state may not discriminate against the products of other states through regulations that give economic advantages to local products and producers. Such a system is the very essence of the tariff and trade barrier problem the Founders were trying to eliminate. Therefore, the Su-

³¹ See *Associated Indus. of Mo. v. Lohman*, 511 U.S. 641, 646-47 (1994); *S.C. Highway Dep’t v. Barnwell Bros., Inc.*, 303 U.S. 177, 185 (1938) (Commerce Clause “by its own force” prohibits certain state actions that interfere with interstate commerce).

³² *Gibbons v. Ogden*, 22 U.S. 1, 231-32, 239 (1824).

³³ *Hughes v. Oklahoma*, 441 U.S. 322, 325-26 (1979).

³⁴ *Gibbons*, 22 U.S. at 231 (essential “to keep the commercial intercourse among the States free from all invidious and partial restraints”). See also *West Lynn Creamery v. Healy*, 512 U.S. 186, 193 n.9 (1994) (citing James Madison).

³⁵ *H.P. Hood & Sons, Inc. v. Du Mond*, 336 U.S. 525, 539 (1949).

³⁶ *Baldwin v. G.A.F. Seelig*, 294 U.S. 511, 523 (1935).

preme Court has repeatedly held that a state law that discriminates against interstate commerce “is virtually *per se* invalid,”³⁷ and “at a minimum . . . invokes the strictest scrutiny.”³⁸ There are few constitutional issues on which the Court has been more consistent and united.³⁹

In the context of commerce, discrimination simply means “differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter,”⁴⁰ or otherwise places an out-of-state product or producer at a “substantial commercial disadvantage” compared to in-state products and producers.⁴¹ Discrimination does not have to be intended, and the offending statute need not have been enacted in a deliberate attempt to give in-state interests a competitive advantage. Because the intent of the legislature is not relevant, “a court need not inquire into the purpose or motivation behind a law to determine that, in actuality, it impermissibly discriminates against interstate commerce.”⁴² Instead, discrimination is a question of the practical impact of a regulation on out-of-state businesses compared to in-state ones.⁴³ The Court focuses “on whether a challenged scheme is discriminatory in effect, . . . measured in dollars and cents, not legal abstractions.”⁴⁴

A regulation is discriminatory if it satisfies any of the following criteria:

³⁷ See *Or. Waste Sys. v. Dep’t of Env’tl. Quality*, 511 U.S. 93, 100 (1994); *C & A Carbone, Inc. v. Town of Clarkstown*, 511 U.S. 383, 402 (1994) (O’Connor, J., concurring).

³⁸ *New Energy Co. v. Limbach*, 486 U.S. 269, 278-79 (1988).

³⁹ See *S. Cent. Bell Tel. Co. v. Alabama*, 526 U.S. 160 (1999) (discriminatory tax struck down); *Fulton Corp. v. Faulkner*, 516 U.S. 325 (1996) (discriminatory tax struck down); *West Lynn Creamery, Inc.*, 512 U.S. 186 (discriminatory milk pricing law struck down); *Or. Waste Sys., Inc.*, 511 U.S. 93 (discriminatory solid waste rule struck down); *Kraft Gen. Foods, Inc. v. Ia. Dep’t of Revenue & Fin.*, 505 U.S. 71 (1992) (discriminatory dividend rule struck down); *Fort Gratiot Sanitary Landfill, Inc. v. Mich. Dep’t of Natural Res.*, 504 U.S. 353 (1992) (discriminatory landfill law struck down); *Chem. Waste Mgmt., Inc. v. Hunt*, 504 U.S. 334 (1992) (discriminatory hazardous waste law struck down); *New Energy Co. v. Limbach*, 486 U.S. 269, 278 (1988) (discriminatory tax exemption struck down); *Armco, Inc. v. Hardesty*, 467 U.S. 638 (1984) (discriminatory tax struck down); *Hughes v. Oklahoma*, 441 U.S. 322 (1979) (discriminatory wildlife law struck down); *City of Philadelphia v. New Jersey*, 437 U.S. 617 (1978) (discriminatory trash shipment rule struck down).

⁴⁰ *Or. Waste Sys.*, 511 U.S. at 99.

⁴¹ *New Energy Co.*, 486 U.S. at 275.

⁴² *Associated Indus. of Mo. v. Lohman*, 511 U.S. 641, 653 (1994).

⁴³ *Chem. Waste Mgmt., Inc.*, 504 U.S. at 344 n.6; *Hughes*, 441 U.S. at 332; *C & A Carbone, Inc.*, 511 U.S. at 402 (O’Connor, J., concurring).

⁴⁴ *Associated Indus. of Mo.*, 511 U.S. at 654.

- a. Products from other states are banned or totally excluded from the local market.⁴⁵
- b. The effect of the regulation is to impose higher costs on out-of-state products than local ones. The Supreme Court has called state laws that raise the price of out-of-state goods in relation to in-state goods “paradigmatic examples” of discrimination against interstate commerce.⁴⁶
- c. The regulation requires out-of-state products to be processed locally before being sold, distributed or allowed to have market access.⁴⁷
- d. The regulation serves no practical purpose other than “mere economic protectionism” of local interests.⁴⁸
- e. The law embargoes local products and prevents them from leaving the state.⁴⁹

Discrimination is not justified simply because the regulation also serves legitimate local concerns. The Court has repeatedly struck down laws that, in the process of advancing state interests, discriminated against nonresidents.⁵⁰ The Court has held that a State can validate a discriminatory law only by showing that the law advances a legitimate local purpose that cannot be adequately served by reasonable nondiscriminatory alternatives.

[When] discrimination against commerce . . . is demonstrated, the burden falls on the State to justify it both in terms of the local benefits flowing from the statute and the unavailability of nondiscriminatory alternatives adequate to preserve the local interests at stake. . . . [F]acial discrimination by itself may be a fatal defect, regardless of the State’s purpose, because “the evil of protectionism can reside in legislative means as well as legislative ends.” At a mini-

⁴⁵ *City of Philadelphia v. New Jersey*, 437 U.S. 617 (1978).

⁴⁶ *West Lynn Creamery, Inc. v. Healy*, 512 U.S. 186, 193 (1994). *Accord* *Or. Waste Sys., Inc., v. Dep’t of Env’tl. Quality*, 511 U.S. 93 (1994).

⁴⁷ *C & A Carbone, Inc.*, 511 U.S. at 383.

⁴⁸ *Bacchus Imps. v. Dias*, 468 U.S. 263, 276 (1984).

⁴⁹ *Hughes v. Oklahoma*, 441 U.S. 322, 337 (1979).

⁵⁰ *H.P. Hood & Sons, Inc. v. Du Mond*, 336 U.S. 525 (1949) (New York cannot exclude Vermont dairy products even in the name of protecting public health); *Hughes*, 441 U.S. at 337 (Oklahoma cannot embargo its minnows even in the name of protecting a scarce resource); *Hunt v. Wash. State Apple Adver. Comm’n*, 432 U.S. 333, 351 (1977) (North Carolina cannot restrict advertising for Washington apples even to prevent consumer confusion); *City of Philadelphia*, 437 U.S. 617 (1978) (New Jersey cannot exclude Pennsylvania garbage to conserve diminishing landfill space); *Chem. Waste Mgmt., Inc. v. Hunt*, 504 U.S. 334 (1992) (Alabama cannot exclude hazardous wastes from other states in the name of public safety).

mum such facial discrimination invokes the strictest scrutiny of any purported legitimate local purpose and of the absence of nondiscriminatory alternatives.⁵¹

The burden is upon the state to show not just that regulation is justified, but that “the *discrimination* is demonstrably justified.”⁵² Understandably, the “standards for such justification are high.”⁵³ The state must make “the clearest showing” that there is no nondiscriminatory alternative,⁵⁴ and its justification must “pass the ‘strictest scrutiny.’”⁵⁵

The Supreme Court has only rarely found that a state has met its burden of proving the need to discriminate against interstate commerce, and then only upon an extensive factual record clearly demonstrating the absence of workable alternatives. In *Maine v. Taylor*,⁵⁶ the Court upheld a ban on out-of-state baitfish based on expert testimony that imported baitfish could introduce non-native parasites that could harm Maine fish and that there was no known way to prevent it other than a total ban. In *Sporhase v. Nebraska ex rel. Douglas*,⁵⁷ the Court upheld an embargo against exporting ground water to other states based on evidence that there was only enough water for the state’s own citizens because of a drought.

2. States may not engage in economic protectionism

The second principle derived from the dormant Commerce Clause is closely related to the first—States may not engage in economic protectionism.⁵⁸ They may not protect local industry by erecting barriers to interstate competition,⁵⁹ nor may they pass laws designed to make sure their own citizens are not at a disadvantage compared to consumers in other states.⁶⁰ Although the Court occasionally uses economic protectionism and discrimination interchangeably, the two concepts are slightly different. For example, a law requiring automobile manufacturers to offer the same rebates in Indiana as they offer in Illinois, Ohio, and Kentucky does not discriminate against interstate commerce, but it does protect the interests of local car dealers who might otherwise lose customers to big-volume dealers just across the border in Chicago, Louisville, and Cincinnati. Also, a law that disadvantages an out-of-state business for the benefit of an in-state

⁵¹ *Hughes*, 441 U.S. at 336-37 (citations omitted).

⁵² *Chem. Waste Mgmt., Inc.*, 504 U.S. at 344 (emphasis in original).

⁵³ *New Energy Co. v. Limbach*, 486 U.S. 269, 278 (1988).

⁵⁴ *C & A Carbone, Inc. v. Town of Clarkstown*, 511 U.S. 383, 393 (1994).

⁵⁵ *Or. Waste Sys. v. Dep’t of Env’tl. Quality*, 511 U.S. 93, 101 (1994).

⁵⁶ *Maine v. Taylor*, 477 U.S. 131, 140-43 (1986).

⁵⁷ *Sporhase v. Nebraska ex rel. Douglas*, 458 U.S. 941, 956-57 (1982).

⁵⁸ *City of Philadelphia v. New Jersey*, 437 U.S. 617, 623-24 (1978).

⁵⁹ *Bacchus Imps. v. Dias*, 468 U.S. 263, 276 (1984).

⁶⁰ *Brown-Forman Distillers Corp. v. N.Y. State Liquor Auth.*, 476 U.S. 573, 580 (1986).

business of a different type (e.g., out-of-state wineries vs. in-state wholesalers) is not discriminatory, because the two businesses are not similarly situated, but it is still protectionist.

3. States may not directly regulate interstate commerce

The third principle derived from the dormant Commerce Clause is that a state's power to regulate commercial transactions stops at the state's borders. No state may directly regulate interstate commerce or commerce taking place in other states. Any such extraterritorial effect makes a state regulation virtually per se invalid.

[O]ur cases concerning the extraterritorial effect of state economic regulations stand at a minimum for the following propositions: First, the "Commerce Clause . . . precludes the application of a State statute to commerce that takes place wholly outside of the State's borders, whether or not the commerce has effects within the state" Second, a statute that directly controls commerce occurring wholly outside the boundaries of a State exceeds the inherent limits of the enacting State's authority and is invalid regardless of whether the statute's extraterritorial effect was intended by the legislature. The critical inquiry is whether the practical effect of the regulation is to control conduct beyond the boundaries of the State.⁶¹

Under this principle, the Court has invalidated a state law on minimum liquor pricing that had the practical effect of regulating the price at which manufacturers could sell liquor in other states,⁶² a state law regulating takeovers of companies doing business in Illinois that would have affected some transactions occurring outside the state,⁶³ and a state milk-price statute that effectively regulated milk prices in neighboring states.⁶⁴ The extraterritorial principle is an outgrowth of the nineteenth century doctrine that states lacked constitutional authority to regulate acts of interstate commerce, that is, actual shipments of goods in their original packages moving between states.⁶⁵

4. States may not unnecessarily burden interstate commerce

The fourth principle derived from the dormant Commerce Clause is that no state may impose significant economic burdens on interstate commerce that exceed the local benefits of regulation. When the state exercises its police powers to protect public health or its taxing power, e.g., by ban-

⁶¹ *Healy v. Beer Inst.*, 491 U.S. 324, 336 (1989).

⁶² *Brown-Forman Distillers Corp.*, 476 U.S. at 579-80.

⁶³ *Edgar v. MITE Corp.*, 457 U.S. 624, 643-46 (1982).

⁶⁴ *Baldwin v. G.A.F. Seelig*, 294 U.S. 511, 528 (1935).

⁶⁵ *Bowman v. Chi. & Nw. Ry.*, 125 U.S. 465, 496-97 (1888); *Vance v. W.A. Vandercook Co.*, 170 U.S. 438, 444-45 (1898).

ning smoking in public places or imposing high taxes on cigarettes, that regulation will often serve both a legitimate state interest and have a negative impact on interstate commerce. Fewer cigarettes will be sold if smoking is banned or the price is raised, harming commerce in tobacco. The Court recognizes that “incidental burdens on interstate commerce may be unavoidable when a State legislates to safeguard the health and safety of its people.”⁶⁶ If those burdens are significant, however, they may violate the Commerce Clause even if nondiscriminatory.

When, however, a statute has only indirect effects on interstate commerce and regulates evenhandedly, we have examined whether the State’s interest is legitimate and whether the burden on interstate commerce clearly exceeds the local benefits. We have also recognized that there is no clear line separating the category of state regulation that is virtually per se invalid under the Commerce Clause, and the category subject to the *Pike v. Bruce Church*⁶⁷ balancing approach. In either situation the critical consideration is the overall effect of the statute on both local and interstate activity.⁶⁸

B. *Commerce in Alcoholic Beverages*

1. Free Trade in the Nineteenth Century

Throughout most of the nineteenth century, alcoholic beverages were treated as ordinary commercial products, and the normal principles of dormant Commerce Clause jurisprudence applied. In 1886, the Supreme Court in *Walling v. Michigan*⁶⁹ struck down a state law that imposed a tax on non-residents engaged in the business of selling liquor to be shipped into Michigan, but not on persons whose principle place of business was within the state. The Court stated that “If this is not a discriminating tax . . . it is difficult to conceive of a tax that would be discriminating,”⁷⁰ declared the tax unconstitutional, and rejected the argument that the tax should be treated differently because its purpose was to discourage the use of intoxicating liquors.⁷¹ It relied for its holding primarily on a non-liquor case, *Welton v. Missouri*,⁷² involving a tax on traveling peddlers, and there is no suggestion that the Court thought of sewing machines any differently than bottles of wine. The taxes were “restraints” that usurped the power of Congress to be the sole regulator of commerce among the states.

⁶⁶ *City of Philadelphia v. New Jersey*, 437 U.S. 617, 623-24 (1978).

⁶⁷ *Pike v. Bruce Church*, 397 U.S. 137, 142 (1970).

⁶⁸ *Brown-Forman Distillers Corp. v. N.Y. State Liquor Auth.*, 476 U.S. 573, 578-79 (1986).

⁶⁹ *Walling v. Michigan*, 116 U.S. 446, 460 (1886).

⁷⁰ *Id.* at 454.

⁷¹ *Id.* at 459-60.

⁷² *Welton v. Missouri*, 91 U.S. 275 (1876).

We have so often held that the power given to Congress to regulate commerce . . . is exclusive in all matters . . . especially as regards any impediment or restriction upon such commerce, that we deem it necessary merely to refer to our previous decisions on the subject, the most important of which are collected in *Brown v. Houston*, 114 U.S. 622, 631, and need not be cited here. We have also repeatedly held that so long as Congress does not pass any law to regulate commerce among the several States, it thereby indicates its will that such commerce shall be free and untrammelled; and that any regulation of the subject by the States, except in matters of local concern only, is repugnant to such freedom.⁷³

States could restrict the manufacture and sale of alcohol within their own borders as part of their police power, as long as such regulations did not affect interstate commerce.⁷⁴

With the rise of the temperance movement, this distinction between local regulation and interstate commerce became a problem. The few states that wanted to restrict liquor were surrounded by states where it was plentiful. As soon as a state passed a dry law, its citizens simply ordered their liquor from wet states. If the dry states passed laws prohibiting their citizens from ordering alcohol from wet states, the Supreme Court simply struck them down as restraints upon interstate commerce. In *Bowman v. Chi. & Nw. Ry.*,⁷⁵ the Court held that it was beyond the power of states to restrict or prohibit the importation of liquor from one state into another. The Court acknowledged that states could not effectively enforce their own dry laws unless they could also prohibit imported liquor, but it held that the Constitution simply did not give states the right to do so.⁷⁶ The Court extended this rule to liquor imported for *commercial use* (re-sale) in *Leisy v. Hardin*.⁷⁷ In the Court's view, a transaction was either part of interstate commerce or a matter of local concern only; it could not be both.⁷⁸ Once it acquired the status of interstate commerce, a package of liquor did not lose that character until it was opened and mingled with the general property of a state. As long as it remained in its original package, liquor was therefore immune from state regulation until sold.⁷⁹

2. The Wilson Act and its interpretation: 1891-1912

The practical result of *Bowman* and *Leisy* was that states could not effectively enforce their dry laws. Anyone could circumvent them by importing liquor through interstate commerce. To close this loophole, Congress

⁷³ *Walling*, 116 U.S. at 455.

⁷⁴ *Thurlow v. Massachusetts*, 46 U.S. 504, 577 (1847); *Mugler v. Kansas*, 123 U.S. 623, 661-63 (1887).

⁷⁵ *Bowman v. Chi. & Nw. Ry.*, 125 U.S. 465, 499-500 (1888).

⁷⁶ *Id.* at 500.

⁷⁷ *Leisy v. Hardin*, 135 U.S. 100 (1890).

⁷⁸ *See Wilkerson v. Rahrer*, 140 U.S. 545, 555 (1891).

⁷⁹ *Leisy*, 135 U.S. at 108-10, 119, 124.

enacted the Wilson Act, which authorized states to regulate imported alcohol “to the same extent and in the same manner” as local alcohol.⁸⁰ The Wilson Act provided:

[All] intoxicating liquors . . . transported into any State or Territory . . . shall upon arrival in such State or Territory be subject to the operation and effect of the laws of such State or Territory enacted in the exercise of its police powers, to the same extent and in the same manner as though such . . . liquors had been produced in such State or Territory, and shall not be exempt therefrom by reason of being introduced therein in original packages or otherwise.

The Wilson Act had a narrow focus. It was intended merely to overturn *Bowman* and *Leisy* and close the loophole that allowed residents of dry states to evade local prohibition by importing their liquor from wet states. It did not change the basic principle that the dormant Commerce Clause applied to alcoholic beverages.⁸¹

The Wilson Act did not accomplish its purpose, however, because the Supreme Court construed it narrowly as empowering States to regulate only the *resale* of imported alcohol in its original package, not the direct *shipment* of alcohol to consumers. In *Rhodes v. Iowa*,⁸² the Supreme Court revisited the same Iowa law that was struck down in *Bowman*. It construed the words “upon arrival” in the Wilson Act to mean that state law could attach to an interstate shipment of liquor only after delivery, and not before. Therefore, Iowa could not impose its own regulations until the recipient attempted to re-sell the liquor. Even after crossing state lines, a shipment of liquor was still interstate commerce, and retained its character as interstate commerce until delivery was completed. The importation, transportation and receipt of a package were all core aspects of interstate commerce and could not be regulated by the states without a clear statement from Congress that it intended to remove the immunity of interstate commerce from transportation and importation as well as from resale in the original package.⁸³

The *Bowman/Leisy* loophole remained largely intact. Although a dry state could prohibit the resale of imported liquor after it was delivered, the state was still powerless to stop its citizens from personally evading dry

⁸⁰ 26 STAT. 313, ch. 728 (1890), now codified at 27 U.S.C. § 121.

⁸¹ See *Scott v. Donald*, 165 U.S. 58, 100-01 (1897) (“the state cannot, under the [Wilson Act], establish a system which . . . discriminates between interstate and domestic commerce” in liquor and creates preferences for domestic products); *Vance v. W.A. Vandercook Co.*, 170 U.S. 438, 455-57 (1898) (Wilson Act does not authorize states to burden interstate commerce in liquor through extensive and inconvenient regulations); *Adams Express Co. v. Kentucky*, 214 U.S. 218 (1909) (regulations barring delivery of alcohol to inebriate could not be enforced against interstate shipper).

⁸² *Rhodes v. Iowa*, 170 U.S. 412 (1898).

⁸³ *Id.* at 423-24. See also *Louisville & Nashville R.R. Co. v. F. W. Cook Brewing Co.*, 223 U.S. 70 (1912) (regulations barring transportation of alcohol into dry county could not be enforced against an interstate shipper).

laws by mail-ordering liquor. As the number of dry states grew, the wholesale evasion of those dry laws grew to an estimated 20,000,000 gallons of liquor per year shipped through interstate commerce.⁸⁴

3. The Webb-Kenyon Act of 1913

The political pressure from the dry states and the temperance movement to close the *Bowman/Leisy/Rhodes* loophole was intense, and Congress went back to the drawing board to try again. They came up with the Webb-Kenyon Act,⁸⁵ which provided:

That the shipment or transportation . . . of any spirituous . . . or other intoxicating liquor of any kind, from one State . . . into any other State . . . which . . . is intended, by any person interested therein, to be received, possessed, sold, or in any manner used, either in the original package or otherwise, in violation of any law of such State . . . is hereby prohibited.

The Webb-Kenyon Act, like the Wilson Act before it, had a narrow focus. It was intended to overturn *Bowman*, *Leisy*, and *Rhodes*. The names of those cases came up repeatedly during Congressional debates.⁸⁶ Congressman Webb explained that the bill was intended to address the problem that, “under the present law and decisions, no State can interfere with the interstate shipment of liquor until it has been actually delivered to the consignee [and] no State official is permitted to touch any interstate shipment of liquor [even if] consigned to a ‘blind tiger,’⁸⁷ ‘bootlegger,’ or ‘speak-easy.’”⁸⁸ Senator Kenyon likewise explained that the bill was intended simply to remove the immunity afforded to interstate transportation of liquor under the Commerce Clause, and to allow dry States to prevent their citizens from evading local prohibition.

I am not concerned at all with the question of whether a State in the exercise of its police power might adopt a law prohibiting the manufacture or sale of intoxicating liquors. If it does do so, it ought to be able to make that law effective. . . . If intoxicating liquors can be freely shipped into a State which has a prohibitory law and the State government is powerless to prevent it . . . then, indeed, it is time for some further amendment to our Constitution.⁸⁹

⁸⁴ 49 CONG. REC. 699-700 (1912) (statements of Sen. Sanders).

⁸⁵ 37 STAT. 699, codified as 27 U.S.C. § 122 (2006).

⁸⁶ See 49 CONG. REC. at 764-67; 49 CONG. REC. 2529, 2689-90, 2794-96, 2807, 2817, 2834, 2909-10 (1913).

⁸⁷ A blind tiger was a restaurant that sold illegal liquor. The name supposedly derives from the practice of placing a stuffed tiger in the window or on the tables to alert patrons that bootleg booze was available in the back room. See SINCLAIR LEWIS, *ELMER GANTRY passim* (1927).

⁸⁸ H.R. REP. NO. 62-1461, at 2.

⁸⁹ 49 CONG. REC. 761 (1912).

No one at the time understood Webb-Kenyon to delegate power to states to discriminate against, burden, or regulate interstate commerce, because such delegation was thought to be beyond the power of Congress. At the time of Webb-Kenyon, the understanding was that state regulation of alcohol under the police power and federal regulation under the commerce power were mutually exclusive. Each had absolute authority within its own sphere. Congress could not constitutionally delegate authority to states to regulate interstate commerce.⁹⁰ Instead, Congress exercised its own authority over commerce to prohibit shipments of alcohol from wet to dry states, depriving them of their character as interstate commerce. That way, states could regulate such shipments as soon as they crossed the border under their police powers.⁹¹ The limited purpose of the Webb-Kenyon Act is clear from its title: "An Act divesting intoxicating liquors of their interstate character *in certain cases*"—namely those covered by *Bowman*, *Leisy* and *Rhodes*, where alcohol was being shipped into a dry state.⁹²

Nor did anyone at the time suggest that the Webb-Kenyon Act would change the *Walling v. Michigan* rule that wet states could not discriminate against interstate commerce in liquor.⁹³ No one suggested that it changed the rule in *Vance v. W.A. Vandercook Co.*⁹⁴ and *Adams Express Co. v. Kentucky*,⁹⁵ that wet states in which liquor was legal could not burden or regulate interstate commerce in liquor. In the debates in Congress, in which *Bowman* and *Rhodes* were repeatedly mentioned, these other lines of cases are not mentioned at all. Indeed, when Senator Root expressed concern over the scope of the Act,⁹⁶ he was assured by his colleagues that the bill was a narrow one that merely allowed dry states to prohibit imports upon

⁹⁰ 49 CONG. REC. 767 (1912) (statements of Sen. Kenyon); *id.* at 2912 (statements of Sen. Thornton).

⁹¹ *Id.* at 2912-13 (statements of Sen. Kenyon); *id.* at 2917 (statements of Sen. Stone).

⁹² 37 STAT. 699, ch. 90 (1913) (emphasis added).

⁹³ Indeed, there were few such laws. Webb-Kenyon was passed in 1913, at the height of the temperance movement. Several states had adopted state-wide prohibition. *E.g.*, GA. CODE ANN. § 1770nn (1907); N.C. REV. LAWS § 2058 (Pell 1908). Most other state liquor codes focused on local option laws that gave communities the power to ban the sale and use of alcohol. *E.g.*, MASS. REV. LAWS ch. 100, §§ 13, 48 (1902); N.M. STAT. ANN. §§ 2927 et seq. (1915); ANN. CONSOL. LAWS OF N.Y., §§ 13, 23 (1917); GEN. CODE OHIO §§ 6097, 6108 et seq. (1910); S.D. REV. CODE § 2856 (1903); PIERCE'S WASH. CODE § 5713 (1905). A few laws prohibited shipments into dry areas by anyone, but neither discriminated against out-of-state sellers nor imposed burdensome regulations on them. *E.g.*, KY. STAT. §§ 2554, 2557a, 2569a (Carroll 1915); ANN. CONSOL. LAWS OF N.Y., §§ 13, 23 (1917). The remaining state liquor laws were classic police power regulations, aimed at moral issues that did not implicate interstate commerce, *e.g.*, banning sales to minors and habitual drunkards, MO. STAT. ANN. § 3017, outlawing sales to Indians, *e.g.*, ANN. CONSOL. LAWS OF N.Y. § 29 (1917); and prohibiting such unseemly activities as women playing banjos in saloons. N.M. STAT. ANN. § 2906 (1915).

⁹⁴ *Vance v. W.A. Vandercook Co.*, 170 U.S. 438 (1898).

⁹⁵ *Adams Express Co. v. Kentucky*, 214 U.S. 218 (1909).

⁹⁶ 49 CONG. REC. 2915 (1913).

the same terms as they prohibit domestic sales.⁹⁷ The bill would only “remove the restrictions which now bind the action of the States in their efforts to honestly enforce their lawful prohibition enactments,”⁹⁸ by “imposing the condition that the goods shall be so subjected to the laws of a State [but] not in any sense whatever delegating authority to the State to control by its legislation interstate commerce.”⁹⁹

There were few opportunities for the courts to interpret Webb-Kenyon in the six years from when it was enacted to when it was mooted by Prohibition. The few cases that were decided adhered to the view that the Act merely gave states power to ban direct shipments of alcohol into dry areas, overturning *Bowman* and finally closing the loophole that had allowed citizens in dry states to evade local prohibition laws through interstate commerce. The Act had no application beyond that.¹⁰⁰ The Supreme Court held that it did not give states power to prohibit shipments into counties where possession and use of alcohol was legal,¹⁰¹ and did not change the general rule that the States may not regulate commerce wholly interstate.

It would be difficult to frame language more plainly indicating the purpose of Congress Such shipments are prohibited only when . . . they shall be possessed, sold or used in violation of any law of the State wherein they are received. Thus far *and no farther* has Congress seen fit to extend the prohibitions of the Act in relation to interstate shipments.¹⁰²

4. Prohibition

In 1919, the Eighteenth Amendment was ratified, and the “Noble Experiment”¹⁰³ of nationwide Prohibition began. Section 1 provided:

After one year from the ratification of this article the manufacture, sale, or transportation of intoxicating liquors within, the importation thereof into, or the exportation thereof from the United States and all territory subject to the jurisdiction thereof for beverage purposes is hereby prohibited.

⁹⁷ *Id.* at 2916 (statements of Sen. Stone).

⁹⁸ *Id.* at 2807 (statements of Rep. Webb).

⁹⁹ *Id.* at 702 (statements of Sen. McCumber).

¹⁰⁰ *James Clark Distilling Co. v. W. Md. Ry. Co.*, 242 U.S. 311, 322 (1917) (Act’s “only purpose was to give effect to state prohibition” laws). *See also* *Brennen v. S. Express Co.*, 90 S.E. 402 (S.C. 1916) (Act does not apply unless there is a state law prohibiting receipt, possession, sale, or use of liquor); *McCormick & Co. v. Brown*, 286 U.S. 131, 142 (1932) (Act “referred to the prohibitory laws of the States, the enforcement of which it was intended to aid”).

¹⁰¹ *Seaboard Air Line Ry. v. North Carolina*, 245 U.S. 298, 303 (1917).

¹⁰² *Adams Express Co. v. Kentucky*, 238 U.S. 190, 199 (1915) (emphasis added).

¹⁰³ The phrase is generally attributed to Herbert Hoover. *See* OXFORD DICTIONARY OF MODERN QUOTATIONS 104 (1991) (1928 letter to Sen. Borah).

The Amendment had three big loopholes. First, it did not prohibit possession or consumption of liquor. Second, it gave everyone wealthy enough to do so (such as the Senators themselves) one year to stock their personal wine cellars so they could take advantage of the first loophole. Third, it was limited to sale “for beverage purposes,” and did not prohibit selling alcohol for medicinal purposes, so that even those who could not afford to stock their cellars under the second loophole could at least get a prescription for whiskey to calm their nerves and help ward off the flu.

Section 2 provided:

The Congress and the several states shall have concurrent power to enforce this Article by appropriate legislation.

This simple provision altered the Constitution in a significant way. For the first time, it gave Congress police power. The traditional wall of separation between state police power and federal commerce power had been breached.

C. *The Twenty-First Amendment and the Repeal of Prohibition*

Prohibition was, of course, a national disaster. The idea was absurd from the beginning, and it was so widely ignored, evaded, and corrupted, and ran so contrary to basic American notions of individual liberty, that it delegitimized the entire U.S. legal system.

[The] Eighteenth Amendment . . . is the first provision ever written into the Constitution which affects directly the life and habits of the people. . . . [T]housands of people who never drank before started immediately to drink as a protest against this infringement of their personal liberty.¹⁰⁴

Prohibition survived barely 13 years. Congress drafted the Twenty-First Amendment to repeal it in 1933, and it was ratified by state conventions later that same year.¹⁰⁵

¹⁰⁴ RATIFICATION OF THE TWENTY-FIRST AMENDMENT TO THE CONSTITUTION OF THE UNITED STATES: STATE CONVENTION RECORDS AND LAWS 191 (Everett S. Brown ed., 1938) [hereinafter RATIFICATION OF THE TWENTY-FIRST AMENDMENT] (statement of Mr. Darnall, President of Maryland Convention). See also 76 CONG. REC. 4514 (1933) (Rep. LaGuardia arguing for repeal “because of the widespread violation of the law by the criminal element [and the] universal disregard of the law by well-meaning, law-abiding people.”).

¹⁰⁵ Article V of the Constitution provides that Amendments may be ratified either by 3/4 of the state legislatures, or by conventions in 3/4 of the states. Although repeal had wide popular support, the drafters feared the state legislatures were too easily captured by the temperance movement and would be reluctant to vote for repeal once it was cast as a moral issue, so they took the unusual step of writing into

Section 1 of the Twenty-First Amendment repealed the Eighteenth, and national prohibition ended. But, what about state prohibition? Several states wished to remain dry, as they had been before Prohibition, and they feared a return to the *Bowman/Leisy/Rhodes* doctrine under which they would be powerless to prevent their citizens from evading local dry laws through interstate commerce.¹⁰⁶ Merely re-enacting the Webb-Kenyon Act might not be adequate because it could be repealed by Congress or held unconstitutional by the Supreme Court. Senator Borah reminded his colleagues that the constitutionality of Webb-Kenyon had initially been sustained only by a divided Court, its continued constitutionality was in doubt, and the Congress could not be counted on to maintain it indefinitely.¹⁰⁷

So, Congress added section 2 to the Amendment to write Webb-Kenyon into the Constitution permanently.¹⁰⁸ It provides:

The transportation or importation into any State . . . for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited.

This language is virtually identical to the Webb-Kenyon Act, 27 U.S.C. § 122:

The shipment or transportation . . . of any . . . intoxicating liquor . . . from one State . . . into any other State . . . to be received, possessed, sold, or in any manner used . . . in violation of any law of such State . . . is hereby prohibited.

The legislative history shows without doubt that the purpose of Section 2 was the same as Webb-Kenyon—“to assure the so-called dry States against the importation of intoxicating liquor into those States.”¹⁰⁹ Senator Blaine reiterated this point many times during his introduction of the Amendment, stating that “[t]he Committee felt . . . that we could well afford to guarantee to the so-called dry States the protection designed by Section two,” and “I am willing to grant to the dry States full measure of pro-

the Twenty-First Amendment the requirement that it be ratified by state conventions. U.S. CONST. amend. XXI, § 3. It is the only Amendment to ever have been ratified in this manner.

¹⁰⁶ See 76 CONG. REC. 4170-71 (1933) (Senator Borah argued that after repeal, the dry states would need to be able to fend off attempts to evade their prohibition laws by illegally importing alcohol as had been allowed under the *Bowman/Rhodes* line of cases); *id.* at 4171 (Senator Wagner argued that the Amendment should give “the dry States . . . assurance that they will be protected” from decisions like *Bowman*).

¹⁰⁷ 76 CONG. REC. 4170.

¹⁰⁸ 76 CONG. REC. 4141 (1933) (statement of Sen. Blaine on behalf of drafting committee); *Craig v. Boren*, 429 U.S. 190, 205-06 (1976).

¹⁰⁹ 76 CONG. REC. at 4141 (statement of Sen. Blaine on behalf of drafting committee). See also Duncan Baird Douglass, *Constitutional Crossroads: Reconciling the Twenty-First Amendment and the Commerce Clause to Evaluate State Regulation of Interstate Commerce in Alcoholic Beverages*, 49 DUKE L.J. 1619, 1631-36 (2000) (reviewing historical reasons for enactment of Section 2).

tection, and thus prohibit the wet States from interfering in their internal affairs respecting the control of intoxicating liquors.”¹¹⁰ The House sponsor, Rep. Robinson, repeated the same message, stating that “Section 2 attempts to protect dry States.”¹¹¹ Every other House member to speak on Section 2 specifically agreed that its purpose was to aid and protect dry states in permitting them, if they wish, to exclude all liquor traffic in their domain.¹¹²

Congress also made it clear that the Amendment had *nothing to do with interstate commerce among wet states*. Senator Glass, who wrote Section 2, explained its limitation:

Liquors may be shipped across a State in interstate commerce from one wet State to another wet State, but [Section 2] as I have drafted it prohibits the shipment of intoxicating liquors into a State whose laws prohibit the manufacture, sale, or transportation of liquors.¹¹³

In the state ratifying conventions, the delegates consistently delivered the same message: Prohibition had been a societal and legal disaster. Socially, it had trampled on individual liberties, done nothing to advance temperance, led to rampant crime, and caused widespread disrespect for authority. Legally, it had upset the natural order of things by violating the sacred principle that only the states, not the federal government, could exercise the police power. The delegates called for a return of the police power to the states so that they could regulate alcohol in ways that promoted temperance realistically without infringing individual liberty.

The core concern of the state delegates was temperance. It is mentioned in 17 of the 19 recorded debates¹¹⁴ and by almost every speaker. For example, Gov. Cross of Connecticut said the Amendment would “promote temperance.”¹¹⁵ Mr. Marshall of Indiana said that “prohibition did not bring temperance,” but its repeal would.¹¹⁶ Gov. Ritchie of Maryland said repeal was a “victory in the interest of temperance in the true sense.”¹¹⁷ Mr. Butler of New York said, “With repeal, the movement for true temperance will be resumed.”¹¹⁸ Gov. Comstock of Michigan said, “We want a regulated traffic in liquor, one that makes for temperance and not for license.”¹¹⁹ Similar

¹¹⁰ 76 CONG. REC. at 4141.

¹¹¹ *Id.* at 4518.

¹¹² *Id.* at 4523 (Rep. McSwain); *id.* at 4526 (Rep. Tierny); *id.* at 4159 (Rep. Garber).

¹¹³ *Id.* at 4219.

¹¹⁴ Only nineteen of thirty-eight states kept records of their debates, which are collected in RATIFICATION OF THE TWENTY-FIRST AMENDMENT, *supra* note 104.

¹¹⁵ *Id.* at 62.

¹¹⁶ *Id.* at 142.

¹¹⁷ *Id.* at 194.

¹¹⁸ *Id.* at 304.

¹¹⁹ *Id.* at 229.

sentiments were expressed by delegates in Idaho,¹²⁰ Missouri,¹²¹ Colorado,¹²² Florida,¹²³ Iowa,¹²⁴ Kentucky,¹²⁵ New Jersey,¹²⁶ Utah,¹²⁷ Virginia,¹²⁸ and Washington.¹²⁹ In New York, the convention ended with Rev. Quinn calling on God to “direct our people to the true idea of temperance and sobriety.”¹³⁰ Interestingly, some delegates thought that the promotion of low-alcohol drinks like beer and wine in lieu of hard liquor was the key to temperance.¹³¹

Delegates also expressed concern that the Eighteenth Amendment had given police power to the federal government. This violated the natural constitutional order in which states had exclusive police power. The wisdom of this natural order had been confirmed by the total ineptitude of the federal government’s attempts to stop bootlegging during Prohibition. To many delegates, this was the more important issue,¹³² and it found expression in 13 of the 19 recorded conventions. Mr. Montgomery of Pennsylvania said that “the Constitution of the United States was most wise in reserving to the several states the police power and in delegating or granting no police power to the Federal Government,” and that the Twenty-First Amendment would restore this traditional balance.¹³³ Mr. Wadsworth of New York said that prohibition had “invited the states to surrender a very important part of their police power.”¹³⁴ Mr. Riter of Utah said that prohibition “transferred from the states to the federal government police power in regard to control and prohibition of personal conduct of citizens.”¹³⁵ Similar remarks were made by delegates in Illinois,¹³⁶ New Jersey,¹³⁷ Iowa,¹³⁸

¹²⁰ RATIFICATION OF THE TWENTY-FIRST AMENDMENT, *supra* note 104, at 100 (expressing the need to adopt policy “which will promote true temperance”).

¹²¹ *Id.* at 249 (“I take it that all of you believe in temperance.”).

¹²² *Id.* at 41 (declaring that “we must work for a new form of temperance”).

¹²³ *Id.* at 70 (stating that “we are fighting the battles of temperance”).

¹²⁴ *Id.* at 153 (defining the vote as “for temperance as opposed to prohibition”).

¹²⁵ *Id.* at 166 (“We shall have before us the duty [to] teach . . . temperance.”).

¹²⁶ RATIFICATION OF THE TWENTY-FIRST AMENDMENT, *supra* note 104, at 281 (“promoting temperance”).

¹²⁷ *Id.* at 401 (declaring the need to “find new ways for encouraging temperance”).

¹²⁸ *Id.* at 439 (noting that “prohibition retarded rather than promoted temperance”).

¹²⁹ *Id.* at 457 (recommending to “re-establish the broad teachings of temperance”).

¹³⁰ *Id.* at 319.

¹³¹ *Id.* at 281, 299.

¹³² See 76 CONG. REC. 4144 (1933) (statements of Sen. Wagner) (“The question which has troubled the American people since the eighteenth amendment was added to the Constitution was not at all concerned with liquor. It was a question of government; how to restore the constitutional balance of power and authority in our Federal system which had been upset by national prohibition.”).

¹³³ RATIFICATION OF THE TWENTY-FIRST AMENDMENT, *supra* note 104, at 355.

¹³⁴ *Id.* at 305.

¹³⁵ *Id.* at 411.

¹³⁶ *Id.* at 112.

¹³⁷ *Id.* at 282.

Kentucky,¹³⁹ Michigan,¹⁴⁰ New York,¹⁴¹ and Virginia,¹⁴² and by members of Congress.¹⁴³

Section 2 was not seen as creating a new order. The states wanted the *old* order restored, in which they had exclusive police power and the federal government had exclusive power over interstate commerce. Mr. Byrnes of Missouri said, "You are here to *restore* to its original purity, that sacred civil document, the Constitution of these United States."¹⁴⁴ Mr. Thatcher of New York, referring to the allocation of police power exclusively to the states, said, "[T]here are certain cardinal principles in the Constitution of the United States that must not be violated, and with that realization, may there be a final end to all experiments involving that great document."¹⁴⁵ Mrs. Gaylord of Missouri called for "*the return* to each state of its former right to regulate and control the manufacture, sale and transportation of intoxicating beverages within its own borders."¹⁴⁶ Mr. Robinson of Connecticut said the Twenty-First Amendment would "*return* to the people of the several states . . . their constitutional right to govern themselves in their internal affairs."¹⁴⁷ Mrs. Todd of Kentucky said that the "very essence of Repeal is that the people of the States shall *again* be allowed to legislate for themselves in matters concerning control and regulation of alcoholic beverages."¹⁴⁸

State delegates pledged to exercise their reclaimed police power over alcohol in ways that would promote temperance without unduly infringing individual rights. Mr. Goolrick of Virginia said that the "failure of prohibition . . . may be found in the fact that it was . . . restrictive of the individual rights and privileges of the people."¹⁴⁹ To avoid making the same mistake, Mr. Goolrick recommended that the new system should be "liberal but at the same time . . . tend to promote temperance."¹⁵⁰ Mr. Haldeman of Kentucky proclaimed that the new system would restore "the personal liberty of

¹³⁸ *Id.* at 160.

¹³⁹ RATIFICATION OF THE TWENTY-FIRST AMENDMENT, *supra* note 104, at 169.

¹⁴⁰ *Id.* at 228.

¹⁴¹ *Id.* at 293-94, 306.

¹⁴² *Id.* at 439.

¹⁴³ See the Congressional debates over a proposed section three to the Twenty-First Amendment which would have given Congress concurrent police power to regulate alcohol, but the idea was roundly criticized. 76 CONG. REC. 4144, 4143-46 (1933) (statements of Sens. Blaine, Walsh and Wagner); *id.* at 4155 (statements of Sens. Walsh and Brookhart); *id.* at 4161-62 (statements of Sens. Brookhart and Norris); *id.* at 4173 (statements of Sens. Borah and Black).

¹⁴⁴ RATIFICATION OF THE TWENTY-FIRST AMENDMENT, *supra* note 104, at 260 (emphasis added).

¹⁴⁵ *Id.* at 293-94.

¹⁴⁶ *Id.* at 247 (emphasis added).

¹⁴⁷ *Id.* at 50 (emphasis added).

¹⁴⁸ *Id.* at 172 (emphasis added).

¹⁴⁹ *Id.* at 439.

¹⁵⁰ RATIFICATION OF THE TWENTY-FIRST AMENDMENT, *supra* note 104, at 439-40.

the American citizen.”¹⁵¹ Gov. Ritchie of Maryland pledged that now “the safeguards of the liberties of the American people were going to be preserved and maintained.”¹⁵² Gov. Comstock of Michigan said that “we have decided to go back and try personal liberty once more, the personal liberty we had before Prohibition.”¹⁵³ Given this history, it is ironic that modern state officials are arguing that this Amendment justifies their efforts to restrict individual liberty in a way that does not promote temperance.

D. *Commerce in Alcoholic Beverages After the Twenty-First Amendment*

Interpreting and applying Section 2 of the Twenty-First Amendment to state regulation of commerce in liquor turned out to be harder than its legislative history would suggest. Section 2 says that:

- The transportation or importation of intoxicating liquors into any State
- for delivery or use therein
- in violation of the laws thereof
- is hereby prohibited.

In historical context, the meaning is clear—the transportation or importation of liquor from a wet state into a dry state is prohibited. But the courts have not always approached the interpretation of this Amendment from a historical perspective. If one looks just at the text, three problems of interpretation arise.

First, does the power to “prohibit” transportation and importation include the lesser power to “allow but heavily regulate” transportation and importation?¹⁵⁴

Second, what phrase does “in violation of the laws thereof” modify? If it modifies the words “delivery or use therein,” then the Twenty-First Amendment authorizes a state to prohibit importation only in the narrow circumstances that the importation would violate laws relating to the *delivery or use* of alcohol. Relatively few state regulations would be justified.

¹⁵¹ *Id.* at 169.

¹⁵² *Id.* at 193.

¹⁵³ *Id.* at 228.

¹⁵⁴ Compare *State Bd. of Equalization v. Young's Mkt. Co.*, 299 U.S. 59, 63 (1936) (“Surely the State may adopt a lesser degree of regulation than total prohibition.”), with *Bridenbaugh v. Freeman-Wilson*, 227 F.3d 848, 853 (7th Cir. 2000) (“The greater power to forbid imports does not imply a lesser power to allow imports on discriminatory terms.”).

On the other hand, if the phrase “in violation of the laws thereof” modifies the words “transportation and importation,” a quite different meaning emerges—states have the power to prohibit importation, if the importation would violate the *laws relating to transportation and importation*. Such a reading would justify a broad range of state regulation on interstate commerce.

Third, what is the meaning of the word “laws”? Although the drafters and ratifiers understood it to mean “dry laws” only, the text does not contain that limitation. If interpreted to mean *all* laws, then the Amendment is far more sweeping.

1. The early “broad power” cases

Immediately after the ratification of the Twenty-First Amendment, the Supreme Court decided three cases on the amendment’s scope: *State Bd. of Equalization v. Young’s Mkt. Co.*,¹⁵⁵ *Indianapolis Brewing Co. v. Liquor Control Comm’n*,¹⁵⁶ and *Ziffrin, Inc. v. Reeves*.¹⁵⁷ In *Young’s Mkt. Co.*, the Court ignored the legislative and ratification history of the Amendment and looked only at its text:

The plaintiffs argue that limitation of the broad language of the Twenty-First Amendment is sanctioned by its history; and by the decisions of this Court on the Wilson Act [and] the Webb-Kenyon Act. . . . As we think the language of the Amendment is clear, we do not discuss these matters.¹⁵⁸

The Court held that Section 2 gave states broad power to regulate liquor and interpreted the power to “prohibit” as also including the power to “adopt a lesser degree of regulation than total prohibition.”¹⁵⁹ That regulation could include attaching conditions to the act of transportation itself,¹⁶⁰ and state power was not limited to enforcing dry laws.¹⁶¹ The early cases gave the Amendment such a broad reading that it looked like states could regulate, restrict, and burden interstate sales and deliveries of liquor in any

¹⁵⁵ *Young’s Mkt. Co.*, 299 U.S. 59 (1936).

¹⁵⁶ *Indianapolis Brewing Co. v. Liquor Control Comm’n*, 305 U.S. 391 (1939).

¹⁵⁷ *Ziffrin, Inc. v. Reeves*, 308 U.S. 132 (1939).

¹⁵⁸ *Young’s Mkt. Co.*, 299 U.S. at 63-64.

¹⁵⁹ *See id.* at 63.

¹⁶⁰ *See id.* at 62 (finding that the Amendment confers “upon the State the power to forbid all importations which do not comply with the conditions which it prescribes.”).

¹⁶¹ *See id.* (finding that plaintiffs “request us to construe the Amendment as saying, in effect: The State may prohibit the importation of intoxicating liquors provided it prohibits the manufacture and sale within its borders; but if it permits such manufacture and sale, it must let imported liquors compete with the domestic on equal terms. To say that, would involve not a construction of the Amendment, but a rewriting of it.”).

way they wanted, “unfettered by the Commerce Clause”¹⁶²—perhaps even allowing discrimination against out-of-state interests.¹⁶³

2. The modern “limited power” cases

Almost immediately after its trio of cases in the 1930s that gave the Twenty-First Amendment a broad non-historical reading, the Supreme Court began to retreat from that extreme position. In *William Jameson & Co. v. Morgenthau*, the Court rejected the proposition that “the Twenty-First Amendment . . . gives to the States complete and exclusive control over commerce in intoxicating liquors, unlimited by the Commerce Clause.”¹⁶⁴ It held in *U.S. v. Frankfort Distilleries, Inc.*, a restraint-of-trade case involving liquor price fixing in Colorado, that the Twenty-First Amendment “has not given the states plenary and exclusive power to regulate the conduct of persons doing an interstate liquor business.”¹⁶⁵ Whatever impact the Amendment had, state power was not “unfettered” by the Commerce Clause as unwisely suggested in *Ziffrin*. The federal Commerce power was unaffected, and its scope was limited to dormant Commerce Clause issues.¹⁶⁶

The Court also made it clear that the Twenty-First Amendment gave states no authority to infringe upon constitutionally protected areas other than commerce, such as equal protection, free speech, the Establishment Clause, due process, or the import-export clause. In *Dep’t of Revenue v. James B. Beam Distilling Co.*, the Court struck down a Kentucky law taxing Scotch whisky that violated the export-import clause.¹⁶⁷ The *Young’s Market* cases were relegated to a brief footnote. In *Wisconsin v. Constantineau*, the Court struck down a Wisconsin law permitting the sheriff to issue notices forbidding the sale of alcohol to habitual drunkards without giving them an opportunity to be heard as violating Due Process.¹⁶⁸ In

¹⁶² *Ziffrin*, 308 U.S. at 138-39.

¹⁶³ See *Young’s Mkt. Co.*, 299 U.S. at 63 (stating in dicta that a state might “permit the domestic manufacture of beer and exclude all made without the State”). At the same time, the Court was careful to say that it was not deciding the discrimination issue and was not stating a general principle that state regulatory power was unlimited. See *id.* at 62 (finding the case did not present a question of discrimination prohibited by the Commerce Clause); *Indianapolis Brewing Co v. Liquor Control Comm’n*, 305 U.S. 391, 394 (1939) (declining to consider the issue of discrimination); *Young’s Mkt. Co.*, 299 U.S. at 64 (stating that the Amendment had not “freed the States from all restrictions upon the police power”).

¹⁶⁴ *William Jameson & Co. v. Morgenthau*, 307 U.S. 171, 172-73 (1939).

¹⁶⁵ *U.S. v. Frankfort Distilleries, Inc.*, 324 U.S. 293, 299 (1945).

¹⁶⁶ See *Collins v. Yosemite Park & Curry Co.*, 304 U.S. 518, 538 (1938) (state could not regulate liquor headed for Yosemite National Park); *Hostetter v. Idlewild Bon Voyage Liquor Corp.*, 377 U.S. 324 (1964) (state could not regulate sale of duty-free liquor at airport).

¹⁶⁷ *Dep’t of Revenue v. James B. Beam Distilling Co.*, 377 U.S. 341, 345-46 (1964).

¹⁶⁸ *Wisconsin v. Constantineau*, 400 U.S. 433 (1971).

Craig v. Boren, the Court struck down an Oklahoma law setting the beer drinking age at 21 for males and 18 for females as violating the Equal Protection Clause, commenting that the Twenty-First Amendment was simply irrelevant to anything other than commerce.¹⁶⁹ In *Larkin v. Grendel's Den, Inc.*, the Court struck down a Massachusetts law that permitted nearby churches to veto the issuance of liquor licenses as violating the Establishment Clause, dismissing the Twenty-First Amendment issue in a cursory footnote.¹⁷⁰ And, in *44 Liquormart, Inc. v. Rhode Island*, the Court struck down a Rhode Island law prohibiting liquor advertising as violating the First Amendment, commenting that the Twenty-First Amendment did not give states license to violate other provisions of the Constitution.¹⁷¹

The tone of the Court's discussion of the Twenty-First Amendment also changed—from commenting on its broad authority to commenting on its obvious limitations. Thus, in *Hostetter v. Idlewild Bon Voyage Liquor Corp.*,¹⁷² in which the Court held that states could not regulate duty-free liquor at airports, the Court acknowledged the “broad-power” language of the *Young's Market* trio, but then said:

To draw a conclusion . . . that the Twenty-First Amendment has somehow operated to “repeal” the Commerce Clause wherever regulation of intoxicating liquors is concerned would, however, be an absurd oversimplification. . . . Both the Twenty-First Amendment and the Commerce Clause are parts of the same Constitution. Like other provisions of the Constitution, each must be considered in the light of the other, and in the context of the issues and interests at stake in any concrete case.¹⁷³

In *324 Liquor Corp. v. Duffy*,¹⁷⁴ the Court stated:

The Court has rejected the view that the Twenty-First Amendment has somehow operated to “repeal” the Commerce Clause wherever regulation of intoxicating liquors is concerned. Instead, the Court has engaged in a pragmatic effort to harmonize state and federal powers. The question in each case is “whether the interests implicated by a state regulation are so closely related to the powers reserved by the Twenty-First Amendment that the regulation may prevail, notwithstanding that its requirements directly conflict with express federal policies.”¹⁷⁵

Despite this retrenchment, the Court left the *Young's Market* cases themselves untouched for fifty years. Then, in the 1980s, it revisited the

¹⁶⁹ *Craig v. Boren*, 429 U.S. 190, 204-09 (1976).

¹⁷⁰ *Larkin v. Grendel's Den, Inc.*, 459 U.S. 116 (1982).

¹⁷¹ *44 Liquormart, Inc. v. Rhode Island*, 517 U.S. 484, 516 (1996).

¹⁷² *Hostetter v. Idlewild Bon Voyage Liquor Corp.*, 377 U.S. 324 (1964).

¹⁷³ *Id.* at 331-32. The language is quoted favorably in later cases, *see, e.g.*, *Bacchus Imps. v. Dias*, 468 U.S. 263, 275 (1984); *Brown-Forman Distillers Corp. v. N.Y. State Liquor Auth.*, 476 U.S. 573, 584 (1986).

¹⁷⁴ *324 Liquor Corp. v. Duffy*, 479 U.S. 335 (1987).

¹⁷⁵ *Id.* at 346-47 (citations omitted).

core question of the balance between the Twenty-First Amendment and the dormant Commerce Clause in another trio of cases: *Bacchus Imports, Ltd. v. Dias*,¹⁷⁶ *Brown-Forman Distillers Corp. v. N.Y. State Liquor Auth.*,¹⁷⁷ and *Healy v. Beer Institute*.¹⁷⁸ This time, the result was quite different.

In *Bacchus Imports, Ltd. v. Dias*, the Court took up the issue left open by *Young's Market*: Can states discriminate against interstate commerce and give economic protection to local liquor producers? At issue was a Hawaii law that imposed a 20% tax on liquor imported from other states, but which exempted locally-produced brandy, rum, and wine. Fifty years earlier, the Court had intimated that such a law would be constitutional.¹⁷⁹ Now it held to the contrary, that the law was discriminatory and protectionist and therefore violated the dormant Commerce Clause. This time, the Court took into account the history of its passage and ratification, and found nothing in either the text or the history of the Twenty-First Amendment suggesting that it had given states absolute power over alcohol or had displaced the nondiscrimination principle of the dormant Commerce Clause. Indeed, it held quite clearly that "one thing is certain: the central purpose of the provision was not to empower States to favor local liquor industries by erecting barriers to competition."¹⁸⁰ The Court retreated from the rhetoric of early cases that state power was unlimited and unfettered. Instead, it wrote of a limited Twenty-First Amendment that gave states power to regulate only when state interest clearly outweighed the federal interest in unrestrained interstate commerce, saying "It is by now clear that the Amendment did not entirely remove state regulation of alcoholic beverages from the ambit of the Commerce Clause."¹⁸¹

In *Brown-Forman Distillers Corp. v. N.Y. State Liquor Auth.*, the Court held that the Twenty-First Amendment also did not authorize states to regulate interstate commerce directly and that liquor laws with "extraterritorial" effect violated the dormant Commerce Clause. The New York law at issue effectively fixed nationwide liquor prices by providing that no distiller could sell liquor to a New York distributor at a price higher than the price charged anywhere else. Since several other states also had such laws, their combined effect provided that no distiller could sell its liquor anywhere at a discount. Thus, a few state laws controlled liquor prices everywhere. The Court held that "When a state statute directly regulates . . . interstate commerce, or when its effect is to favor in-state economic interests over out-of-state interests, we have generally struck down the statute with-

¹⁷⁶ *Bacchus*, 468 U.S. 263.

¹⁷⁷ *Brown-Forman Distillers Corp.*, 476 U.S. 573.

¹⁷⁸ *Healy v. Beer Institute*, 491 U.S. 324 (1989).

¹⁷⁹ *State Bd. of Equalization v. Young's Mkt. Co.*, 299 U.S. 59, 63 (1936) (dictum) (A state "may permit the domestic manufacture of beer and . . . subject the foreign article to a heavy importation fee.").

¹⁸⁰ *Bacchus*, 468 U.S. at 275.

¹⁸¹ *Id.*

out further inquiry” as violating the dormant Commerce Clause.¹⁸² The Twenty-First Amendment did not alter this rule.

In *Healy v. Beer Institute*, the Court reiterated the holdings of *Bacchus* and *Brown-Forman* that, if a state liquor law discriminated against interstate commerce, regulated commerce in other states, or provided economic protection to local businesses, it was invalid. *Healy* involved a price affirmation law like the one in *Brown-Forman*, which was also discriminatory because it did not require in-state distillers to make such an affirmation. The Court held the law unconstitutional and concluded that it could not be saved by the Twenty-First Amendment.¹⁸³

3. Dicta in non-Commerce Clause cases

At the same time the Supreme Court was whittling down the scope of the Twenty-First Amendment in dormant Commerce Clause cases, it was inserting contrary dicta in non-Commerce Clause cases. Even while it was striking down every restrictive liquor law that came before it, the Court was paying lip service to the old rule that states had virtually unlimited power to regulate commerce in liquor. In *California Retail Liquor Dealers Assn. v. Midcal Aluminum, Inc.*, the Court struck down a price-posting statute as violating the Sherman Act, despite saying that “The Twenty-First Amendment grants the States virtually complete control over whether to permit importation or sale of liquor and how to structure the liquor distribution system.”¹⁸⁴ In *Capital Cities Cable, Inc. v. Crisp*, the Court struck down an Oklahoma law prohibiting cable TV companies from broadcasting liquor commercials as violating the Federal Communications Act, despite saying that “[t]he States enjoy broad power under § 2 of the Twenty-First Amendment to regulate the importation and use of intoxicating liquor within their borders.”¹⁸⁵ In *44 Liquormart, Inc. v. Rhode Island*, the Court struck down a state law prohibiting advertising the sale price of liquor on First Amendment grounds, despite saying that “the Twenty-First Amendment . . . grants the States authority over commerce.”¹⁸⁶

182 *Brown-Forman Distillers Corp.*, 476 U.S. at 579.

183 *Healy*, 491 U.S. at 341-42.

184 *Cal. Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 110 (1980).

185 *Capital Cities Cable, Inc. v. Crisp*, 467 U.S. 691, 712 (1984).

186 *44 Liquormart, Inc. v. Rhode Island*, 517 U.S. 484, 515 (1996). See also *North Dakota v. United States*, 495 U.S. 423, 431 (1990) (Supremacy Clause case; dictum in plurality opinion that “within the area of its jurisdiction, the State has ‘virtually complete control’ over the importation and sale of liquor and the structure of the liquor distribution system.” (Citing *Young's Market Co.*)).

4. The (brief) re-emergence of the Webb-Kenyon Act

The Webb-Kenyon Act had been re-enacted in 1935 following the repeal of Prohibition,¹⁸⁷ but it was assumed to be superfluous because it duplicated the language of the Twenty-First Amendment. If the Twenty-First Amendment were not strong enough to sustain the constitutionality of a restrictive state liquor law, then a mere statute could not save it. The Webb-Kenyon Act was therefore ignored for 60 years. It was not mentioned in a single Supreme Court liquor case after 1936 except as a historical curiosity.¹⁸⁸ Despite these less than sterling credentials, the states rediscovered Webb-Kenyon when looking for ways to defend their discriminatory wine shipping regimes. They argued that when Congress passed the Act, it had delegated power to states to regulate commerce in alcoholic beverages as they saw fit, even in ways that discriminated against interstate commerce.

The argument was implausible. Nothing in the Act specifically says that states may discriminate against interstate commerce in liquor, and the legislative history reflects universal agreement in Congress that Webb-Kenyon did no such thing.¹⁸⁹ The usual rule is that the courts will not read a Congressional statute as authorizing discrimination unless such intent is clearly and unequivocally stated that “Congress certainly has the power to authorize state regulations that burden or discriminate against interstate commerce, but we will not assume that it has done so unless such intent is clearly expressed.”¹⁹⁰ Indeed, the one previous time this argument had been made, the Supreme Court rejected it in a cursory footnote.¹⁹¹

¹⁸⁷ 37 STAT. 699, ch. 740 (1935).

¹⁸⁸ *Craig v. Boren*, 429 U.S. 190, 205-06 (1976); *Hostetter v. Idlewild Bon Voyage Liquor Corp.*, 377 U.S. 324, 333 n.11 (1964); *Dep’t of Revenue v. James B. Beam Distilling Co.*, 377 U.S. 341, 345 n.7 (1964).

¹⁸⁹ See discussion *supra* Part II.B.3.

¹⁹⁰ *Hillside Dairy, Inc. v. Lyons*, 539 U.S. 59, 66 (2003) (citations omitted); *New York v. United States*, 505 U.S. 144, 171 (1992) (States’ authority to discriminate must be expressed with “unambiguous intent” by Congress); *Wyoming v. Oklahoma*, 502 U.S. 437, 458 (1992) (Congress must manifest “unambiguous intent” to allow States to discriminate).

¹⁹¹ *James B. Beam Distilling Co.*, 377 U.S. at 345 n.7 (“There is nothing in . . . the language of either the Wilson Act or the Webb-Kenyon Act to support the view that Congress intended by those laws to consent to state taxation upon importation of liquor.”).

III. THE WINE WAR

A. *Background*

1. History of the three-tier system

Before Prohibition, there had been competition in the alcoholic beverage trade, which led to (gasp!) lower prices, abundant product availability, and lots of beer-drinking. Everyone was happy, except those in the temperance movement. After Repeal, supporters of temperance argued that all the free trade and unregulated competition that had existed before Prohibition was responsible for excessive consumption, and if we did not want to return to the sinful days of the “saloon,” we’d better find a way to restrict competition, raise prices and reduce availability. So, the states created the three-tier system—manufacturers had to sell only to wholesalers who sold to retailers, and no one could have any business interest in more than one tier. Competition among wholesalers was outlawed. Prices were fixed. And there were plenty of local entities handling liquor the states could tax.

Exactly what “problem” the three-tier system was supposed to solve was unclear. Its advocates talked about preventing the return of those nineteenth century dens of iniquity called “saloons,” but creating three distribution tiers was irrelevant to this issue. It also did not work; saloons are quite common in most cities. Its advocates also talked about preventing a return to the evil of the “tied house,” an arrangement whereby a beer manufacturer would directly own and control a pub or inn that sold only its products. Why anyone thought this was an evil is not explained anywhere—the only argument advanced was that the manufacturer would pressure the innkeeper to sell as much beer as possible, leading to excessive drinking, but the argument is absurd. Was the assumption that the innkeeper would otherwise try *not* to sell beer, thereby going broke? Anyone in the business of selling alcohol is driven by the same profit motive—to sell as much as possible. Creating a three tier system does not miraculously turn manufacturers, wholesalers, and retailers into board members of the Temperance League. In any event, the three-tier system did not end tied houses—it just tied them to wholesalers instead of manufacturers.

Two justifications for the system are most plausible. First, because organized crime had taken over broad control of all aspects of the liquor industry during Prohibition, creating multiple tiers and prohibiting ownership in more than one tier could dilute the mob’s post-Prohibition influence. Second, the creation of a mandatory wholesale distributor system gave the states a local, easily taxed entity, helping raise revenue that was sorely needed after five years of the Great Depression.

The three-tier system made the wine war inevitable. If all wine must pass through a local wholesaler to reach consumers, it creates a bottleneck.

When there are too many wineries and too few wholesalers, the system will fail because the wholesalers will service the large volume producers and the small wineries will be frozen out of access to the market if they are denied direct access. Their only recourse will be a legal war.

2. The wine industry today

The inevitable happened, of course. There are now 25,000 different wines produced in the United States. There are more than 4,000 wineries.¹⁹² Consumer interest and demand has skyrocketed,¹⁹³ and the three-tier system cannot handle it. The number of wholesalers is steadily shrinking. Compared to the 1960s, there are now six times as many wineries but only one-sixth the number of wholesalers.¹⁹⁴ That has turned the three-tier distribution system into the three-tier non-distribution system. What started out as a system to allow controlled and regulated distribution has become its major obstacle.

Of the 25,000 wines, only about 500 make it through the system to retail shelves. Fifty large wineries dominate the market and provide 90% of the wine that is handled by the three-tier system. Fewer than 100 wineries have stable national distribution in any form.¹⁹⁵ Three thousand wineries have no wholesaler at all, even in local markets. Small wineries can sometimes obtain temporary wholesale distribution to major markets developing a consumer demand *without* the product actually being available—for example, by being mentioned favorably several times in a publication such as *Wine Spectator*—but nothing will get those wines to Indiana or Arkansas.¹⁹⁶ Without a wholesaler, a winery may sell only to tourists who stop by, and in small quantities to individual consumers by direct shipment.

However, state regulatory systems were not set up for direct shipping. All sales were supposed to go through wholesalers. In 1986, California passed the first law permitting direct shipments, but only from states that,

¹⁹² Brief for WineAmerica et al. at 5-6, *Granholt v. Heald*, 544 U.S. 460 (2005). Most of the growth in wineries has taken place outside of California, in states like Oregon, Texas, Michigan, New York, and Washington. In Texas alone, the number of wineries has gone from six in 1980 to ninety-one today. There are now wineries in all fifty states.

¹⁹³ The circulation of the *Wine Spectator* has gone from 150,000 in 1994 to nearly 375,000 in 2004 with a readership of more than one million. *Wine Spectator Advertising Information: Paid Circulation Has Grown Rapidly*, WINE SPECTATOR (2003), available at http://www.winespectator.com/Wine/Images/Graphics/ads/WS_NAT_EKIT.pdf (last visited Aug. 21, 2007).

¹⁹⁴ At its peak, there were around 5,000 wholesalers. Now there are approximately 400. Alan E. Wiseman & Jerry Ellig, *Market and Nonmarket Barriers to Internet Wine Sales: The Case of Virginia*, 6:2 BUSINESS AND POLITICS at 5 (2004), available at <http://www.bepress.com/bap/vol6/iss2/art4> (last visited Aug. 21, 2007); *FTC Report*, *supra* note 17, at 6.

¹⁹⁵ Wiseman & Ellig, *supra* note 194, at 5.

¹⁹⁶ See *FTC Report*, *supra* note 17, at 23-25.

on a reciprocal basis, allowed its citizens to import California wines.¹⁹⁷ A dozen other states passed similar laws.¹⁹⁸ A few states began to allow direct shipping more generally,¹⁹⁹ and a few allowed its citizens to ship back wine purchased in person on site at the winery's tasting room.²⁰⁰ Most states refused to permit any form of direct shipping, though. Wine could only be distributed by wholesalers, even if that meant 3,000 wineries were kept out of the market.

Foreclosed from national distribution, many small wineries turned their attention to developing a local market. In many areas, they have become valuable local resources, bringing employment and tourism to economically depressed rural areas. They are credited with transforming the economy of the Finger Lakes district of New York, the Willamette Valley of Oregon, and the Columbia River Valley in Washington. They generate new tax revenues for the states. They attract tourists and contribute as anchor sites in tourist areas, by offering restaurants, bed-and-breakfasts, inns, boutiques, and craft businesses. For every \$3 a winery receives in gross revenue from all sources, tourists will add roughly \$1 to the local economy.²⁰¹ Accordingly, the states began to find ways to assist the growth of local wineries—creating wine grape councils, wine trails, reduced license fees, and the right to sell directly on the premises without having to find a wholesaler.

3. The Internet opens new supply routes, but the wholesalers close them

Then came the Internet. Its emergence as a national distribution channel has substantially increased consumer access to rare, unusual, and high-end wines. Direct shipments from wineries to consumers are estimated at over \$500 million annually, or 3% of the wine market.²⁰² The vision of the Founders had been that some day we would become a single national economic unit, with producers in every state having access to the markets in every other.

Our system, fostered by the Commerce Clause, is that every farmer and every craftsman shall be encouraged to produce by the certainty that he will have free access to every market in the Nation. . . . Likewise, every consumer may look to the free competition of every producing

¹⁹⁷ CAL. BUS. & PROF. CODE § 23661.2(b) (repealed following *Granholtm*).

¹⁹⁸ *E.g.*, IOWA CODE § 123.187 (2003).

¹⁹⁹ *E.g.*, N.H. REV. STAT. § 178:14 (2003).

²⁰⁰ *E.g.*, ARIZ. REV. STAT. § 4-203.04(J).

²⁰¹ Brief for WineAmerica et al., *supra* note 192, at 7, n.6 (citing Bill Nelson & Cary Greene, *Components of a Model Winery Law*, VINEYARD AND WINERY MANAGEMENT (Vol. 29, No. 3, May/June 2003)).

²⁰² *FTC Report*, *supra* note 17, at 5.

area in the Nation to protect him from exploitation by any. Such was the vision of the Founders; such has been the doctrine of this Court which has given it reality.²⁰³

The Internet was about to make this vision a reality.

The possibility of a true national Internet wine market threatened the wine wholesalers' privileged (and lucrative) position as wine's exclusive distributor. They reacted quickly, by going to the state legislatures with proposed legislation²⁰⁴ that would ban direct Internet sales. Wholesalers plied gullible legislators with stories of tax evading scofflaws and anonymous bootleggers using the Internet to sell booze to kids with impunity, and they made large campaign contributions.²⁰⁵ Most state legislatures passed prohibition laws easily.

Small wineries were frustrated. Consumers were frustrated. The wholesalers had demanded and obtained statutory protection against Internet competition, thereby changing the system from one that distributed wine to one that prevented distribution. The stage was set for *Granholm*.²⁰⁶

B. *Granholm v. Heald*

1. The case

In 2000, thirteen wine consumers challenged Michigan's law prohibiting direct interstate wine sales and shipments. They were fed up with laws that denied them access to the hundreds of small producers whose wines were not distributed by the wholesalers, but were readily available on the Internet. They were joined by a small California winery that did not have a wholesaler in Michigan and, consequently, was completely excluded from the market.²⁰⁷

²⁰³ See *H.P. Hood & Sons, Inc. v. Du Mond*, 336 U.S. 525, 539 (1949).

²⁰⁴ *E.g.*, IND. CODE § 7.1-5-11-1.5(a) (2003) (provided that: "It is unlawful for a person in the business of selling alcoholic beverages in another state or country to ship or cause to be shipped an alcoholic beverage directly to an Indiana resident who does not hold a valid wholesaler permit under this title. This includes the ordering and selling of alcoholic beverages over a computer network.").

²⁰⁵ The wine and spirits wholesalers trade associations are the second-largest contributors to state political campaigns in the U.S. See Vijay Shanker, Note, *Alcohol Direct Shipment Laws, the Commerce Clause, and the Twenty-First Amendment*, 85 VA. L. REV. 353, 361-64 (1999) (wholesalers contribute substantial amounts of money to state legislative candidates; most state laws prohibiting small wineries from direct shipping were actually drafted by lobbyists for the wholesalers).

²⁰⁶ *Granholm v. Heald*, 544 U.S. 460 (2005); *Heald v. Engler*, 342 F.3d 517 (6th Cir. 2003), *cert. granted*, 72 U.S.L.W. 3507 (U.S. May 24, 2004) (No. 03-1116); argued together with *Swedenburg v. Kelly*, 358 F.3d 223 (2d Cir. 2004), *cert. granted*, 72 U.S.L.W. 3600 (U.S. May 24, 2004) (No. 03-1247).

²⁰⁷ *Granholm*, 544 U.S. at 468.

Michigan was among two dozen states that prohibited direct interstate shipment of wine to consumers.²⁰⁸ It was chosen as a test case because its law was among the most discriminatory and least defensible. At the same time that Michigan was preventing out-of-state wineries from selling and shipping directly to consumers, it allowed its own 40 in-state wineries to do so.²⁰⁹ Michigan also allowed its 7,500 in-state retailers²¹⁰ to ship wine directly to consumers. The Commerce Clause is at its strongest and the Twenty-First Amendment its weakest when states discriminate, so this was the ideal place to attack. Similar lawsuits were filed by consumers and small wineries in other states with discriminatory regimes—New York,²¹¹ Texas,²¹² Florida,²¹³ Indiana,²¹⁴ North Carolina,²¹⁵ and Virginia.²¹⁶ The Wine Wholesalers intervened to try to protect their lucrative monopolistic position from competition.

The initial skirmishes in district court produced mixed but encouraging results—five consumer victories and only two losses. On appeal, the consumers prevailed in the 5th and 6th Circuits,²¹⁷ lost in the 2nd and 7th,²¹⁸ and fought to a draw in the 4th²¹⁹ and 11th.²²⁰ The Michigan and New York cases were consolidated and went to the Supreme Court.

²⁰⁸ See *id.* at 467.

²⁰⁹ A list of Michigan wineries can be found at <http://www.michiganwines.com/Wineries/wineries.html> (last visited Aug. 21, 2007).

²¹⁰ The number of retail licenses comes from the MICH. LIQUOR CONTROL COMM'N, ANNUAL FINANCIAL REPORT 2003 at 10, available at http://www.michigan.gov/documents/annual_report_2003_final_86520_7.pdf (last visited Aug. 21, 2007).

²¹¹ *Swedenburg v. Kelly*, 358 F.3d 223 (2d Cir. 2004).

²¹² *Dickerson v. Bailey*, 336 F.3d 388 (5th Cir. 2003).

²¹³ *Bainbridge v. Turner*, 311 F.3d 1104 (11th Cir. 2002).

²¹⁴ *Bridenbaugh v. Freeman-Wilson*, 227 F.3d 848 (7th Cir. 2000).

²¹⁵ *Beskind v. Easley*, 325 F.3d 506 (4th Cir. 2003).

²¹⁶ *Bolick v. Roberts*, 199 F. Supp. 2d 401 (E.D. Va. 2002).

²¹⁷ *Dickerson v. Bailey*, 336 F.3d 388 (5th Cir. 2003); *Heald v. Engler*, 342 F.3d 517 (6th Cir. 2003).

²¹⁸ *Swedenburg v. Kelly*, 358 F.3d 223 (2d Cir. 2004); *Bridenbaugh*, 227 F.3d 848 (7th Cir. 2000).

²¹⁹ *Beskind v. Easley*, 325 F.3d 506 (4th Cir. 2003) (holding North Carolina's Alcohol Beverage Control laws unconstitutional for discriminating against out-of-state wine manufacturers and sellers, but vacating the District Court's ruling of striking down the main provisions of the state's direct-shipment bans).

²²⁰ *Bainbridge v. Turner*, 311 F.3d 1104 (11th Cir. 2002) (reversing the District Court's finding that the ban on interstate shipments was constitutional, but remanding the case to give the state further opportunity to prove that the ban advanced an important state interest).

2. The plaintiffs' argument: discrimination violates the Commerce Clause

The plaintiffs' argument was simple: this was a case of discrimination. Michigan allowed its in-state wineries to sell directly to consumers without going through a wholesaler, and to ship those purchases to residences. However, it prohibited out-of-state wineries from engaging in these same commercial activities. Because this scheme discriminated against interstate commerce and gave economic advantages to local wineries, it was invalid under the Commerce Clause and could not be saved by the Twenty-First Amendment. Plaintiffs relied primarily on *Bacchus Imports v. Dias*,²²¹ and Justice Scalia's concurring opinion in *Healy v. Beer Institute*,²²² for the proposition that the dormant Commerce Clause applied with full force to state laws that discriminated against interstate commerce in wine.²²³

Plaintiffs advanced three related legal arguments as to why the wine shipment law met the constitutional definition of discrimination. First, Michigan gave in-state wineries easier and less costly access to the market. Out-of-state wineries had to sell their wine through separate wholesalers and retailers, both of which marked up the price before reselling the wine to consumers.²²⁴ State laws that raise the price of out-of-state goods in relation to in-state products are "paradigmatic examples" of discrimination against interstate commerce.²²⁵ Second, if an out-of-state winery could not find a wholesaler willing to distribute its wine—and there are 3,000 who cannot—it is totally excluded from the market. State laws that cause local goods to have a larger share of the market are also classic examples of discrimination against interstate commerce.²²⁶ Third, the law protected the economic interests of Michigan wholesalers by shielding them from competition.²²⁷ Protectionism is also a classic example of unconstitutional discrimination.²²⁸

²²¹ *Bacchus Imports v. Dias*, 468 U.S. 263, 275-76 (1983).

²²² *Healy v. Beer Institute*, 491 U.S. 324, 344 (1989).

²²³ See also Vijay Shanker, *supra* note 205, at 379 (direct shipment prohibitions violate Commerce Clause).

²²⁴ See James Molnar, *Under the Influence: Why Alcohol Direct Shipment Laws Are a Violation of the Commerce Clause*, 9 U. MIAMI BUS. L. REV. 169, 186 (2001) (quoting Wall Street Journal as calling this the most expensive distribution system for any package good).

²²⁵ *West Lynn Creamery, Inc. v. Healy*, 512 U.S. 186, 193 (1994).

²²⁶ *Exxon Corp. v. Maryland*, 437 U.S. 117, 126 n.16 (1978).

²²⁷ Plaintiffs introduced evidence that the wholesalers were the ones who drafted and proposed the ban on direct shipments, and engineered its passage. The wholesalers have considerable political clout. See Vijay Shanker, *supra* note 205, at 361-64 (wholesalers contribute substantial amounts of money to state legislative candidates; most state laws prohibiting small wineries from direct shipping were actually drafted by lobbyists for the wholesalers).

²²⁸ *City of Philadelphia v. New Jersey*, 437 U.S. 617, 624 (1978).

3. The States' argument

The argument advanced by the states was more complicated. They conceded that the wine distribution rules treated in-state and out-of-state wineries differently, to the disadvantage of nonresidents. They conceded that, if the product were shirts instead of wine, the prohibition against direct Internet sales would be unconstitutional. Nevertheless, they argued that there was no Commerce Clause violation in this case and, even if there had been, the Twenty-First Amendment trumped the Commerce Clause and gave them unlimited power to regulate or ban the importation of alcoholic beverages.

a. No discriminatory intent

Michigan argued that it did not enact the wine shipment rule with the intent to engage in economic protectionism, but rather with the intent to regulate an alcoholic beverage. The different treatment was the accidental by-product of the state's legitimate decision that everyone needed to be located in Michigan to be regulated effectively. Michigan's attorneys pointed to the line in *Bacchus* that liquor regulations enacted for "mere economic protectionism" were not entitled to the same deference as those enacted pursuant to the Twenty-First Amendment.²²⁹ They argued that *Bacchus* did not apply, because Michigan's statutes were not enacted with the intent to discriminate, but were an attempt to regulate under Twenty-First Amendment powers.

b. The Twenty-First Amendment trumps the Commerce Clause

Michigan's second argument was that the Twenty-First Amendment trumped the Commerce Clause under the authority of the *Young's Market* line of cases from the 1930s.²³⁰ The state characterized the current case law as inconsistent, pointing to the "broad authority" dicta in several non-Commerce Clause cases²³¹ for the argument that *Young's Market* was still good law. To the extent that *Bacchus* deviated from this principle, they argued, it was wrongly decided and should be abandoned.

In the alternative, Michigan argued that, even if the Twenty-First Amendment does not trump the Commerce Clause in all situations, it does so in this case, where the laws at issue relate directly to "importation." The Twenty-First Amendment speaks specifically to importation, singling it out

²²⁹ *Bacchus Imps. v. Dias*, 468 U.S. 263, 276 (1984).

²³⁰ See discussion *supra* Part II.D.1.

²³¹ See discussion *supra* Part II.D.3.

as an area of exclusive state regulation. Michigan characterized this as the “core concern” of the Amendment, arguing that at least laws specifically advancing this core concern are immune from strict Commerce Clause scrutiny.²³²

c. The ban is necessary to protect state interests

However, Michigan’s primary argument was that discrimination was justified because it was reasonably necessary to advance legitimate local purposes—keeping alcohol out of the hands of minors, raising revenue, and generally protecting public health and safety.

i. Youth Access

Michigan and other states asserted as their primary interest, that the restrictive distribution laws were needed to prevent youth access to alcohol. They argued that underage drinking is a serious problem, that minors have easy access to credit cards and the Internet, and that the anonymity of electronic purchasing and common carrier shipping would allow minors to avoid having to prove their age. Restrictive regulations were needed to prevent an epidemic of minors receiving wine shipments from out-of-state wineries over the Internet.

There were four problems with this argument.

First, most states allowed in-state retail wine sellers to take orders by mail, telephone, and Internet, and ship or deliver them within the state.²³³ There were over 7,500 wineries and retailers authorized to make home de-

²³² This argument was dubious from the beginning. The core concern of the Twenty-First Amendment is clearly empowering states to enforce local dry laws, not for wet states to regulate importation procedures. See *Dickerson v. Bailey*, 336 F.3d 388, 404 (5th Cir. 2003) (core concern of § 2 is “the promotion of temperance”); *Wine Indus. of Mich. v. Miller*, 609 F.2d 1167, 1170 (6th Cir. 1980) (only significant purpose of the Twenty-First Amendment was to permit “dry” states to enforce local prohibition); Duncan B. Douglass, *supra* note 109, at 1631-36 (review of legislative history of Twenty-First Amendment shows that it was meant to refer only to state dry laws); Vijay Shanker, *supra* note 205, at 375 (1999) (temperance is the core purpose of the Twenty-First Amendment). Nor does the Court engage in constitutional interpretation by taking a single word out of context. See *United States v. Balsys*, 524 U.S. 666, 673 (1998). It is the meaning of the whole of § 2 that matters, and in the overall context of the Amendment, the power to regulate importation is a means to an end, not an end in itself. The means chosen to advance a state’s legitimate interests are not immune from scrutiny and legitimate ends “may not be accompanied by discriminating against interstate commerce.” *City of Philadelphia*, 437 U.S. at 627. *Accord Chem. Waste Mgmt., Inc. v. Hunt*, 504 U.S. 334, 340-42 (1992).

²³³ MICH. COMP. LAWS § 436.1537; MICH. COMP. LAWS § 436.1111(7); MICH. ADMIN. CODE r. 436.1011(6)(b).

liveries in Michigan.²³⁴ If minors were ordering wine for home delivery, it would not matter if it came from in-state or out-of-state sources, since minors are not likely to be seeking only one particular label.²³⁵ It was going to be hard for states to justify the in-state/out-of-state distinction.

Second, the argument lacks evidentiary support. Available data show that minors consume mostly beer and hard liquor, and relatively little wine. They rarely buy any kind of alcohol by direct shipments, which take several days to arrive, because their purchases tend to be spontaneous and made for immediate consumption. They are far more likely to have someone over the age of 21 buy it for them or obtain it from a local retail outlet that does not check identification. Minors also can obtain alcohol easily at parties, from friends and family, and by stealing it.²³⁶ On-line ordering of small quantities of inexpensive wine—the types of purchases minors would be likely to make—is also more expensive than local purchases. The FTC estimates that “[m]inors would have to pay a hefty premium, from 33-83%, to purchase a bottle of wine costing less than \$20 online and have it delivered to them via 2nd Day Air.”²³⁷

Third, the evidence from those states that allow direct shipping did not confirm Michigan’s fears. The experience in those states showed no increase in youth access because of direct shipping of wine.²³⁸

Fourth, even assuming a few minors occasionally obtained a few bottles of wine by Internet from out-of-state wineries, Michigan’s total ban on all interstate shipments under all circumstances was overbroad. Michigan barred shipments that had been purchased face-to-face at a winery tasting room, after showing an I.D, as well as “anonymous” Internet purchases. It barred shipments to adults as well as minors. In other situations in which states want to shield minors from harmful products, such as pornography, the Court has been reluctant to burden legitimate adult access in order to prevent occasional youth access. It has generally required that states narrowly tailor their restrictions so that legal adult access is burdened in only the most limited ways.²³⁹ The kind of literature or beverages available to

²³⁴ MICH. LIQUOR CONTROL COMM’N, ANNUAL FINANCIAL REPORT 2003 at 10, available at http://www.michigan.gov/documents/annual_report_2003_final_86520_7.pdf (last visited Aug. 21, 2007).

²³⁵ See Susan Lorde Martin, *Wine Wars—Direct Shipment Of Wine: The Twenty-First Amendment, The Commerce Clause, And Consumers’ Rights*, 38 AM. BUS. L.J. 1, 7 (2000).

²³⁶ The studies are summarized in REDUCING UNDERAGE DRINKING: A COLLECTIVE RESPONSIBILITY 166-68, 175-76 (Richard J. Bonnie & Mary Ellen O’Connell eds., 2004), available at <http://www.nap.edu/books/0309089352/html> (last visited Aug. 21, 2007).

²³⁷ FTC Report, *supra* note 17, at 33.

²³⁸ *Id.* at 26-29.

²³⁹ See 44 Liquormart, Inc. v. Rhode Island, 517 U.S. 484, 507 (1996); Lorillard Tobacco Co. v. Reilly, 533 U.S. 525, 563 (2001); Reno v. ACLU, 521 U.S. 844, 875 (1997); Ashcroft v. Free Speech Coalition, 535 U.S. 234, 252 (2002).

adults cannot be limited to those that would be suitable for distribution to children.

ii. Loss of tax revenue

The second interest asserted by the states was tax collection. They argued that the ban on interstate direct shipments was necessary to ensure that taxes would be paid. The states believed that their own resident businesses (local wineries, retailers, and wholesalers) would pay taxes on sales, but that non-resident businesses would not. The argument was speculative, because it was being made by states that had not tried to collect taxes from out-of-state businesses on direct sales. It was also contradicted by the evidence from states that allowed direct shipping and required that taxes be paid. The latter reported no problems with tax evasion.²⁴⁰

iii. Enforcing the Dram Shop Act

Michigan also asserted that the direct shipment ban was necessary to enforce its dram shop act because it feared that out-of-state sellers would not be subject to suit. The argument is not really a legal one, since Michigan had long-arm statutes that would technically give its courts jurisdiction over any out-of-state person who committed an act resulting in a tort in the state.²⁴¹ Federal diversity jurisdiction would similarly give injured plaintiffs access to federal court.²⁴² Rather, the argument was more a worry that, as a practical matter, it would be more difficult and more expensive to sue and to collect a judgment from an out-of-state defendant.

iv. Maintaining an orderly market in the interest of public health

The states made a fourth argument that a ban on direct shipping from out-of-state wineries was necessary to maintain an orderly and regulated market because unregulated liquor traffic posed a danger to public health and safety. They argued that the people who sell potentially dangerous products need to be identified, investigated, regulated, and held accountable.

²⁴⁰ See *FTC Report*, *supra* note 17, at 38-40 (no reports of significant tax evasion by direct shippers).

²⁴¹ MICH. COMP. LAWS §§ 600.705, 715.

²⁴² 28 U.S.C. § 1332 (2004).

The problem with this argument is that the dangers of an unregulated traffic in liquor justify licensing and regulation, not a total ban on shipping, and certainly not a ban on interstate shipping only. It cannot be the case that only out-of-state wine is dangerous if sold directly to the public. The Supreme Court has consistently rejected the public safety argument as justification for *discriminating* against out-of-state businesses—e.g., excluding other states' harmful waste from landfills,²⁴³ keeping large out-of-state trucks off local highways,²⁴⁴ or excluding potentially unwholesome out-of-state food products.²⁴⁵ Although health and safety considerations are entitled to weigh in dormant Commerce Clause balancing, "if a state *discriminates* against out-of-state interests . . . such facial discrimination will be subject to a high level of judicial scrutiny even if it is directed toward a legitimate health and safety goal."²⁴⁶ A state may regulate a dangerous product, of course, but must do so evenhandedly. There is "no valid health and safety reason for limiting the amount of waste . . . from outside the State, but not the amount . . . from inside the State."²⁴⁷ If an out-of-state shipment deserves to be restricted, so does a similar in-state shipment.

4. Plaintiffs' rebuttal: Reasonable nondiscriminatory alternatives

In response to the states' argument that they needed to discriminate against out-of-state wine shippers in order to advance important state interests, plaintiffs relied on a series of Commerce Clause cases holding that discrimination is constitutionally authorized only if there are no reasonable non-discriminatory alternatives.²⁴⁸ The plaintiffs asserted that each of the states' interests could be advanced without totally banning interstate wine shipments.

Youth access can be minimized by adopting procedural safeguards such as age verification, labeling of boxes as containing alcohol, requiring adult signatures upon delivery, and conducting stings. The FTC had found that these methods were an effective alternative to a total ban.²⁴⁹ A delivery

²⁴³ *C & A Carbone, Inc. v. Town of Clarkstown*, 511 U.S. 383, 393 (1994); *Fort Gratiot Sanitary Landfill, Inc. v. Mich. Dep't of Natural Res.*, 504 U.S. 353 (1992); *City of Philadelphia v. New Jersey*, 437 U.S. 617, 624 (1978).

²⁴⁴ *Kassell v. Consol. Freightways Corp.*, 450 U.S. 662, 667 (1981); *Raymond Motor Transp., Inc. v. Rice*, 434 U.S. 429 (1978).

²⁴⁵ *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511, 522-23 (1935); *Dean Milk Co. v. Madison*, 340 U.S. 349, 353-54 (1951).

²⁴⁶ *GMC v. Tracy*, 519 U.S. 278, 307 n.15 (1997) (emphasis added).

²⁴⁷ *Fort Gratiot Sanitary Landfill, Inc.*, 504 U.S. at 367.

²⁴⁸ *Hughes v. Oklahoma*, 441 U.S. 332, 336-37 (1979); *New Energy Co. v. Limbach*, 486 U.S. 269, 278 (1988); *Chem. Waste Mgmt., Inc. v. Hunt*, 504 U.S. 334, 344 (1992); *C & A Carbone, Inc.*, 511 U.S. at 393; *Or. Waste Sys., Inc. v. Dep't of Envtl. Quality*, 511 U.S. 93, 101 (1994).

²⁴⁹ *FTC Report, supra* note 17, at 26-29.

driver for a common carrier can be trained to check IDs just as effectively as a liquor store employee. This alternative is in use in many states.²⁵⁰

Tax collection can be accomplished by adopting regulations requiring out-of-state suppliers to obtain permits and to collect and remit taxes. The FTC Report found that this alternative effectively protected tax revenues in a less restrictive manner than a direct ban on out-of-state shipments.²⁵¹ New Hampshire has used this alternative for several years²⁵² and reports that, not only has it not lost any tax revenue by allowing direct shipping, it has actually seen wine tax revenue increase—by \$121,635 in 2003—as former illegal shippers begin shipping legally.²⁵³

Dram shop acts and other private forms of accountability can be protected through long-arm jurisdiction statutes that give local courts jurisdiction over any out-of-state person who causes a tort arising from the illegal sale of alcohol.²⁵⁴ Federal diversity jurisdiction would give injured plaintiffs access to federal court.²⁵⁵

Public health and safety can be protected by holding out-of-state wineries to the same standards as local wineries. Shippers can be required to apply for a state license, submit financial documents, submit to a police background check, have liability insurance, post bonds, submit sales reports, and abide by state laws regulating sales and deliveries. And, states can police unsafe interstate sales in the same way they police unsafe local sales—through stings.²⁵⁶

5. The problem of enforcement

The argument over alternatives boiled down to a question of enforcement. Michigan argued that the nondiscriminatory alternative of licensing and regulation might look reasonable on paper, but would not work in reality because states lacked the ability to hold out-of-state wineries accountable. They can threaten to put a local winery out of business, but have little threat to hold over an out-of-state winery. They can make surprise inspections of local wineries, but not those located across the country. Out-of-state wineries would ignore state regulations with impunity, knowing there was little a state could do to punish them for transgressions. The amicus

²⁵⁰ See, e.g., N.H. REV. STAT. ANN. § 178:27(II) (2003); N.C. GEN. STAT. § 18B-1001.1(c) (2004); N.D. CENT. CODE § 5-01-16(5) (1987); S.C. CODE ANN. § 61-4-747(c)(2) (Law. Co-op. 2003); VA. CODE ANN. § 4.1-112.1(C) (Michie 2003); WYO. STAT. ANN. § 12-2-204(d)(iii-iv) (2003).

²⁵¹ *FTC Report*, *supra* note 17, at 38-39.

²⁵² See N.H. REV. STAT. § 178:14-a(II).

²⁵³ Gary Dennis, *Wine Online*, MANCHESTER UNION LEADER, Sept. 14, 2004, at F1 (quoting John Byrne, N.H. Liquor Commissioner).

²⁵⁴ E.g., MICH. COMP. LAWS §§ 600.705, 600.715.

²⁵⁵ 28 U.S.C. § 1332 (2004).

²⁵⁶ See *FTC Report*, *supra* note 17, at 35-36.

brief filed by 33 states went so far as to claim that “States have only two choices: restrict direct shipments by out-of-state wineries or leave this potentially dangerous product virtually unregulated as long as it is shipped directly to a consumer from out of state.”²⁵⁷ This lack of enforcement ability justified discrimination, the states argued.

The argument was problematic. When *Granholtm* was being argued, 26 states allowed some form of direct shipping and reported no enforcement, accountability, or compliance problems.²⁵⁸ Most required direct shippers to get a state license in order to sell in the state, which would be revoked if the winery misbehaved.²⁵⁹ This kind of deterrent threat works for in-state businesses and should work for out-of-state businesses as well. The cost of noncompliance—loss of a license and thousands of dollars in future sales—outweighs the immediate benefit of illegally shipping one case of wine, and it therefore should be sufficient to deter illegal commercial activity.²⁶⁰

There are also three indirect enforcement routes. First, states can ask the Tax and Trade Bureau (TTB) to proceed against a winery’s federal basic permit. Every winery must hold such a permit,²⁶¹ which can be revoked if a winery violates state laws.²⁶² Furthermore, the TTB has assured the states that it will act on any complaints.²⁶³ Second, states can use the Twenty-First Amendment Enforcement Act that gives jurisdiction to federal courts to order out-of-state wineries to comply with state laws.²⁶⁴ The National Alcohol Beverage Control Association has called this “an effective tool to use in preventing the illegal interstate flow of alcohol beverages.”²⁶⁵ Third, states can file complaints with the regulatory agency in the shipper’s home state. Shipments to minors may violate the laws of the state in which the shipment originates as well as the state in which it is received.²⁶⁶ Many states also require their own licensees to comply with the laws of other states,²⁶⁷ and provide for sanctions if such laws are violated.²⁶⁸ Some states

²⁵⁷ Brief of Ohio and 32 Other States as *Amici Curiae*, at 10.

²⁵⁸ See *FTC Report*, *supra* note 17, at 29-31.

²⁵⁹ *E.g.*, S.C. CODE ANN. § 61-4-747 (Law. Co-op. 2003); NEB. REV. STAT. §§ 53-124(11), 53-160, 53-194.03 (2004).

²⁶⁰ See Timothy F. Malloy, *Regulation, Compliance And the Firm*, 76 TEMP. L. REV. 451, 453-54 (2003).

²⁶¹ 27 U.S.C. § 203 (2006).

²⁶² 26 U.S.C. § 5271(e) (2006).

²⁶³ BATF Ruling 2000-1 (2000).

²⁶⁴ 27 U.S.C. § 122a (2004).

²⁶⁵ *FTC Report*, *supra* note 17, at 30.

²⁶⁶ See, *e.g.*, CAL. BUS. & PROF. CODE § 23661.2; COLO. REV. STAT. ANN. § 12-47-104(1); 235 ILL. COMP. STAT. 5/6-29(b); WASH. REV. CODE § 66.12.200.

²⁶⁷ *E.g.*, DEL. CODE ANN. tit. 4, § 104(a), (b) (“No sale of alcoholic liquor shall be made to a person in a state or a division of a state where such sale is prohibited by law.”; “No shipment of alcoholic liquor shall be made into a state or into a division of a state where such shipment is prohibited by law.”).

provide for reciprocal enforcement—if a local winery loses its privileges in another state, its home-state license may not be renewed.²⁶⁹

The states clinging to their protectionist regimes made no argument that there was anything unique about their circumstances that would make enforcement more difficult for them than for other states. They merely argued that each state was entitled to decide for itself how much risk to take. However, the argument ran contrary to the Supreme Court's previous holdings that the practical and economic difficulties in inspecting and holding accountable out-of-state businesses do not justify discrimination.²⁷⁰

6. The economic argument

The wine war is about commerce, which is an economic activity. I know nothing about economics, and cannot tell a monopoly from a cartel or a rent from a profit. Luckily, an amicus brief was filed in *Granholm* by three Nobel laureates in economics and the Chair of the Economics Department at George Mason University.²⁷¹ The brief summary of the economic argument that follows is taken primarily from that brief.

a. E-commerce generally

E-commerce generally has been a boon to consumers and small businesses. Retail e-commerce sales have been growing at a huge rate and in the second quarter of 2004 amounted to \$15.7 billion. Online retail sales are growing at ten times the rate of their “brick-and-mortar” counterparts. As of 2002, e-commerce among businesses had reached roughly \$1 trillion per year. E-commerce is available for virtually all products, whether expensive, cheap, new, used, plentiful, or rare. Online commerce has brought consumers wider availability of products and greater price competition. Consumers now have the ability to do nationwide comparison shopping for nearly everything they buy. E-commerce has proved essential to many

²⁶⁸ See N.H. REV. STAT. ANN. § 178:27(VIII) (“Upon notification by authorities in another state which imposes a reciprocal enforcement policy, a New Hampshire licensee proved to be making illegal direct shipments to consumers and licensees in said state shall be subject to action by the liquor commission. Such actions may include fines and suspension and revocation of New Hampshire liquor licenses.”).

²⁶⁹ E.g., ARIZ. REV. STAT. § 4-203.04(C); LA. REV. STAT. ANN. § 26:359(G).

²⁷⁰ *Dean Milk Co. v. Madison*, 340 U.S. 349, 354-55 (1950).

²⁷¹ Brief for George A. Akerlof et al. as amici curiae supporting petitioners, *Eldred v. Ashcroft*, 538 U.S. 916 (2003); as amici curiae supporting respondent, *Granholm v. Heald*, 544 U.S. 460 (2005).

small businesses, who have gained access to larger markets without having to pay fees to middlemen or setting up additional distribution channels.²⁷²

b. E-commerce in wine

In its recent report on state barriers to e-commerce in the wine industry, the Federal Trade Commission noted that “state bans on interstate direct shipping represent the single largest regulatory barrier to expanded e-commerce in wine.”²⁷³ The *Wall Street Journal* called the three-tier distribution system for wine the most expensive distribution system for any package good in the country.²⁷⁴

When the three-tier system was created in 1933, there were few wineries and many distributors, and it worked well. However, the wine industry has recently seen a remarkably high degree of new market entry by wineries and an increase in demand by consumers. At the same time, the number of distributors has fallen due to industry consolidation. The number of wholesalers has dropped from several thousand in the 1950s to a few hundred today. In some regions, the distributor market may be approaching near-monopolistic conditions.²⁷⁵ The limited number of distributors gives them increased bargaining power, which enables them to select only the most cost-efficient wines for distribution—primarily those produced in large quantities by the biggest wineries and wine consortiums. Thirty U.S. wine companies now supply over 90 percent of the wine sold at retail, and the top three firms account for 60 percent of volume.²⁷⁶

State regulatory interventions further impede competition at the wholesale level. Many states have enacted laws that grant wholesalers preferential contract rights, establish exclusive territorial arrangements between wholesalers and wineries, and deter price cutting.²⁷⁷ The FTC has been critical of some of these measures due to their anti-competitive effects.²⁷⁸

The leading (indeed, the only) empirical study of wine shipment bans was done in Virginia by Allan E. Wiseman and Jerry Ellig. They found that

²⁷² Brief for American Homeowners' Alliance et al. at 7-9 as amici curiae supporting respondents, *Granholt v. Heald*, 544 U.S. 460 (2005) (quoting various federal government sources).

²⁷³ *FTC Report*, *supra* note 17, at 3.

²⁷⁴ See James Molnar, *supra* note 224, at 186 (quoting WALL ST. J.).

²⁷⁵ *FTC Report*, *supra* note 17, at 6.

²⁷⁶ Gina M. Riekhof & Michael E. Sykuta, *Politics, Economics, and the Regulation of Direct Interstate Shipping in the Wine Industry*, CORI WORKING PAPER 03-04 at 7, available at http://papers.ssm.com/sol3/papers.cfm?abstract_id=481947 (last visited Aug. 21, 2007).

²⁷⁷ DOUGLAS GLEN WHITMAN, *STRANGE BREW: ALCOHOL AND GOVERNMENT MONOPOLY* 27-28 (2003).

²⁷⁸ *FTC Report*, *supra* note 17, at 6-7.

wine availability was higher online.²⁷⁹ Direct shipping restrictions do not reduce the aggregate supply of wine—there is more than enough wine available locally to get everyone as drunk as they wish. Rather, the shipping bans compress the range of choice. Inventory costs and the diseconomies of scale prevent wholesalers and retailers from offering anything close to the breadth of choice of wines and vintages actually for sale somewhere. Given the economic necessities, the distribution network generally limits choices to a small number of well-known brands. This market fails to serve the needs of consumers of high-end wines, who purchase wine for future rather than immediate consumption, and who view a broader selection as important. Direct shipment barriers force upon these consumers high opportunity costs in the form of lost income or foregone leisure time associated with travel to distant specialty wine stores or wineries. Opening those barriers increases competition, which will force current local market participants to increase selection and supply a greater variety of wines.

Wiseman and Ellig also found some price advantages for online purchases, at least of high-end wine bought by the case.²⁸⁰ However, because of the high cost of transportation, small quantities of low-end wine were cheaper if purchased locally. If trade barriers were eliminated, general economic theory suggests that increased competition should generally reduce prices.²⁸¹ Similarly, economic rents accruing to distributors because of their monopolistic position will be eroded, further reducing the price to consumers to some degree.²⁸² Actual price effects will vary because of transportation costs. When wine is purchased by a consumer over the Internet and shipped directly, the transportation costs are the same for a case of “Two-Buck Chuck”²⁸³ and a case of Screaming Eagle.²⁸⁴ On the other hand, when wine is purchased by a wholesaler and shipped through the three-tier system, transportation costs vary by the type of wine. Economies of scale mean that the distribution costs for high-volume low-end wine is less per case than for small lots of expensive high-end wine. Direct shipping is therefore more likely to benefit consumers of high-end wine, which is handled in small lots, than for consumers of low-end wine, which is more efficiently handled in large quantities.

No one can predict the consequences of deregulating the wine market—after all, many economists predicted consumer gains from airline deregulation, but whether or not the effect has actually been beneficial is de-

²⁷⁹ Wiseman & Ellig, *supra* note 195, at 20-22.

²⁸⁰ Wiseman & Ellig, *supra* note 195, at 22-28.

²⁸¹ *FTC Report*, *supra* note 17, at 16-17.

²⁸² *See id.* at 23.

²⁸³ Nickname of the popular Charles Shaw brand of wines, which are sold for less than \$4.00 per bottle in Trader Joe's supermarkets.

²⁸⁴ Among the most highly-rated and high-priced wines produced in the United States.

batable.²⁸⁵ Nevertheless, the economist amici reached three conclusions. *First*, the demise of state protection of the three-tiered system will generate greater diversity of distribution arrangements, greater product availability for consumers, and expanded market opportunities for wineries. *Second*, an expanding market is not a zero-sum game, so increased competition will not necessarily harm the wholesalers. The current three-tiered system might flourish if relieved of the expense of handling boutique wines and defending their turf from Internet competition. The broader availability of “boutique” wines would tend to sharpen consumer awareness and appreciation, redounding to the benefit of all segments of the wine industry. *Third*, in a freer market, “better” wines produced by more efficient wineries would tend to expand at the expense of “worse” wines whose market position is currently being propped up by advertising and artificial market control.²⁸⁶

Assuming, *arguendo*, that the mandatory three-tier system originally had a legitimate purpose—to reduce consumption and limit the influence of organized crime—even the best regulatory systems often outlive their usefulness and mutate into a means of protecting private rather than public interests.²⁸⁷ This is clearly the case with the mandatory three-tier system. It is held in place and defended by special interest groups.²⁸⁸ Riekhof and Sykuta have found that the economic interests of the wholesalers have played the most significant role in the enactment of direct shipment bans against nonresidents, and that the relative size of the native wine industry was significantly correlated to the adoption of laws allowing in-state direct shipping. Legislative considerations of the public interest have been conspicuously absent.²⁸⁹

The nondiscrimination principle serves as a safeguard against “naked” interest group transfers that serve no public purpose, but merely transfer wealth from unorganized constituencies such as consumers to highly organized interests such as liquor distributors.²⁹⁰ It also protects against interstate exploitation in which states seek to impose costs on (non-voting) outsiders,

²⁸⁵ *E.g.*, Michael E. Levine, *Is Regulation Necessary? California Air Transportation and National Regulatory Policy*, 74 *YALE L.J.* 1416 (1965).

²⁸⁶ Brief of George A. Akerlof et al., *supra* note 271, at 14-15 (citing Dale M. & Philip L. Martin, *Inside the Bottle: The Wine Business*, *CHOICES* 30, 33 (Fall 2002)).

²⁸⁷ *See id.* at 17-18 (citing Sam Peltzman, *Toward a More General Theory of Regulation*, 19 *J.L. & ECON.* 211 (1976); Richard A. Posner, *Theories of Economic Regulation*, 5 *BELL J. ECON.* 335 (1974); George Stigler, *The Theory of Economic Regulation*, 2 *BELL J. ECON.* 3 (1971)).

²⁸⁸ *See id.* at 18-19 (citing Bruce Yandle, *Bootleggers and Baptists: The Education of a Regulatory Economist*, *REGULATION* 12 (May/June 1983)).

²⁸⁹ *See id.* at 19-20 (citing Gina M. Riekhof & Michael E. Sykuta, *supra* note 271, at 4, 22, 26).

²⁹⁰ *See id.* at 22 (citing Cass Sunstein, *Naked Preferences and the Constitution*, 84 *COLUM. L. REV.* 1689 (1984)).

by regulating on an extra-territorial basis or exempting in-state interests from burdensome taxes and regulations.²⁹¹

7. The *Granholm* decision

On May 16, 2005, the Supreme Court announced its decision in *Granholm v. Heald*.²⁹² The Court ruled in favor of consumers and small wineries. It struck down Michigan's total ban on interstate direct shipping as discriminatory in intent, and it struck down New York's physical-presence rule²⁹³ as discriminatory in effect. The Court applied its traditional Commerce Clause jurisprudence. The Twenty-First Amendment did not override or even weaken the Commerce Clause, and did not authorize states to discriminate against nonresidents and protect local economic interests. The Court held that all of the states' asserted interests in banning interstate sales could be advanced through the nondiscriminatory alternative of even-handed licensing and regulatory laws. States could not constitutionally give their own wineries preferential access to the market.

Granholm dealt with only one issue in Commerce Clause jurisprudence: discrimination against interstate commerce.

We hold that the laws in both States discriminate against interstate commerce in violation of the Commerce Clause, Art. I, § 8, cl. 3, and that the discrimination is neither authorized nor permitted by the Twenty-First Amendment.²⁹⁴

The Court did not address other closely related issues, such as whether the mandatory wholesaler requirement is a local processing rule prohibited by *C & A Carbone, Inc. v. Town of Clarkstown, N.Y.*,²⁹⁵ or an invalid form of economic protectionism that violates *Philadelphia v. New Jersey*.²⁹⁶ Nor did it comment on other Commerce Clause issues outside the umbrella of discrimination, such as whether wine distribution laws improperly regulate

²⁹¹ See *id.* at 22 (citing Saul Levmore, *Interstate Exploitation and Judicial Intervention*, 69 VA. L. REV. 563 (1983)).

²⁹² The decision was only 5-4, but the margin is not that slim. Two of the dissenting Justices are now gone from the Court (Rehnquist and O'Connor), and a third (Stevens, who is 86 years old) may retire soon as well.

²⁹³ In New York, the state argued that all wineries were being treated the same, because any winery that established a physical presence in the state could sell and ship wine directly to consumers. Brief for State of N.Y. at 37-40, 2004 WL 2190371.

²⁹⁴ *Granholm v. Heald*, 544 U.S. 460, 466 (2005).

²⁹⁵ *C & A Carbone, Inc. v. Town of Clarkstown, N.Y.*, 511 U.S. 383 (1994).

²⁹⁶ *Philadelphia v. New Jersey*, 437 U.S. 617, 624 (1978). See also *Bacchus Imps. v. Dias*, 468 U.S. 263, 276 (1984).

commercial transactions occurring outside the state²⁹⁷ or impose significant burdens on interstate commerce that exceed local benefits under the *Pike v. Bruce Church* balancing test.²⁹⁸

The decision strongly favored consumers, small wineries, and the free market. The Court held that states cannot disadvantage out-of-state wineries by denying them a reasonable means of access to the consumer market equivalent to the market access enjoyed by local wineries. It is a violation of the Commerce Clause “to allow in-state wineries to sell wine directly to consumers in that State but to prohibit out-of-state wineries from doing so,”²⁹⁹ or to “to allow local wineries to make direct sales to consumers in New York on terms not available to out-of-state wineries.”³⁰⁰ The Court said that the “mere fact of nonresidence should not foreclose a producer in one State from access to markets in other States,” even if the product is an alcoholic beverage.³⁰¹ It is a violation of the Commerce Clause for a state “to grant in-state wineries a competitive advantage over wineries located beyond the State’s borders”³⁰² or to give “in-state wineries access to the State’s consumers on preferential terms.”³⁰³

The Court was unimpressed by the states’ asserted need to ban or heavily regulate interstate wine sales in order to prevent youth access, collect taxes, and maintain an orderly market. Although these are legitimate state interests, the Twenty-First Amendment “does not allow States to ban, or severely limit, the direct shipment of out-of-state wine while simultaneously authorizing direct shipment by in-state producers.”³⁰⁴ Discrimination against interstate commerce “is neither authorized nor permitted by the Twenty-First Amendment,”³⁰⁵ which “does not allow States to regulate the direct shipment of wine on terms that discriminate in favor of in-state producers.”³⁰⁶ Nor may states prohibit direct sales by out-of-state wineries or make them “impractical from an economic standpoint.”³⁰⁷ Nor was any

²⁹⁷ See *Healy v. Beer Institute*, 491 U.S. 324, 336 (1989); *Brown-Forman Distillers Corp. v. N.Y. State Liquor Auth.*, 476 U.S. 573, 578-79 (1986).

²⁹⁸ *Pike v. Bruce Church*, 397 U.S. 137 (1970).

²⁹⁹ *Granholt*, 544 U.S. at 465-66.

³⁰⁰ *Id.* at 470.

³⁰¹ *Id.* at 472.

³⁰² *Id.* at 466.

³⁰³ *Id.* at 474.

³⁰⁴ *Id.* at 493.

³⁰⁵ *Granholt*, 544 U.S. at 466.

³⁰⁶ *Id.* at 476.

³⁰⁷ *Id.* at 466. The Court viewed discrimination as a question of economic effect. It described the Michigan regime as requiring “all out-of-state wine, but not all in-state wine, to pass through an in-state wholesaler and retailer before reaching consumers. These two extra layers of overhead increase the cost of out-of-state wines to Michigan consumers. The cost differential, and in some cases the inability to secure a wholesaler for small shipments, can effectively bar small wineries from the Michigan market.” *Id.* at 474. It described New York’s requirement that out-of-state wineries establish a distribution operation in New York as “additional steps that drive up the cost of their wine. . . . For most wineries, the

particular power over interstate commerce found in the Webb-Kenyon Act.³⁰⁸

This ruling was solidly connected to the Court's general Commerce Clause jurisprudence, with no suggestion that the Twenty-First Amendment changed this in any way.³⁰⁹ Like other laws, a state liquor law that discriminates against interstate commerce will be valid only if the state can prove, "based on concrete evidence,"³¹⁰ that it advances "a legitimate local purpose that cannot be adequately served by reasonable nondiscriminatory alternatives."³¹¹ There is no presumption of validity because the state is regulating an alcoholic beverage that poses a risk to minors.

Even were we to credit the States' largely unsupported claim that direct shipping of wine increases the risk of underage drinking, this would not justify regulations limiting only out-of-state direct shipments.³¹²

There is no presumption of validity because of the state's interest in tax collection and other legitimate interests.

Increased direct shipping, whether originating in state or out of state, brings with it the potential for tax evasion. . . . If licensing and self-reporting provide adequate safeguards for wine distributed through the three-tier system, there is no reason to believe they will not suffice for direct shipments. . . . The States have not shown that tax evasion from out-of-state wineries poses such a unique threat that it justifies their discriminatory regimes. . . . Michigan and New York offer a handful of other rationales, such as facilitating orderly market conditions, protecting public health and safety, and ensuring regulatory accountability. These objectives can also be achieved through the alternative of an evenhanded licensing requirement. . . . [I]mprovements in technology have eased the burden of monitoring out-of-state wineries. Background checks can be done electronically. Financial records and sales data can be mailed, faxed, or submitted via e-mail.³¹³

expense of establishing a brick-and-mortar distribution operation in one State, let alone all fifty, is prohibitive." *Id.* at 474-75.

³⁰⁸ *Id.* at 483. ("The Wilson Act reaffirmed, and the Webb-Kenyon Act did not displace, the Court's line of Commerce Clause cases striking down state laws that discriminated against liquor produced out of state.").

³⁰⁹ *See id.* at 472. ("Time and again this Court has held that, in all but the narrowest circumstances, state laws violate the Commerce Clause if they mandate 'differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter.'"); *id.* at 473 ("Allowing States to discriminate against out-of-state wine 'invite[s] a multiplication of preferential trade areas destructive of the very purpose of the Commerce Clause.'"); *id.* at 476 ("State laws that discriminate against interstate commerce face 'a virtually *per se* rule of invalidity.'"); *id.* at 475 ("New York's in-state presence requirement runs contrary to our admonition that States cannot require an out-of-state firm to become a resident in order to compete on equal terms.").

³¹⁰ *Granolm*, 544 U.S. at 493.

³¹¹ *Id.* at 489.

³¹² *Id.* at 490.

³¹³ *Id.* at 491-92.

The Court acknowledged that even-handed regulatory systems requiring wine to be distributed through state-run outlets or a privatized three-tier system were, in theory, legitimate exercises of state authority under the Twenty-First Amendment.³¹⁴ However, such a system must work in practice—giving out-of-state wineries reasonable and realistic access to the state market. If the state prohibits wineries from distributing their wine directly to consumers, it must provide an alternative method that actually distributes the wine, rather than one that prevents distribution.³¹⁵

Finally, the Court inserted dictum on a matter not briefed or argued: reciprocity laws that allow direct shipping only from states that grant reciprocal direct shipping privileges.

States should not be compelled to negotiate with each other regarding favored or disfavored status for their own citizens. . . . Rivalries among the States are thus kept to a minimum, and a proliferation of trade zones is prevented. . . . The perceived necessity for reciprocal sale privileges risks generating the trade rivalries and animosities, the alliances and exclusivity, that the Constitution and, in particular, the Commerce Clause were designed to avoid. State laws that protect local wineries have led to the enactment of statutes under which some States condition the right of out-of-state wineries to make direct wine sales to in-state consumers on a reciprocal right in the shipping State. . . . The current patchwork of laws—with some States banning direct shipments altogether, others doing so only for out-of-state wines, and still others requiring reciprocity—is essentially the product of an ongoing, low-level trade war. Allowing States to discriminate against out-of-state wine “invite [s] a multiplication of preferential trade areas destructive of the very purpose of the Commerce Clause.”³¹⁶

IV. WHAT NEXT?

A. *Does It Matter How States Level The Playing Field?*

States have had a variety of legislative reactions to *Granholm*'s command to create a level economic playing field that does not discriminate against nonresident wineries. Some have leveled up, extending direct sales and shipping privileges to out-of-state wineries and opening their markets to competition from nonresidents. Others have leveled down, extending the ban on shipping to local wineries and closing the direct sales market to everyone. Still others have leveled sideways, opening the door to some interstate shipments upon terms that appear facially nondiscriminatory, but which, as a practical matter, will still give preferential market access to local wineries. Although there are many small variations, the three patterns are:

First: Anyone may ship wine with a direct shipping permit (leveling up). Any winery may take Internet orders and ship them by common car-

³¹⁴ See *id.* at 465-66, 488-89.

³¹⁵ See *id.* at 473-74.

³¹⁶ *Granholm*, 544 U.S. at 473.

rier to consumers if it gets a state permit. The permit generally requires that the shipper verify age, remit taxes, label boxes as containing alcohol and requiring an adult signature, and file periodic reports with the state regulatory agency.³¹⁷ These laws appear constitutional unless the regulations attached to the permit are so burdensome that they have the practical effect of excluding many small wineries from the market. For example:

- a. *Permit cost.* In North Carolina, a direct shipper permit is free.³¹⁸ But in Nebraska, it is \$500.³¹⁹ Where the fee is high, it will exclude from the market small nonresident wineries with only limited sales in the state. Although the Supreme Court has said that a state can constitutionally pass on the legitimate costs associated with licensing and inspections,³²⁰ the state probably cannot make the process so burdensome and expensive that it has the practical effect of excluding nonresident wineries.
- b. *Case limits.* In Minnesota, a winery may ship no more than two cases of wine per year to any one customer.³²¹ In Indiana, a winery may ship no more than 3,000 cases per year to all customers.³²² Such limitations appear arbitrary and have the effect of limiting the nonresident wineries' market access. The quantity restrictions give limited, rather than full, access to the market and preserve most of the wholesalers' monopolistic position as the only distribution route for most major wine brands. The statutes therefore seem to violate the rule against "mere economic protectionism"³²³ and must be justified as necessary to promote an important state interest that cannot be advanced by nondiscriminatory means. It is difficult to imagine what legitimate interest the states will assert in creating case limits.
- c. *Production limits.* Kentucky will issue small winery shipping permits only to wineries with annual production of 50,000 gallons or less,³²⁴ though all Kentucky wineries produce less than 50,000

³¹⁷ E.g., N.H. REV. STAT. ANN. § 178:14-a (2006); CAL. BUS. & PROF. CODE § 23661.3 (2006).

³¹⁸ N.C. GEN. STAT. § 18B-902(d) (2006).

³¹⁹ NEB. REV. STAT. § 53-124 (12) (2006).

³²⁰ Dean Milk Co. v. Madison, 340 U.S. 349, 354-55 (1951).

³²¹ MINN. STAT. ANN. § 340A.417(a) (2006).

³²² IND. CODE § 7.1-3-26-12 (2006).

³²³ Bacchus Imps. v. Dias, 468 U.S. 263, 296 (1984); City of Philadelphia v. New Jersey, 437 U.S. 617, 624 (1978).

³²⁴ KY. REV. STAT. ANN. § 243.155(1)(b) (2006).

gallons per year.³²⁵ Maryland will issue winery permits with direct sales privileges only to wineries with an annual production limit of 27,500 gallons—which happens to be the annual production figure of the largest in-state winery that sells direct and does not use a wholesaler.³²⁶ By contrast, Indiana sets permit eligibility at a whopping 500,000 gallons a year³²⁷—the annual production level of its largest winery. As with case limits, these annual production limits are protective of local wineries. It is hard to fathom a legitimate state interest in them.

Second: No one may ship wine (leveling down). Some states have simply closed the electronic market. No wine may be bought over the Internet and shipped. If a consumer wants to buy wine, the consumer must hitch up the wagon, drive to the winery, and purchase it on site.³²⁸ Although even-handed on their face, these laws discriminate against nonresident wineries and exclude them from state markets “in practical effect” because no one can actually afford to drive 2,700 miles from Maine to California to pick up a few bottles of Latham Zinfandel. Some states compound this problem by limiting the quantity of wine that an individual may personally bring back into the state,³²⁹ which rules out even a once-a-year wine buying trip to stock a wine cellar that might be economically feasible. The attempt to level down still leaves local wineries with preferential access to the market—even if it is not as preferential as it used to be.

One aspect of leveling down deserves special attention. If a state eliminates the ability of its own wineries to ship wine directly and limits all wineries alike to face-to-face sales, it gives them a superficially appealing argument that this is a nondiscriminatory rule designed to assure that all purchasers must show identification in order to prevent youth access. However, the argument fails to stand up to scrutiny. The face-to-face requirement as a practical matter excludes distant out-of-state wineries from the market, but it still meets the Supreme Court’s definition of discrimination. That means the state must prove that there is no reasonable alternative to closing the market—i.e., that adopting procedural safeguards such as electronic age verification,³³⁰ labeling of boxes as containing alcohol, re-

³²⁵ Chris Smigell et al., *Kentucky Wine Purchasing and Production Survey*, UNIV. OF KENTUCKY HORTICULTURE DEPT., available at <http://www.uky.edu/Ag/NewCrops/winecontent04.pdf> (last visited Aug. 21, 2007).

³²⁶ MD. CODE ANN., art. 2B, § 2-101 (2006).

³²⁷ IND. CODE § 7.1-3-12-4.

³²⁸ E.g., KY. REV. STAT. ANN. § 243.155 (2006); ME. REV. STAT. ANN., tit. 28-A, § 1355(3) (2006).

³²⁹ See IND. CODE § 7.1-5-11-15 (2006) (2 case limit per trip); N.J. STAT. ANN. § 33:1-2(a) (no personal transportation at all, except from reciprocal states).

³³⁰ See, e.g., http://www.choicepoint.com/business/financial/ageverif_fs.html (last visited Aug. 21, 2007).

quiring adult signatures upon delivery, and training drivers in proper age verification, would not be an effective way to limit youth access.³³¹ The argument would also run into the problem that the Court requires states, in exercising their power to limit youth access to harmful materials, to tailor their restrictions narrowly, so legal adult access is not overly burdened.³³²

Third: Anyone may ship wine that was purchased face-to-face (leveling sideways). An emerging trend is to permit direct shipping, but only if the consumer purchases the wine in a face-to-face transaction on the winery's premises.³³³ This scheme benefits a few citizens who happen to vacation in Napa Valley and prefer to ship wine home rather than carry it back themselves. However, it does nothing for the average consumer who cannot afford the time and money to drive 2,000 miles to California in the first place. It also completely fails to address the commerce issue, because it does not increase access to the local market for out-of-state wineries. Once local residents have traveled all the way to the out-of-state winery, they could buy the wine and carry it home even without this new law. Giving the customer the option to ship it rather than carry it back does not open market access to any new wine or winery.

B. *Reciprocity Laws*

Before *Granholm*, 13 states had reciprocity laws.³³⁴ These laws typically provide that an out-of-state winery may ship directly to consumers only if the winery is located in a state that affords reciprocal direct-shipping privileges. The Supreme Court in *Granholm* said in dictum that these laws were "generating . . . trade rivalries" and creating "an ongoing, low-level trade war . . . destructive of the very purpose of the Commerce Clause."³³⁵ In light of this dictum, reciprocity laws cannot survive. Indeed, California changed its reciprocal law to a direct-shipping permit law immediately following the *Granholm* decision.³³⁶

³³¹ *FTC Report, supra* note 17, at 29, 34 (recommending this alternative).

³³² *E.g.*, 44 *Liquormart, Inc. v. Rhode Island*, 517 U.S. 484, 507 (1996); *Lorillard Tobacco Co. v. Reilly*, 533 U.S. 525, 563 (2001); *Reno v. ACLU*, 521 U.S. 844, 875 (2002); *Ashcroft v. Free Speech Coalition*, 535 U.S. 234, 252 (2002).

³³³ *E.g.*, KY. REV. STAT. ANN. § 243.155 (2006); MISS. CODE ANN. § 67-5-11 (2006).

³³⁴ California, Colorado, Hawaii, Idaho, Illinois, Iowa, Minnesota, Missouri, New Mexico, Oregon, Washington, West Virginia, and Wisconsin.

³³⁵ *Granholm v. Heald*, 544 U.S. 460, 473 (2005).

³³⁶ CAL. BUS. & PROF. CODE § 23661.3 (2006).

C. *How Far Can Granholm Be Extended?*

1. The easy cases

Granholm held that, in the context of laws prohibiting out-of-state wineries from shipping directly to consumers, the usual Commerce Clause rules applied. States cannot discriminate by intent or in practical effect against out-of-state wineries and give local wineries preferential market access unless there is no nondiscriminatory alternative. The Court rejected the states' arguments that the ban was necessary to prevent youth access, preserve tax revenues, assure an orderly market for the protection of public health and safety, or because of the inability to force nonresidents to comply with state laws. The Court also rejected the argument that the Twenty-First Amendment gave state liquor laws affecting interstate commerce any added presumption of validity or that alcohol regulations were exempt in any way from the rule against discriminatory regulations. The implication is that the Court will apply the same dormant Commerce Clause principles to state regulation of liquor that it applies to state regulation of other dangerous products, such as toxic waste. The Court does not say this explicitly, so the question is, how far is the Court likely to extend this principle?

The easier issues are those that merely vary the context in which state laws discriminate. For example, the result should be the same if one simply varies the kind of license held by the shipper. If a state cannot discriminate against out-of-state *wineries* by allowing only in-state wineries to ship directly, then it is hard to see how it can discriminate against out-of-state wine *retailers* by allowing only in-state retailers to ship directly to customers.³³⁷ Similarly, if one merely varies the type of potential customer who wants to receive the shipment, the result should be the same. If a state cannot discriminate against out-of-state wineries by allowing only in-state wineries to sell directly to *consumers*, then it is hard to see how it can discriminate against out-of-state wineries by allowing only in-state retailers to ship directly to *restaurants* or *wine retailers*.³³⁸

³³⁷ Several lawsuits have been filed raising this issue. *E.g.*, *Siesta Vill. Mkt., LLC v. Perry*, No. 3:06CV0585, 2006 WL 1880524 (N.D. Tex. July 7, 2006); *Coulombe v. Jolly*, 447 F. Supp. 2d 1117 (C.D. Cal. 2006). However, there is one difference between retailers and wineries—retailers do not hold a federal permit like wineries do, so one avenue of enforcement is not available to the states. *See* § III, B. 4, *supra*.

³³⁸ Lawsuits have been filed in several states raising this issue. *E.g.*, *Baude v. Heath*, No. 1:05CV0735, 2005 WL 4889256 (S.D. Ind. Sept. 23, 2005); *Beau v. Moore*, No. 4:05CV0903, 2005 WL 2807186 (E.D. Ark. Oct. 26, 2005).

2. The intermediate cases

Somewhat less certain is the fate of variants of the New York law struck down in *Granholm*. New York's physical presence rule discriminated as a matter of practical effect³³⁹ because it would be prohibitively expensive for an out-of-state winery to comply with it. If requiring a non-resident winery to establish a physical presence in order to have access to the state market constituted "discrimination" because it was so burdensome that its practical effect was to close the market to nonresidents, then other kinds of burdens may have the same discriminatory effect. There are two problems inherent in extending this principle. First, these are fact-sensitive issues that may depend on proof. Second, there may be many situations where the practical effect is not all-or-nothing. Several aspects of state shipping laws fall into this category.

- a. *Direct shipping permit fee.* In North Carolina, a direct-shipper permit is free³⁴⁰ and burdens no one. In Texas, the fee is \$75.³⁴¹ This, too, seems to burden no one. But a permit to ship to Nebraska costs \$500.³⁴² If a winery wants to sell directly to consumers and restaurants in Indiana, the permits will cost \$700.³⁴³ For in-state wineries, the bulk of whose business is sales in Indiana, the expense is justified. But what about out-of-state wineries? Some may do enough business in Indiana to justify the expense but others, who make only a few sales each year, do not. Many small wineries will continue to be excluded from the state.
- b. *On-site purchase rules.* In Kentucky, wine may be shipped only if the purchase was made on site in a face-to-face transaction.³⁴⁴ It is potentially expensive, both in terms of time and money, for a consumer to have to travel to a winery to buy wine. Consumers who live in Louisville will probably be willing to drive the 15 miles to the Huber Winery in Indiana, but probably will not be willing to travel 1,800 miles to buy wine in Oregon. Again, some wineries will continue to be excluded as a practical matter from the local market.

³³⁹ The "practical effect" test is part of the Supreme Court's standard definition of discrimination against interstate commerce. See *Associated Indus. of Mo. v. Lohman*, 511 U.S. 641, 654 (1994).

³⁴⁰ N.C. GEN. STAT. § 18B-902(d) (2006).

³⁴¹ TEX. ALCO. BEV. CODE ANN. § 16.02 (1995).

³⁴² NEB. REV. STAT. § 53-124 (11) (1943).

³⁴³ The winery will need a \$500 farm winery permit, IND. CODE ANN. § 7.1-4-4.1-15 (2006), a \$100 direct shipper permit, IND. CODE ANN. § 7.1-3-26-8, and a \$100 small wine wholesaler permit, IND. CODE ANN. 7.1-4-4.1-13(c) (2006).

³⁴⁴ KY. REV. STAT. ANN. § 243.155 (2006).

- c. *Delivery in own vehicle rules.* The flip side of the on-site purchase rule is the rule in some states forbidding the use of common carriers and limiting sellers to deliveries using their own vehicles.³⁴⁵ The result is the same. It is just as expensive and inconvenient for a winery employee to drive to the consumer as for the consumer to drive to the winery. Huber Winery might send its truck 15 miles to Louisville to make deliveries, but no Oregon winery is going to drive 1,800 miles to deliver a case of Pinot Noir. Laws that require wineries to use their own vehicles and employees to deliver wine also make direct sales impossible as a practical matter to most out-of-state wineries, and the state market will remain closed to them.

3. The hard cases

The harder issues will involve the validity of state laws that severely level down and treat in-state and out-of-state wineries equally badly. The *Granholm* litigation was about practical discrimination—in-state wineries could sell wine directly to consumers without going through a wholesaler, and out-of-state wineries could not. But, what happens if a state cuts off the in-state wineries' ability to sell directly? Although only Maryland has gone so far as to forbid its own wineries from selling directly to *consumers* at their tasting rooms,³⁴⁶ a number of states have cut off their own wineries' abilities to sell directly to *restaurants and retailers*, requiring that everyone alike use wholesale distribution for this purpose.³⁴⁷ States passed these laws in anticipation of a future *Granholm*-like lawsuit charging them with discrimination against out-of-state wineries with respect to direct sales to retailers. By requiring in-state and out-of-state wineries alike to use wholesalers, discrimination has been eliminated and *Granholm* does not apply.

However, just because *Granholm* does not apply does not mean the Commerce Clause does not apply. It would be a mistake to read *Granholm* as saying that state alcohol regulations are immune from Commerce Clause scrutiny unless they discriminate. To the contrary, *Granholm* stands for the proposition that *all* traditional Commerce Clause principles apply to liquor just like other products. Therefore, if the Twenty-First Amendment does not authorize states to violate the Commerce Clause's antidiscrimination principle, then it also does not authorize states to violate other central principles of the Commerce Clause.

³⁴⁵ E.g., FLA. STAT. ANN. § 561.57(2) (2006).

³⁴⁶ MD. ANN. CODE, art. 2B, § 2-204 (2006).

³⁴⁷ E.g., in 2006, Mississippi amended its native winery law to prohibit direct sales by its own wineries to retail permittees. See 2006 MISS. S. B. 2454, amending MISS. CODE ANN. § 67-5-11 (2006).

Closing down the direct-sale market and requiring every winery to use a wholesaler violates several core Commerce Clause principles. First and foremost, it is an act of economic protection that serves little purpose except to line the wholesalers' pockets. Economic protectionism violates the Commerce Clause.³⁴⁸ Second, it creates a local processing rule that requires wine that could more efficiently³⁴⁹ be distributed directly from the out-of-state wineries to be distributed exclusively by in-state wholesalers. Local processing rules violate the Commerce Clause.³⁵⁰ Third, it imposes significant burdens on interstate commerce by raising costs and limiting market access, which exceed local benefits. The Supreme Court in *Granholm* rejected the states' claims that requiring wholesale distribution was necessary to prevent youth access, collect taxes, and maintain an orderly market. It is difficult to see any other local benefits to mandatory wholesale distribution the state could come up with. When the burdens outweigh the local benefits, such laws typically violate the Commerce Clause.³⁵¹

V. CONCLUSION

At the core of the *Granholm* litigation is the question of whether the three-tier distribution system for wine created in 1933 is *really* "unquestionably legitimate?" Despite the dicta in *Granholm* and other cases that say so, there is good reason to doubt the efficacy of such boilerplate language. The Court has not said the three-tier distribution system is unquestionably legitimate *for all purposes*, including preventing distribution of out-of-state wines. The evidence is overwhelming that requiring wineries to distribute through a wholesaler closes the market to most out-of-state wineries, serves no public interest, and economically benefits only the wholesalers. It is a classic protectionist, anti-competitive trade barrier to out-of-state products and a local processing rule. It violates almost every doctrine of the Court's dormant Commerce Clause jurisprudence, frustrates the intent of the Framers to create a single national economic union, and survives on the flimsy premise that the Twenty-First Amendment authorized states to regulate commerce in alcoholic beverages any way they see fit.

In *Granholm*, the Court said once again that the Twenty-First Amendment did not override the dormant Commerce Clause and did not give states broad regulatory authority over interstate commerce. States may

³⁴⁸ *Bacchus Imps. v. Dias*, 468 U.S. 263, 276 (1984).

³⁴⁹ *Wiseman & Ellig*, *supra* note 195, at 22-28. It is more efficient for the 90% of wineries that are small and sell wine in small quantities, not for the major producers.

³⁵⁰ *C & A Carbone, Inc. v. Town of Clarkstown*, 511 U.S. 383 (1994).

³⁵¹ *Brown-Forman Distillers Corp. v. N.Y. State Liquor Auth.*, 476 U.S. 573, 578-79 (1986).

not regulate wine distribution any way they see fit for any purpose. As the history of the Twenty-First Amendment shows, the Amendment was intended to give states power to regulate *local* production and sale within their borders, and to prohibit interstate commerce *in violation of local dry laws*. One cannot realistically argue that the Twenty-First Amendment gave wet states the power to erect trade barriers that prevent nonresidents from selling wine, to give preferential access to the market to local wine sellers, or to protect the economic interests of in-state wholesalers. That is what the three-tier system does, and *Granholm* suggests that its days may be numbered.