To: Justice Souter
From: Christopher Geidner
Date: November 14, 2004
Re: Bench Memo: *Granholm v. Heald* (No. 03-1116)
Michigan Beer & Wine Wholesalers v. Heald (No. 03-1120)
Swedenburg v. Kelly (No. 03-1274)

Issue:

The question in these cases is whether, under Section Two of the Twenty-first Amendment of the United States Constitution, it violates the "dormant" Commerce Clause for a state to prohibit the out-of-state direct shipment of alcoholic beverages while allowing in-state direct shipment.

Procedural Posture:

Granholm v. Heald and *Michigan Beer & Wine Wholesalers v. Heald* come to this Court on a writ of certiorari from a unanimous ruling in the United States Court of Appeals for the Sixth Circuit. *Heald v. Engler*, 342 F.3d 517 (6th Cir. 2003). *Swedenburg v. Kelly* comes to this Court on a writ of certiorari from a unanimous decision in the United States Court of Appeals for the Second Circuit. 358 F.3d 223 (2d Cir. 2004). Certiorari was granted by this Court in all three cases on May 24, 2004. 72 U.S.L.W. 3725 (2004).

Background:

Constitutional Background

On Dec. 6, 1933, the "noble experiment" of Prohibition ended as the Twenty-first Amendment to the United States Constitution became the law of the land. *See Swedenburg*, 358 F.3d at 227. Section Two of the amendment reads: "The transportation or importation into any State, Territory, or Possession of the United States for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited." U.S. CONST., amend. 21, sec. 2.

This provision, as has been consistently construed by this Court, grants "the States virtually complete control over whether to permit importation or sale of liquor and how to structure the liquor distribution system." *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 110 (1980); *see also State Board of Equalization v. Young's Market Co.*, 299 U.S. 59, 62 (1936) ("The words used [in the Twenty-first Amendment] are apt to confer upon the State the power to forbid all importations which do not comply with the conditions which it prescribes."). Justice Brandeis, writing for the Court in *Young's Market*, continued:

> The plaintiffs ask us to limit this broad command. They 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.

Id.

In the years intervening, however, the Court has struck down several state provisions as violative of the Constitution's "dormant" Commerce Clause, calling into question whether *Young's Market* remains good law as to a state's right to freely regulate importation of intoxicating liquors as it sees fit. *See Heald*, 342 F.3d at 522 ("The state relied on these cases [including *Young's Market*] in the district court, but we find that reliance disingenuous at best because, as early as the 1960s, the Supreme Court signaled a break with this line of reasoning."); *see also* Resp. Brief at 15–16, Granholm v. Heald (No. 03-1116). *But see also* Pet. Brief at 25, *Granholm* ("[T]he Court of Appeals [in so concluding] gave insufficient force to the 21st Amendment and undue prominence to the Commerce Clause . . . .")

The "break" referred to by the court in *Heald* most recently reared its head in *Healy v. Beer Institute*, 491 U.S. 324 (1989), and before that in *Brown-Forman Distillers Corp. v. New York State Liquor Authority*, 476 U.S. 573 (1986) and *Bacchus Imports v. Dias*, 468 U.S. 263 (1984). In these three cases, the Court struck down under the dormant Commerce Clause laws that "impos[ed] price restrictions exclusively upon those who sell beer not only in Connecticut but also in the surrounding States," *Healy*, 491 U.S. at 344 (Scalia, J., concurring); required the "price of liquor to wholesalers . . . [be] no higher than the lowest price at which such item of liquor will be sold by such [distiller] to any wholesaler anywhere in any other state of the United States," *Brown-Forman*, 476 U.S. at 576; and granted exemptions from the Hawaii liquor tax for two locally-produced liquors "to encourage development of the Hawaiian liquor industry," *Bacchus*, 468 U.S. at 265, respectively.

In these cases, the Court held:

> The question in this case is thus whether the principles underlying the Twenty-first Amendment are sufficiently implicated by the [state policy] to outweigh the Commerce Clause principles that would otherwise be offended. Or as we recently asked in a slightly different way, "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."

Id. at 275–76. In applying this test to strike down the Hawaii tax exemption, the Court noted that "the State does not seek to justify its tax on the ground that it was designed to promote temperance or to carry out any other purpose of the Twenty-first Amendment, but instead acknowledges that the purpose was 'to promote a local industry.'" *Id.* at 276 (quoting appellee-state's brief). The exemption, in other words, was not passed under the authority granted by the Twenty-first Amendment relating to "transportation or importation" of intoxicating liquors.

The *Brown-Forman* Court likewise concluded that "New York has attempted to regulate sales in other States of liquor that will be consumed in other States therefore dispos[ing] of the Twenty-first Amendment issue." 476 U.S. at 585. In the same vein, the *Healy* Court concluded that a state statute that "ha[s] the inherent practical extraterritorial effect of regulating liquor prices in other States" is an unconstitutional violation of the Commerce Clause. 491 U.S. at 343.

What these cases did not address, however, is the effect of this line of jurisprudence on state regulations directly affecting to the importation of intoxicating liquors.

Factual Background

The laws of Michigan and New York at issue in these consolidated cases raise this question. The laws constitute parts of broad regulatory schemes for controlling and ensuring the orderly importation, distribution, and consumption of alcoholic beverages in the respective states. *See* Pet. Brief at 3–11, *Granholm*; Resp. Brief at 1–8, Swedenburg v. Kelly (No. 03-1274). One of the provisions in each of these regulatory schemes provides that no winemaker is permitted to directly ship its products from out-of-state locations to consumers in the states. In Michigan, the law at issue is Sec. 203:

> [A] sale, delivery, or importation of alcoholic liquor . . . shall not be made in this state unless the sale, delivery, or importation is made by the commission, the commission's authorized agent or distributor, an authorized distribution agent approved by order of the commission, a person licensed by the commission, or by prior written order of the commission.

MICH. COMP. LAWS § 436.1203(1) (2004).

The New York statute similarly restricts out-of-state shipments:

> No alcoholic beverages shall be shipped into the state unless the same shall be consigned to a person duly licensed hereunder to traffic in alcoholic beverages. This prohibition shall apply to all shipments of alcoholic beverages into New York state and includes importation or distribution for commercial purposes, for personal use, or otherwise, and irrespective of whether such alcoholic beverages were purchased within or without the state . . . .

NY CLS AL BEV § 102(c) (2004).

Both states maintain three-tier delivery systems, which include separate regulations for manufacturers, wholesalers, and retailers. *See* Resp. Brief at 2, *Swedenburg*; Pet. Brief at 6, *Granholm*. In conjunction with this system, the Second Circuit noted that "all [alcohol sellers] must either utilize the three-tier system or obtain a physical presence from which the state can monitor and control the flow of alcohol." *Swedenburg*, 358 F.3d at 238. Concurrently, however, the Sixth Circuit concluded that it "cannot endorse [such] regulation . . . as a constitutionally benign product of the state's three-tier system and, thus, a proper exercise of [Michigan's Twenty-first Amendment] authority, despite the fact that such a system places a minor burden on interstate commerce." *Heald*, 342 F.3d at 524 (internal quotations omitted).

The plaintiff-appellants in the case arising from the Second Circuit "own family wineries in Virginia and California, respectively. Many of their customers are tourists from other states, who enjoy their wine and would like to obtain it when they return home." Pet. Brief at 2, *Swedenburg*. The respondents represent the State of New York in their official capacities. The Sixth Circuit case features plaintiff-appellees "Michigan wine consumers and journalist who, although stymied by Michigan's discriminatory laws, seek to purchase out-of-state wine by direct shipment," Resp. Brief at 6, *Granholm*, as well as an "out-of-state winer[y] that is excluded from the Michigan market." *Id.* at 5.

In addition to the State of Michigan defendants, the Michigan Beer and Wine Wholesalers Association, "a trade association of Michigan beer and wine wholesalers[,] intervened as a defendant in the district court." Pet. Brief at *ii*, Mich. Beer & Wine Wholesalers Ass'n v. Heald (No. 03-1120).

The Sixth Circuit, in *Heald*, concluded that "the regulations in question are discriminatory in their application to out-of-state wineries, in violation of the dormant Commerce Clause, and cannot be justified as advancing the traditional 'core concerns' of the Twenty-first Amendment." 342 F.3d at 520.

The Fourth and Eleventh Circuits have taken this view that the Twenty-first Amendment does not protect against dormant Commerce Clause challenges to state alcohol importation regulations that prohibit direct delivery from out-of-state liquor producers to in-state consumers. *See Beskind v. Easley*, 325 F.3d 506 (4th Cir. 2003); *Bainbridge v. Turner*, 311 F.3d 1104 (11th Cir. 2002). The Fifth Circuit reached a comparable decision in a similar case. *See Dickerson v. Bailey*, 336 F.3d 388 (5th Cir. 2003) (striking down the relevant provisions of the Texas Wine Marketing Assistance Program). The program in Texas was formed specifically to "assist the Texas wine industry in promoting and marketing Texas wines." TEX. ALCO. BEV. CODE § 110.002 (2004).

The Second Circuit, putting forward the contrary view—and one with which the Seventh Circuit is in agreement, *see Bridenbaugh v. Freeman-Wilson*, 227 F.3d 848 (7th Cir. 2000)—held in *Swedenburg* that the regulation was "properly within the scope of section 2 of the Twenty-first Amendment, such that it is exempted from the normal operation of the Commerce Clause, or more precisely, the dormant Commerce Clause." 358 F.3d at 227 (internal quotations omitted).

Analysis:

The *Young's Market* case and these present cases address the issue of importation of intoxicating liquors, and no case since *Young's Market*'s affirmation of that state right has called into question the validity of a direct exercise of Section Two authority. *See, e.g.*, Pet. Brief at 22, *Granholm* ("Subsequent decisions of this Court have recognized the continuing vitality of the 21st Amendment and the principle of *Young's Mkt.* that states have very broad powers to regulate alcohol."). The state of New York and Michigan's regulatory schemes should thus be upheld as valid exercises of the states' powers under the Twenty-first Amendment.

This is so in spite of a growing idea, prompted by Supreme Court dicta, that the Twenty-first Amendment, in all cases, merely requires a balancing of dormant Commerce Clause interests against those of the Twenty-first Amendment. *See e.g.*, Brief of Amici Curiae Members of the United States Congress in Support of Respondents at 10, Granholm v. Heald (No. 03-1116) ("The Twenty-first Amendment did not elevate the states' authority above the Commerce Clause or any other provision of the Constitution.") [hereinafter Congress Amici Brief]. The idea that the Twenty-first Amendment has any independent authority is even in question in these cases. *See, e.g.*, Pet. Brief at 32, *Swedenburg* (asserting that those in support of these state regulations must have "overlooked the fact that there would have been no Constitution to which to attach a 21st Amendment were it not for the presence of the Commerce Clause"). In order to see why this has happened—and why it is dicta that should be cut short in the cases before the

Court presently—these far branches of the Twenty-first Amendment-Commerce Clause tree must be traced back to their roots.

The *Healy* Court held—in accordance with *Brown-Forman*—that "the Twenty-first Amendment *does not immunize* state laws from invalidation under the Commerce Clause when those laws have the practical effect of regulating liquor sales in other States." 491 U.S. at 342 (emphasis added). Justice Scalia noted in his concurrence that facial discrimination against interstate commerce "*eliminates the immunity* afforded by the Twenty-first Amendment." *Id.* at 344 (Scalia, J., concurring in part) (emphasis added). This strong assertion is justified through a citation to *Bacchus*.

The *Brown-Forman* Court, on which the *Healy* majority relied, itself had relied on *Bacchus* for the holding that "[i]t is *well settled* that the Twenty-first Amendment did not entirely remove state regulation of alcohol from the reach of the Commerce Clause." 476 U.S. at 584. Thus, all six justices agreeing with the judgment in *Healy* relied on *Bacchus* for this idea that the Twenty-first Amendment does not immunize states from dormant Commerce Clause challenges. The *Bacchus* Court, in turn, relied on an earlier case in holding:

> It is *by now clear* that the Amendment did not *entirely* remove state regulation of alcoholic beverages from the ambit of the Commerce Clause. For example, in *Hostetter v. Idlewild Bon Voyage Liquor Corp.*, [377 U.S. 324, 331–32 (1964)], the Court stated:
>
> "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."
>
> We also there observed that "[b]oth the Twenty-first Amendment and the Commerce Clause are parts of the same Constitution [and] each must be considered in light of the other and in the context of the issues and interests at stake in any concrete case." [*Id.* at 332.]

Bacchus, 468 U.S. at 275 (emphasis added).

In 1964, the *Hostetter* Court first noted—although not in the part cited to by the *Bacchus* Court—that "[t]his Court made clear in the early years following adoption of the Twenty-first Amendment that by virtue of its provisions *a State is totally unconfined* by traditional Commerce Clause limitations when it restricts the importation of intoxicants destined for use, distribution, or consumption within its borders." 377 U.S. at 330 (emphasis added). It went on to note that "[t]his view of the scope of the Twenty-first Amendment with respect to a State's power to restrict, regulate, or prevent the traffic and distribution of intoxicants within its borders *has remained unquestioned*." *Id.* (emphasis added). Similar to its unfair characterization by the *Bacchus* Court, this "absurd oversimplification" language has been used freely—without condition—by those opposed to the New York and Michigan statutes. *See, e.g.*, Pet. Brief at 33–34, *Swedenburg*; Congress Amici Brief at 10.

In relation to "the passage of liquor through [New York's] territory, under the supervision of the United States Bureau of Customs acting under federal law, for delivery to consumers in foreign countries," *Hostetter*, 377 U.S. at 329, however, the Court made

the statement that it would be an "absurd oversimplification" to assert the Commerce Clause had been completely repealed as to liquor regulations, and then held:

> If the Commerce Clause had been pro tanto 'repealed,' then Congress would be left with no regulatory power over interstate or foreign commerce in intoxicating liquor. Such a conclusion would be patently bizarre and is demonstrably incorrect. In *Jameson & Co. v. Morgenthau*, [307 U.S. 171 (1939)], 'the Federal Alcohol Administration Act was attacked upon the ground that the Twenty-first Amendment to the Federal Constitution, U.S.C.A., gives to the States complete and exclusive control over commerce in intoxicating liquors, unlimited by the commerce clause, and hence that Congress has no longer authority to control the importation of these commodities into the United States.' The Court's response to this theory was a blunt one: 'We see no substance in this contention.' [*Id.* at 172–73]. *See also United States v. Frankfort Distilleries*, [324 U.S. 293 (1945) (Sherman Act)].

Hostetter, 377 U.S. at 332. This clarification of the scope of the "absurd simplification" statement is made clear by the Petitioners in *Granholm*. Pet. Brief at 26 ("Clearly *Hostetter* was not a repudiation of early cases such as *Ziffrin* and *Young's Market*.").

The cases cited by the *Hostetter* Court also are instructive. *Morgenthau* addressed federal power relating to importation of liquor from abroad, and much of its discussion of the Twenty-first Amendment is repeated above in *Hostetter*. In *Frankfort Distilleries*, addressing federal power in a case in which there was no conflict between state law and federal policy, the Court held:

> Granting *the state's full authority* to determine the conditions upon which liquor can come into its territory and what will be done with it after it gets there, it does not follow from that fact that the United States is wholly without power to regulate the conduct of those who engage in interstate trade outside the jurisdiction of the State of Colorado.

324 U.S. at 299 (emphasis added).

Thus, these two cases—*Morgenthau*, addressing federal power, and *Frankfort Distilleries*, addressing the power of a state to regulate liquor outside its borders—led the Court, in a case addressing federal power to act in relation to international matters, to issue its limited holding in *Hostetter*. These cases were clarifications of the *scope* of the amendment, not cases addressing the *application* of the amendment when implicated.

These humble notices of the scope of the Amendment then morphed in *Bacchus* to the idea that Twenty-first Amendment only necessitated a balancing of its interests against those of the Commerce Clause as to any state or federal regulation of liquor. The *Brown-Forman* Court quickly found this substantive change to the *application* of the Twenty-first Amendment to be "*well settled*," and the *Healy* Court appeared to think it beyond question that the Twenty-first Amendment merely necessitated a Commerce Clause balancing test.

Fortunately, this test presented in *Bacchus*, *Brown-Forman*, and *Healy* is dicta because the statutes could have been struck down on grounds available through the earlier line of cases. This is in fact supported by the Second Circuit's opinion in *Swedenburg*, in which the court noted that the *Bacchus*, *Brown-Forman*, and *Healy* cases

"'limited' the scope of section 2 only insofar as it related to a state's attempt to regulate the traffic of alcohol outside of its borders or in violation of other powers reserved to the federal government." 358 F.3d at 236.

In *Brown-Forman* and *Healy*, like in *Frankfort Distilleries*, the Court held that the regulations had the effect of regulating liquor outside the states' borders, and they were thus properly struck down as unconstitutional under the Commerce Clause because the regulations were outside the scope of power provided by the Twenty-first Amendment. *Bacchus* likewise did not create a controlling Twenty-first Amendment interpretation because the tax exemptions at issue did not represent an attempt to regulate the "transportation or importation" of intoxicating liquors. *See, e.g.*, Pet. Brief at 29, *Granholm* (distinguishing *Bacchus* from the instant case on these grounds). The respondents in the Michigan case reply that "the Hawaiian regime expressly imposed a tax on all liquors imported into Hawaii for use therein that it did not impose on locally produced liquors." Resp. Brief at 29, *Granholm*. To the contrary, the Hawaiian tax structure for importation of liquors was never altered; two specific in-state exemptions were created to encourage local industry. The dormant Commerce Clause, outside consideration of the Twenty-first Amendment, thus applies to these actions taken by the Hawaii legislature.

This interpretation of *Bacchus* would be relevant to cases like the Fifth Circuit's *Dickerson*, in which the program solely served to create an after-the-fact exemption to promote Texas wineries. It was not, thus, a part of an overall, broad regulatory scheme, such as those at play in Michigan and New York, and arguably could be struck down under *Bacchus*. The Second Circuit, in fact, explicitly distinguished the New York law at issue in *Swedenburg* from the Texas law at issue in *Dickerson*. *See Swedenburg*, 358 F.3d at 228, 228 n.3.

To the extent that those opposed to the Michigan and New York statutes attempt to argue that the *Bacchus* balancing test has previous Supreme Court pedigree, they fail. The Petitioner in *Swedenburg* says of *Morgenthau* that the case represented "an approach that balanced competing constitutional interests." Pet. Reply Brief, Swedenburg v. Kelly, No. 03-1274 (Oct. 27, 2004). All it offers for support, however, is *Morgenthau*'s holding, already discussed, that the Twenty-first Amendment does not give the states "complete and exclusive control over commerce in intoxicating liquors." *Id.* This is not a balancing of competing interests; it is an acknowledgement of the limited scope of the amendment.

For these reasons, this Court should continue to apply the test of *Hostetter*, that "a State is totally unconfined by traditional Commerce Clause limitations when it restricts the importation of intoxicants destined for use, distribution, or consumption within its borders." 377 U.S. at 330. This decision would comport with standards of stare decisis, as the necessary holdings of the three most recent cases can be upheld as good law even as the test they purport to advance is jettisoned as dicta.

This reading of these cases eliminates one of the common arguments of the parties opposed to the state regulations in these cases: reliance on Judge Easterbrook's statement that "the greater power to forbid imports does not imply a lesser power to allow imports on discriminatory terms." *Bridenbaugh*, 227 F.3d at 853; *see, e.g.*, Resp. Brief at 10, 22, *Granholm*. This statement is supported by a reference to *Brown-Forman*, which—as discussed—is correctly read as defining the scope of the Twenty-first Amendment by holding that the regulation at issue was outside its scope. Thus, Easterbrook's later

justification of this statement by asserting that "[c]ases such as *Brown-Forman* and *Bacchus* apply an unconstitutional-conditions approach to use of the § 2 power," *Bridenbaugh*, 227 F.3d at 853, is rendered inconsistent with the approach described in this memo urging that the *Bacchus*, *Brown-Forman*, and *Healy* line of cases should be limited to their necessary holdings.

Finally, under the narrow reading discussed in this memo, it also would not be necessary to overrule *Bacchus*, a possibility mentioned by both the Michigan-appellant and its states amicus brief. *See* Pet. Brief at 28, *Granholm* ("Michigan respectfully submits that *Bacchus* was wrongly decided insofar as the 21st Amendment is concerned."); Brief of Amici Curiae State of Ohio et al. in Support of Petitioners at 4, Granholm v. Heald (No. 03-1116) ("If *Bacchus* [actually limited state regulatory power under the Twenty-first Amendment], the amici States urges that it was wrongly decided and should be overruled.").

For these reasons, the judgment of the Sixth Circuit should be reversed by this Court in *Granholm v. Heald* and *Michigan Beer & Wine Wholesalers v. Heald* and the judgment of the Second Circuit should be affirmed in *Swedenburg v. Kelly* by applying the rule of this Court laid down since the passage of the Twenty-first Amendment through the Court's decision in *Hostetter*, as necessarily limited in scope since by *Bacchus*, *Brown-Forman*, and *Healy*.