No. 03-1274

In The
Supreme Court of the United States

JUANITA SWEDENBURG, *et al.*,

Petitioners,

v.

EDWARD D. KELLY, *et al.*,

Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Second Circuit

PETITIONERS' BRIEF ON THE MERITS

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QUESTION PRESENTED

Does a State's regulatory scheme that permits in-state wineries directly to ship alcohol to consumers but restricts the ability of out-of-state wineries to do so violate the dormant Commerce Clause in light of Sec. 2 of the 21st Amendment?

PARTIES TO THE PROCEEDINGS

Petitioners, who were plaintiffs/appellees below, are Juanita Swedenburg, in her own capacity, Juanita Swedenburg, as proprietor of Swedenburg Winery, a Virginia partnership; David Lucas, in his own capacity, David Lucas, as proprietor of The Lucas Winery, a California sole proprietorship; Patrick G. Fitzgerald, Cortes DeRussy, and Robin Brooks.[1]

State respondents, who were defendants/appellants below, are Edward D. Kelly, Chairman of the State Liquor Authority, Division of Alcoholic Beverage Control, State of New York, in his official capacities; Lawrence J. Gedda, Commissioner of the New York State Liquor Authority, Division of Alcoholic Beverage Control, State of New York, in his official capacities; Joseph Zarriello, Commissioner of the New York State Liquor Authority, Division of Alcoholic Beverage Control, State of New York, in his official capacities.

Private respondents, who were intervenor/defendants/appellants below, are Charmer Industries, Inc.; Premier Beverage Company LLC; Peerless Importers, Inc.; Local 2d Of The Allied Food and Commercial Works International Union; Eber Brothers Wine and Liquor Corp.; Metropolitan Package Store Association, Inc., a trade association of New York-licensed alcoholic beverage retailers.

[1] None of the petitioners are corporations, and have no parent companies or subsidiaries.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-33a)[2] is reported at 358 F.3d 223 (2d Cir. 2004). The opinion of the district court granting summary judgment to petitioners (Pet. App. 34a-71a) is reported at 232 F. Supp. 2d 135 (S.D.N.Y. 2002). The order of the district court entering judgment for the petitioners (Pet. App. 72a-73a) is not reported.

STATEMENT OF JURISDICTION

The judgment below was entered on February 12, 2003. (Pet. App. 1a). The jurisdiction of this Court is proper under 28 U.S.C. §1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS

This case implicates the Commerce Clause, U.S. Const., art. I, §8, cl. 3 (Pet. App. 74a); the 21st Amendment (Pet. App. 74a); and the Privileges and Immunities Clause, U.S. Const., art. IV, §2 (Pet. App. 74a). Statutes involved include the Wilson Act, 27 U.S.C. §121 (Pet. App. 75a); the Webb-Kenyon Act, 27 U.S.C. §122 (J.A. 25); the 21st Amendment Enforcement Act, 27 U.S.C. §122a (Pet. App. 76a); N.Y. Alco. Bev. Cont. Law §102(1)(c), and (d) (J.A. 18); §§3(12-a), 76(2), 76(4), 76(5), 76-a(6)(d) (Pet. App.

[2] References to the Appendix to the Petition for Writ of Certiorari are noted as "Pet. App." References to the Joint Appendix filed in this Court are noted as "J.A." References to the Joint Appendix filed in the Court below are noted as "2d Cir. J.A."

86a-90a, 93a), 77(4)(b)(4), 77(4)(f), 77(5) (J.A. 15), 99-b(1)(k), 105(9), and 130(1) (Pet. App. 95a-100a); and N.Y. C.L.S. Penal §10.00(4) (Pet. App. 101a).

STATEMENT OF THE CASE

A. Facts.

1. Petitioners Juanita Swedenburg and David Lucas 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 (J.A. 37-39; 2d Cir. J.A. 91-92, 3558-59). Among their customers are petitioners Patrick Fitzgerald, Cortes DeRussy, and Robin Brooks, all of whom live in New York.[3]

Mrs. Swedenburg is typical of the small winemakers who dominate the industry today. She opened her winery in the Virginia countryside in 1988. She is involved in all aspects of the winery's operations, from planting to harvesting to production to sales. Her total production is below 2,000 cases per year. Her award-winning wines cost between $10-$15 per bottle. Over 90 percent of her sales are to people who visit the winery, about half of whom reside outside Virginia. (J.A. 37).

Because they live in New York, the consumer petitioners cannot obtain wine from Swedenburg Winery or Lucas Winery, as a result of laws challenged in this litigation. New York, like most if not all states, uses a "three-tier"

[3] New York is the nation's second-largest wine market (2d Cir. J.A. 205).

system for distribution of most alcohol: producer to distributor to retailer to consumer. N.Y. Alco. Bev. Cont. Law (hereinafter ABC Law) §102(1)(c) (Pet. App. 81a) provides that "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." Accordingly, even if New York consumers travel to Virginia or California to visit the wineries, they cannot lawfully ship wine back to themselves. Unless the wine is carried by a New York liquor distributor, they cannot obtain the wine at all.

2. Prior to 1970, New York permitted some direct interstate shipments of wine for personal use (2d Cir. J.A. 364). *See People v. Ryan*, 8 N.E.2d 313, 315 (N.Y. 1937). But those exceptions were extinguished (2d Cir. J.A. 366) and the law was tightened to ensure that even wine for personal use would have to flow through liquor distributors (2d Cir. J.A. 387).[4] That "law was enacted . . . to prevent what was considered to be an unfair and unwise form of competition with New York state licensees, and to eliminate unfair tax advantages." *House of York v. Ring*, 322 F. Supp. 530, 533 (S.D.N.Y. 1970); *see also* (J.A. 46-48).

3. While state law requires all out-of-state wineries to sell their wines through the three-tier system or not at all, New York has made multiple exemptions to that rule available to in-state wineries. The exemptions were expressly passed to promote the New York wine industry (2d Cir. J.A. 293, 299-301; Pet. App. 54a-55a). For example, ABC Law §76-a(6)(d) (Pet. App. 94a) permits licensed

[4] Section 102(1)(c) provides an exception for wines obtained outside the United States.

farm wineries – i.e., wineries located in New York producing wine only from New York grapes – to ship their own or other "New York State labeled wines"[5] directly to New York consumers.[6] Section 105(9) allows licensed retailers to deliver alcoholic beverages in their own vehicles or vehicles hired from a trucking company registered with the liquor authority. Under §76(4), commercial wineries can obtain a retail sales license and sell any New York State labeled wine at retail for consumption off-premises. Wineries in New York can also conduct tastings of New York State labeled wines (§76(2)(a)), they can sell New York State labeled wines at dinner theaters (§76(4)) and at state fairs (§77(5), and they can utilize "wine by wire" services to make deliveries on behalf of "other wineries within the state" (§76(5)). Both wineries and retailers in New York also can deliver alcoholic beverages in their own vehicles or those hired from a trucking company registered with the liquor authority pursuant to §105(9).

Most of the approximately 190 New York wineries, all but one of which are small, rely heavily on direct shipping to New York consumers (J.A. 42-43). However, New York's ban on direct shipping limits interstate markets for New

[5] "New York State labeled wine" means wine made from grapes "at least seventy-five percent the volume of which were grown in New York State." ABC Law §3(20-a).

[6] Contrary to the liquor distributor respondents' repeated assertions, farm wineries do not have to use their own trucks, but instead may "[d]eliver or transport any New York State labeled wine manufactured or produced by the licensee or any other winery or farm winery . . . in any vehicle owned, leased, or hired by the licensee." ABC Law §76-a(6)(d). Farm wineries typically use United Parcel Service or similar carriers to deliver their wines to consumers (J.A. 44).

York wineries. About a dozen states (*see* map at 14) allow direct interstate wine shipments only from states that themselves allow such shipments. As a result, New York's law forecloses certain markets to the detriment of small New York wineries.

4. No license exists for out-of-state wineries to ship directly to New York consumers (J.A. 159). *See House of York*, 322 F. Supp. at 533. According to respondents, out-of-state wineries could technically ship directly to New York consumers by establishing a bricks-and-mortar business operation in New York, essentially becoming part of the three-tier system. Assuming this were possible, an out-of-state winery would have to open a New York commercial winery and a warehouse, obtain a retailer license, and ship through its own trucks or trucks licensed by the State Liquor Authority (J.A. 159-60; 2d Cir. J.A. 347, 359-60). The warehouse must be fully staffed, separate from other premises, and devoted solely to wine distribution, with stiff sanctions for violations (J.A. 149-151; 2d Cir. J.A. 347, 350-60). Establishing such full-scale business operations in another state is prohibitive for a small winery like Swedenburg or Lucas (J.A. 201; 2d Cir. J.A. 3560); and no winery has ever qualified to do so (J.A. 159). Moreover, an out-of-state winery still would not be able to avail itself of any of the sales and shipping opportunities listed above that are limited to wineries selling "New York State labeled wines."

In 1995, the New York Legislature overwhelmingly passed a bill to allow limited direct interstate shipment of wine to consumers (2d Cir. J.A. 444, 450-52); but under heavy pressure from the liquor distributors among others (2d Cir. J.A. 460, 477, 481-485, 496-500, 506-515, 522-534), the bill was vetoed by the governor (2d Cir. J.A. 442-43).

5. The effects of bans on direct interstate wine shipments are magnified by recent economic trends. In recent decades the liquor distributor industry has contracted. In 1999, the top 25 distributors accounted for 63.5 percent of all U.S. alcohol sales, and their share is growing (2d Cir. J.A.185-86, 279-86).[7]

At the same time, the number of American wineries has increased substantially, growing to more than 3000 in all 50 states (source: Tax and Trade Bureau). The vast majority are small family farms. In 1998, while the nation's top 25 wineries produced 215 million cases, or 82.7 percent of all wine, the remainder was produced by over 2400 wineries, most of which produced 5,000 cases or fewer (J.A. 187; 2d Cir. J.A. 184). As a result, distributors can make available on store shelves only a fraction of the tens of thousands of wines produced each year (J.A. 38-39, 186-187; 2d Cir. J.A. 3578), and have even less capacity to fully stock older vintages. Many wines that are unavailable on store shelves are available from the wineries, but New York consumers cannot obtain them due to the direct shipping ban (J.A. 187-189; 2d Cir. J.A. 3547-50, 3554-55, 3578-82, 3595).

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[7] As of 2004, their share reportedly has increased to 67.9 percent of the U.S. market, with sales of $21.7 billion. *See* "Top U.S. Wholesalers Keep Expanding as Big Changes Loom," *Impact*, April 15, 2004 at 1.

Although there are many distributors in the New York market, the industry is dominated by four giants – not coincidentally, the intervenor respondents here – each of which is among the top 25 national liquor distributors with combined sales of $2.74 billion nationally and $1.63 billion in New York. By contrast, the remaining New York liquor distributors average less than $1 million in annual sales (2d Cir. J.A. 185-86).

Other states have solved that conundrum by allowing wineries to ship across (and within) state boundaries directly to consumers. The number of states allowing direct shipping has increased markedly. When this lawsuit was filed in 1999, only 19 states permitted it and 31 prohibited it; while today 26 states allow it and 24 states forbid it (*see* map at 14). Accountability in states allowing direct shipping is ensured in multiple ways. States often require shipping permits, payment of taxes, and measures to protect against underage access (J.A. 46-47, 194-196). The Tax and Trade Bureau (TTB) (formerly Bureau of Alcohol, Tobacco and Firearms (BATF)) can revoke a winery's license if it violates state laws governing alcohol (BATF, Industry Circular No. 96-3, *Direct Shipment Sales of Alcohol Beverages* (February 11, 1997) (hereinafter BATF Industry Circular);[8] (J.A. 196-197; 2d Cir. J.A. 3581-82). Moreover, through the 21st Amendment Enforcement Act, 27 U.S.C. §122a, Congress authorized state attorneys general to enforce their liquor laws in their home-state federal courts against out-of-state wineries.

6. Direct shipment of wines has become the economic life-blood of thousands of small wineries, like Swedenburg and Lucas (J.A. 37-38, 44, 187-188; 2d Cir. J.A. 3546-50). The Internet has created the technological capacity for consumers to obtain any wine from any winery (J.A. 45-49). But in states like New York where direct interstate shipments are forbidden, wineries like Mrs. Swedenburg's must turn away orders from consumers, severely limiting the wineries' prospects for survival and constricting

[8] Available at http://www.atf.treas.gov/pub/ind_circulars/ic_96-3.htm.

consumer choices (J.A. 38-39, 190-191; 2d Cir. J.A. 93-94, 3546, 3552, 3557, 3574).

A 2003 staff report by the Federal Trade Commission found on the basis of extensive hearings that "state bans on interstate direct shipping represent the single-largest regulatory barrier to expanded e-commerce in wine." Fed. Trade Comm'n, *Possible Anticompetitive Barriers to E-Commerce: Wine* at 3, 14 (2003), at http://www.ftc.gov/os/2003/07/winereport2.pdf (hereinafter FTC Report). The report found that such bans reduce consumer choice and increase prices. *Id.* at 3, 16-25. It reported that the states that allow direct interstate shipments of wine have satisfied their legitimate regulatory objectives by constructing mechanisms to safeguard against underage access and, where desired, to collect tax revenues. *Id.* at 4, 26-39.

B. Procedural History.

1. Plaintiffs filed this lawsuit in 1999, challenging ABC Law §§102(1)(c) and (d) (Pet. App. 81a-82a), as applied to prohibit direct interstate wine shipments, as a violation of the Commerce Clause and the Privileges and Immunities Clause (U.S. Const. art. IV, §2).[9] After considering an extensive record and the parties' cross-motions for summary judgment, the district court found the ban unconstitutional under the Commerce Clause. Applying *Bacchus Imports v. Dias*, 468 U.S. 263 (1984), the court engaged in a two-part inquiry. First, the court concluded that under the Commerce Clause, the state's differential

[9] Plaintiffs also challenged the state's advertising ban under §102(1)(a) as a violation of the First Amendment. Both the district court and court of appeals invalidated that provision.

direct shipment rules, under which "out-of-state wineries must consign their products to a (three-tier) wholesaler, [while] in-state wineries do not" (Pet. App. 53a), triggered Commerce Clause scrutiny. "That the New York direct shipping ban on out-of-state wine burdens interstate commerce and is discriminatory (on its face) is clear from the wording (let alone the impact) of the exemptions favoring in-state wineries" (Pet. App. 53a). Not only does the system "provide an impermissible economic benefit and (protection) to only in-state interests," there exist "nondiscriminatory alternatives available to serve the state's interests" (Pet. App. 54a). The court found the effort and expense for an out-of-state winery to obtain a New York commercial winery license and establish business operations in the state to be "unreasonable" (Pet. App. 55a). As a result, the court concluded that the "ban on the direct shipment of out-of-state wine is *not* 'evenhanded' and constitutes a per se Commerce Clause violation" (Pet. App. 57a) (emphasis in original).

The court then turned to the State's 21st Amendment defenses, and found that "[t]he State has not established that its legitimate goals" of temperance and tax revenues "cannot be accomplished in a nondiscriminatory manner" (Pet. App. 64a). The court enjoined defendants from prohibiting out-of-state wineries from shipping wine to consumers on the same terms and conditions as New York wineries (Pet. App. 72a-73a).

2. The Second Circuit reversed. Though the court acknowledged that the district court had "rel[ied] on the method of analysis utilized by a number of the other federal courts in similar challenges" (Pet. App. 9a), it proceeded to use an analysis "that only one other circuit court has employed" (Pet. App. 13a). Specifically, the court

rejected a "two-tier" analysis in which the statute is assessed both under the Commerce Clause and 21st Amendment (Pet. App. 12a), instead considering "the scope of the Twenty-first Amendment's grant of authority to the states to determine whether the challenged statute is within the ambit of that authority, such that it is exempted from the effect of the dormant Commerce Clause" (Pet. App. 13a). The court found that "[a]ll wineries, whether in-state or out-of-state, are permitted to obtain a license as long as the winery establishes a physical presence in the state" (Pet. App. 25a). Although "fully recogniz[ing] that the physical presence requirement could create substantial dormant Commerce Clause problems if this licensing scheme regulated a commodity other than alcohol" (Pet. App. 26a), here the State's aim was to "ensure accountability" over alcohol distribution (Pet. App. 27a), and therefore was within the State's 21st Amendment powers.

3. This Court granted the petition for writ of *certiorari* limited to the question presented, and consolidated the case with a Michigan case raising the same question in Nos. 03-1116 and 03-1120.

SUMMARY OF THE ARGUMENT

It is common today to lament the vanishing of the family farm from American life. The tradition of the yeoman farmer, true to the soil, is a deeply imbedded image that exemplified basic American values from the founding era through the Depression.

Today, that tradition is kept alive in vineyards across America by stalwart family farmers like Juanita Swedenburg and David Lucas. It is to the protection of such small entrepreneurs against discriminatory trade barriers that the promise of the Commerce Clause was addressed. As Justice Jackson majestically declared in *H.P. Hood & Sons, Inc. v. DuMond*, 336 U.S. 525, 539 (1949),

> 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. . . . Such was the vision of the Founders; such has been the doctrine of this Court which has given it reality.

The Commerce Clause thus operates to prohibit a state from discriminating against the farmers and craftsmen of its sister states in favor of its own industries. This guarantee is well-established in 150 years of case law, *see West Lynn Creamery v. Healy*, 512 U.S. 186, 194 (1994), a doctrine that operates to protect both producers and consumers.

As the record abundantly demonstrates, the ban on direct interstate wine shipments here was not adopted for benign purposes. Regardless, the method itself is impermissible. Choosing two sets of rules for alcohol distribution – one for in-state producers and another far more onerous set for out-of-state producers – not only violates the cardinal Commerce Clause requirement of nondiscrimination, but also betrays the State's protectionist predilections.

Such a discriminatory scheme is permissible only if the 21st Amendment nullifies the Commerce Clause, so that the State need only invoke the 21st Amendment to shield a distribution regime even if it serves protectionist ends through blatantly discriminatory means. The Second Circuit did as much when it created an unprecedented 21st Amendment "exempt[ion]" (Pet. App. 13a) to the Commerce Clause, in stark contradiction to this Court's holding in *Bacchus Imports v. Dias*, 468 U.S. 263 (1984), and decades of other precedents. Those decisions command that both constitutional guarantees must be respected: specifically, that while the 21st Amendment provides states broad authority over the distribution of alcohol within their borders, it does not invest states with power to enact discriminatory legislation dressed in a facade of temperance. The protectionism manifest in this case cannot stand.

ARGUMENT

I. NEW YORK'S DISCRIMINATORY WINE SHIPMENT BAN CONSTITUTES A VIOLATION OF THE COMMERCE CLAUSE.

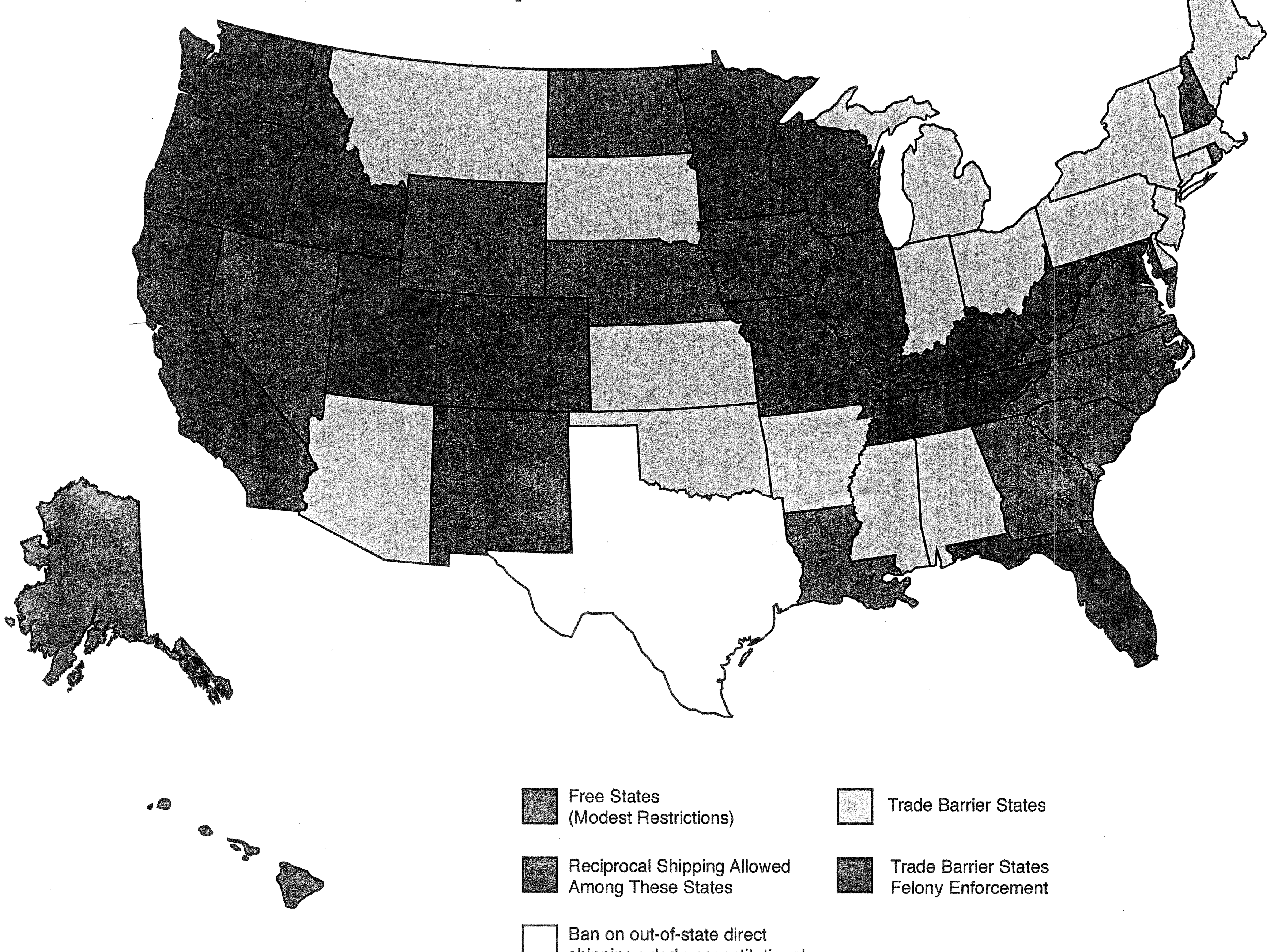
By expressly declining to engage in a "two-tier" constitutional analysis (Pet. App. 12a), the part of the Constitution that the court below jettisoned was the Commerce Clause and its requirement of nondiscrimination in state regulation of commercial intercourse. The court had to perform that surgery in order to reach the conclusion that the New York direct interstate shipment ban was constitutional, for the court itself acknowledged that the ban "create[s] substantial dormant Commerce Clause problems" (Pet. App. 26a). In that latter conclusion, the court undoubtedly was correct.

"The few simple words of the Commerce Clause," this Court declared in *Hughes v. Oklahoma*, 441 U.S. 322, 325

(1979), "reflected a central concern of the Framers that was an immediate reason for calling the Constitutional Convention: 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." The hodgepodge of conflicting state regulations over direct interstate shipping of wine depicted on the map on the following page paints in striking terms precisely the portrait of economic Balkanization the Framers sought to avoid. In some states, Mrs. Swedenburg can freely sell her wine directly to consumers; in others, to do so would constitute a felony. More to the point: in New York, a domestic winery can freely sell and ship wine to consumers; but if Mrs. Swedenburg tries to do so, she would be subject to criminal penalty[10] and loss of her livelihood, solely by virtue of her residency. That is the type of disability the Commerce Clause forbids.

[10] In New York, violation of direct shipping laws is a criminal misdemeanor (ABC Law §130; J.A. 151).

Restricting Interstate Shipment of Wine to Consumers



Source: Institute for Justice

Nor is the plight of Juanita Swedenburg and her desirous patrons at all unique. The Federal Trade Commission has characterized state bans on direct shipment of wine to consumers as "the single largest regulatory barrier to expanded e-commerce in wine," leading to diminished consumer selection and increased prices. FTC Report at 3, 14-25. Just this year, the FTC found that allowing direct interstate shipping would "allow New York residents to purchase a greater variety of wines at lower prices," and "would enhance consumer welfare and enable New York to meet its other public policy goals."[11] Plainly, the Commerce Clause is implicated by both the interests of producers and consumers; and as we shall show in Part II, the 21st Amendment presents no bar to their vindication.[12]

[11] Letter from Todd Zywicki, Director, Office of Policy Planning, Federal Trade Commission, et al., to William Magee, Chairman, New York Assembly Agriculture Committee, et al. of 3/29/04, at 2, at http://www.ftc.gov/be/V040012.pdf (hereinafter FTC Letter).

[12] We are mindful and respectful of the fact that some Justices have called into question the legitimacy of "negative Commerce Clause" analysis. *See, e.g.*, *Camps Newfound/Owatonna, Inc. v. Town of Harrison*, 520 U.S. 564, 609-39 (1997) (Thomas, J., dissenting); *Tyler Pipe Indus. v. Wash. State Dep't of Rev.*, 483 U.S. 232, 265 (1987) (Scalia, J., concurring in part and dissenting in part). Despite those misgivings, we urge the Justices to reach a result here in keeping with the well-developed jurisprudence under that doctrine.

We do not take the thoughtful concerns of those Justices to indicate disagreement with the underlying constitutional values, but rather with the derivation of those values from the Commerce Clause. In this case, the same result petitioners urge under the Commerce Clause should also obtain under the Privileges and Immunities Clause, U.S. Const. art. IV, §2, which protects the right of out-of-state residents to conduct business on the same terms as in-state residents. *See, e.g.*, *Hillside Dairy Inc. v. Lyons*, 539 U.S. 59 (2003); *United Bldg. & Constr. Trades Council v. Mayor and Council of Camden*, 465 U.S. 208, 219 (1984); *Supreme Ct. of N.H. v. Piper*, 470 U.S. 274 (1985); *Toomer v.*

(Continued on following page)

A. Discriminatory Direct Shipment Bans Violate the Commerce Clause.

The overriding concern of the Commerce Clause is discrimination. "For over 150 years, our cases have rightly concluded that the imposition of a differential burden on any part of the stream of commerce – from wholesaler to retailer to consumer – is invalid, because a burden placed at any point will result in a disadvantage to the out-of-state producer." *West Lynn Creamery*, 512 U.S. at 702.[13] Failure by a state to adhere to the "cardinal requirement of nondiscrimination" is almost always fatal. *New Energy*

Witsell, 334 U.S. 385, 396 (1948); *Dickerson v. Bailey*, 336 F.3d 388, 403 n.67 (5th Cir. 2003).

As even the Second Circuit concedes ("Section 2's grant of authority to the state to regulate alcohol within its borders could not sustain state statutes that violated individual liberties protected by other constitutional provisions" (Pet. App. 19a)), the 21st Amendment impacts the scope of the Commerce Clause, but not any other provision of the Constitution. *See*, *e.g.*, *44 Liquormart v. Rhode Island*, 517 U.S. 484, 516 (1996); *Craig v. Boren*, 429 U.S. 190, 206 (1976). Petitioners raised a Privileges and Immunities claim below, on which this Court did not grant review. Still, it makes sense from the standpoint of both judicial economy and justice to take into account the background principles of the Privileges and Immunities Clause when interpreting the Commerce Clause in this case. (For a fuller explication of this argument, *see* Brief of Amicus Curiae Virginia Wineries Association filed in Case No. 03-1274).

The discriminatory wine ban implicates other constitutional doctrines as well, including equal protection, *see, e.g.*, *Metropolitan Life Ins. Co. v. Ward*, 470 U.S. 869 (1985); *Yick Wo v. Hopkins*, 118 U.S. 356 (1897); and the right to travel, *see, e.g.*, *Saenz v. Roe*, 526 U.S. 489 (1999). A decision upholding a discriminatory ban under the Commerce Clause would be in patent disharmony with the values protected by those constitutional guarantees.

[13] "The Court, without dissent, has vigorously enforced the nondiscrimination principle to this day." Anderson, "Direct Shipment of Wine, the Commerce Clause and the Twenty-first Amendment: A Call for Legislative Reform," 37 *Akron L. Rev.* 1, 19 (2004).

Co. of Ind. v. Limbach, 486 U.S. 269, 274 (1988). Discrimination, then, is both the beginning and end of the Commerce Clause inquiry, for it ferrets out the protectionism that the clause was meant to proscribe.

In *Hughes*, 441 U.S. at 336, the Court set forth the "general rule" of Commerce Clause inquiry:

> [W]e must inquire (1) whether the statute regulates evenhandedly with only "incidental" effects on interstate commerce, or discriminates against interstate commerce either on its face or in practical effect; (2) whether the statute serves a legitimate local purpose; and, if so, (3) whether alternative means could promote this local purpose as well without discriminating against interstate commerce.

The initial burden to show discrimination rests with the challenging party, but once that burden is met, "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." *Hunt v. Wash. Apple Adver. Comm'n*, 432 U.S. 333, 353 (1977). "At a minimum such facial discrimination invokes the strictest scrutiny of any purported legitimate local purpose and of the absence of nondiscriminatory purposes." *Hughes*, 441 U.S. at 337. "Furthermore, when considering the purpose of a challenged statute, this Court is not bound by '[t]he name, description or characterization given it by the legislature or the courts of the State,' but will determine for itself the practical impact of the law." *Id.* at 336 (citations omitted).

There are many forms of facial discrimination, all of which trigger strict scrutiny. The classic form of facial discrimination, of course, is where a state flat-out imposes two different sets of fees or requirements, with the more onerous burden placed upon interstate commerce. *See, e.g.*, *Boston Stock Exch. v. State Tax Comm'n*, 429 U.S. 318 (1977). Variations on the theme include instances where the state creates a set of fees or regulations, then creates an exemption for in-state industries or products, *see, e.g.*, *Bacchus*, 468 U.S. 273; *Hale v. Bimco Trading*, 306 U.S. 375 (1939); where the state creates special burdens for interstate commerce as a condition of doing business in the state, *see*, *e.g.*, *Union Co. v. Kansas*, 216 U.S. 1 (1910); and where the state requires the establishment of in-state business operations to enjoy special benefits available to residents. *See, e.g.*, *Bethlehem Motors Corp. v. Flynt*, 256 U.S. 421 (1921); *see also* Part IC, *infra*. New York's ban on direct interstate wine shipments is distinguished in that it manages to encompass *all* of the foregoing varieties of facial discrimination against interstate commerce.

In sum, the demands placed upon the State to justify a facially discriminatory statute constitutes "an extremely difficult burden, 'so heavy that "facial discrimination may by itself be a fatal defect."'" *Camps Newfound/ Owatonna,* 520 U.S. at 582 (citations omitted). The clumsy and severe discrimination practiced by New York should be condemned.

B. The State's Ban on Interstate Direct Shipping, and the Exemptions for Domestic Wineries, Are Protectionist in Structure, Origin, and Avowed Intent.

The Court need not journey far to discover overtly protectionist motives in this case: as in *Bacchus*, the State has confessed its protectionist motivations.

The State adopted its three-tier system for alcohol distribution following the end of Prohibition. Since then, there have been three flashpoints at which the State avoided the high road in favor of the protectionist route: (1) when it tightened restrictions on interstate direct shipments in 1970; (2) when it created exemptions to those restrictions for in-state producers; and (3) when the governor vetoed legislation in 1995 that would have permitted interstate direct shipping. All three instances are uncontroverted and well-documented in the record.

In 1970, changes were made to the ABC laws to close direct shipment loopholes (2d Cir. J.A. 387). The legislative history makes clear, as summarized by a telegram to the governor from the "Council [of] Greater NY Wholesale Liquor," that "our ndustry (sic) an (sic) the state are hurt by the conditions this bill corrects," and that the bill "is supported by the entire alcoholi (sic) beverage industry" (2d Cir. J.A. 372); and indeed, support poured in from affected in-state business interests (2d Cir. J.A. 415-29). In a case challenging the law that same year, the district court found that it "was enacted . . . to prevent what was considered to be an unfair and unwise form of competition with New York state licensees, and to eliminate unfair tax advantages." *House of York*, 322 F. Supp. at 533.

In 1995, the legislature passed by an overwhelming margin a bill authorizing direct shipment of wine from states providing reciprocal opportunities for New York wineries. The bill contained quantity limits and safeguards against underage access (2d Cir. J.A. 449-53). Many New York State wineries supported the bill because it would open markets to their products in other states (2d Cir. J.A. 447, 458-59, 489-93, 502-03, 516-19). Liquor distributors and their allies turned out in force against the bill (2d Cir. J.A. 477, 481-88, 497, 499-500, 505, 507, 509-10, 522-36). The bill was vetoed by Gov. George Pataki, whose veto message was avowedly protectionist. He assailed its "potentially negative impact . . . on existing, licensed New York businesses relying on wine sales," arguing that it could "lead to a decrease in sales for New York liquor stores and distributors" (2d Cir. J.A. 442).

Likewise, the direct shipment exemptions on their face are intended to promote New York wineries (Pet. App. 54a-55a; 2d Cir. J.A. 296-305), an intent conceded by the state's attorney in the district court (Pet. App. 55a). "Thus, we need not guess at the legislature's motivation, for it is undisputed that the purpose of the exemption was to aid [local] industry." *Bacchus*, 468 U.S. at 271. The discriminatory ban against direct interstate wine shipments is a system by, of, and for New York economic interests. As such, it constitutes a classic violation of the Commerce Clause.

C. The In-State Premises Requirement Does Not Decontaminate the Discrimination.

One point on which the parties agree is that there is no way an out-of-state winery, as such, can ship directly to New York consumers. As the State Liquor Authority's general counsel flatly admitted, "the plaintiffs seek to engage in a business – the direct shipment of wine from out-of-state wineries to New York consumers – which is not allowed under the ABC law" (J.A. 159). Given the fact that in-state wineries freely may do so, that presents a clear-cut case of discrimination.

The Second Circuit's way around that serious obstacle was to respond: then just become a *New York winery*. It concluded that there is no real discrimination because out-of-state wineries can access direct shipment opportunities merely by establishing a "physical presence" in the state. So stated, the burden sounds so light, so ephemeral, as to be downright evanescent. Why didn't the plaintiff wineries think of doing that? All of this litigation could have been avoided.

As depicted in the appeals court decision, one might imagine that the legislature sat down in dispassionate, statesmanlike fashion and produced a thoughtful system to create a careful, structured "physical presence" requirement. In fact, of course, it did no such thing. What the legislature did was to tighten the screws on interstate direct shipping on the one hand while creating exemptions for in-state wineries on the other. It took the general counsel of the State Liquor Authority, in response to this lawsuit,[14] to cobble together different parts of the law to construct a theoretically possible route for out-of-state wineries to access direct shipping opportunities. That putative solution is so complex, convoluted, and burdensome that not a single winery has ever even attempted it.[15]

[14] Previously, the State flatly informed out-of-state wineries that they could not ship directly to New York consumers (2d Cir. J.A. 306-346).

[15] The requirements, as described by respondents' witness (J.A. 159-160), include opening a branch office and warehouse, applying for a winery license and warehouse permit, then applying for a retailer permit that allows sale to "a householder for consumption in his home," and shipping through a common carrier licensed to deliver alcoholic beverages. The warehouse must be fully staffed, separate from other premises, and devoted solely to wine distribution, with stiff sanctions for violations (J.A. 150-151; 2d Cir. J.A. 347, 350-60). Moreover, an out-of-state winery would have to buy or lease an office and establish operations in New York *before* even knowing whether its New York

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(J.A. 159). Yet that is the peg on which the Second Circuit hung its hat.[16]

It doesn't work, on multiple levels. An in-state business premises requirement would be the exception that swallows the rule of nondiscrimination. If a state may deflect a Commerce Clause claim by saying that an out-of-state producer can transact with in-state consumers so long as it does so as an in-state business, that would eviscerate the Commerce Clause, for it is almost always at least technically possible to do exactly that. The point of the Commerce Clause (and, for that matter, the Privileges and Immunities Clause) is to protect the flow of commerce *across* state lines. And as a practical matter, obviously, the large majority of American wineries that are small cannot maintain fully staffed, bricks-and-mortar business operations in multiple states, let alone all 50 – which would be permitted, of course, by the rule proposed below.

That concept is antithetical to the national market that animated the Framers. Imagine Thomas Jefferson's reaction if he had been told after the Constitution was adopted that in order to sell goods in New York, he would have to move there. Juanita Swedenburg, likewise a proud

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license was approved. *See* ABC Laws §§105(1), 110(1)(b) & (f) (J.A. 159). Even assuming an out-of-state winery could overcome these incredibly costly hurdles, as amicus Millbrook Winery points out, the sales and shipping options are still heavily skewed in favor of wineries that are physically located in New York and those that produce wine from New York grapes. *See* Brief of Amicus Curiae Millbrook Vineyard and Winery filed in Case No. 03-1274.

[16] This concept appears to have originated in an earlier Second Circuit ruling dealing not with wine but with tobacco products. *See Brown & Williamson Tobacco Corp. v. Pataki*, 320 F.3d 200 (2d Cir. 2003).

Virginian, feels the same way. That is why it is a centerpiece of Commerce Clause jurisprudence that a state cannot encourage an out-of-state firm "to become a resident in order to compete on equal terms." *Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64 (1963); *accord*, *Fulton Corp. v. Faulkner*, 516 U.S. 325, 333 n.3 (1996). As a result, "the Court has viewed with particular suspicion state statutes requiring business operations to be performed in the home State that could more efficiently be performed elsewhere. Even where the State is pursuing a clearly legitimate local interest, this particular burden on commerce has been declared to be virtually per se illegal."[17] *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 145 (1970).

States have attempted such end-runs around the Commerce Clause for well over a century, and this Court has rejected them equally as long. In *Ward v. Maryland*, 79 U.S. 418 (1870), the state argued that out-of-state businesses could avail themselves of certain in-state preferences by bringing their goods into the state to sell, which the Court rejected. As Justice Bradley observed, "[S]uch a law would effectually prevent the manufacturers of the manufacturing States from selling their goods in other States unless they established commercial houses therein, or sold to resident merchants who chose to send them orders." *Id.* at 432 (Bradley, J., concurring). Such is precisely the vice here. *See, e.g.*, Brownlee, "Economic

[17] As a result, "most courts would find that a 'regular place of business' requirement is per se unconstitutional." *Codar, Inc. v. Ariz.*, No. 94-1690Z, 1996 U.S. App. LEXIS 21536, at *10 (9th Cir. August 19, 1996); *accord*, *Nutritional Support Svcs., L.P. v. Miller*, 830 F. Supp. 625 (N.D. Ga. 1993); *Ga. Ass'n of Realtors, Inc. v. Ala. Real Est. Co.*, 748 F. Supp. 1487 (M.D. Ala. 1990); *Underhill Assocs., Inc. v. Coleman*, 504 F. Supp. 1147 (E.D. Va. 1981).

Protection for Retail Liquor Dealers: Residency Requirements and the Twenty-first Amendment," 1990 *Colum. Bus. L. Rev.* 317 (1990).

Similarly, in *Dean Milk Co. v. Madison*, 340 U.S. 349 (1951), the Court struck down a law requiring that milk sold in Madison, Wisconsin must be processed at a plant nearby. Finding that such a requirement "plainly discriminates" against interstate commerce, *id.* at 354, the Court concluded that the law was unconstitutional because "reasonable and adequate alternatives" were available to protect health and safety concerns. *Id.* Similarly, in *C&A Carbone, Inc. v. Town of Clarkstown*, 511 U.S. 383, 391 (1994), the Court invalidated a flow control ordinance, finding that "the article of commerce is not so much the solid waste itself, but rather the service of processing and disposing of it," so that restricting such service to specific entities "thus deprives out-of-state businesses of access to a local market." *Id*. at 389. So too does the challenged law restrict access to a local market by creating a local distribution monopoly; but the law here is even more brazen because it exempts local producers from the same requirements.

D. The New York System Is Blatantly Discriminatory.

Even if the theoretical option of an in-state, bricks-and-mortar business establishment requirement were to qualify for the talismanic status under the 21st Amendment afforded to it by the Second Circuit, it would be unavailing in this case, for it still leaves the playing field sharply skewed. "Under this scheme," the appeals court acknowledged with remarkable understatement, "out-of-state wineries will incur some costs in establishing and maintaining a physical presence in New York, costs not incurred by in-state wineries" (Pet. App. 26a).

In essence, the court of appeals perceives the extra costs as a type of permissible differential tax. But the Commerce Clause does not say that discriminatory burdens are okay so long as some theoretical means exist for an outsider firm to gain access to the market. Rather, it is held to require a fully level playing field. For that reason, differential tax burdens repeatedly have been struck down. *See*, *e.g.*, *James B. Beam Distilling Co. v. Ga.*, 501 U.S. 529 (1991); *Bacchus*, 468 U.S. at 272; *Armco Inc. v. Hardesty*, 467 U.S. 638, 645-46 (1984)*; Boston Stock Exch.*, 429 U.S. at 332; *Halliburton*, 373 U.S. at 65-75.

Even if those costs were moderate, which they are not,[18] it would make no difference; for discriminating, like sinning, is a vice whose consequences are the same even if you only do it a little bit. "The commerce clause forbids discrimination, whether forthright or ingenious." *Best & Co. v. Maxwell,* 311 U.S. 454, 455-56 (1940). It precludes *any* "differential burden on any part of the stream of commerce." *West Lynn Creamery*, 512 U.S. at 202. Where a law is facially discriminatory, any impact on interstate commerce, no matter how small, is sufficient to invoke strict scrutiny. "The volume of commerce affected . . . is of no relevance to the determination of whether a State has discriminated against interstate commerce." *Wyoming v. Oklahoma*, 502 U.S. 437, 455 (1992). "[A]ctual discrimination, wherever it is found, is

[18] For the overwhelming majority of out-of-state wineries that do not also happen to own New York wineries, the cost of establishing a fully staffed winery and warehouse in New York (and elsewhere if such a restriction is valid) is prohibitive, to put it mildly (*see, e.g.*, J.A. 201-202; 2d Cir. J.A. 3560-61).

impermissible, and the magnitude and scope of discrimination have no bearing on the determinative question whether discrimination has occurred." *Assoc. Indus. of Mo. v. Lohman*, 511 U.S. 641, 650 (1994). Hence, "where discrimination is patent . . . , neither a widespread disadvantage to in-state interests nor a widespread disadvantage to out-of-state competitors need be shown." *New Energy Co. of Ind. v. Limbach*, 486 U.S. at 276. *Accord*, *Fulton Corp. v. Faulkner*, 516 U.S. 325, 334 n.3 (1996) (no *de minimis defense to facial discrimination*); *Bacchus*, 468 U.S. at 269 ("the small volume of sales of exempted liquor" is irrelevant); *Maryland v. Louisiana*, 451 U.S. 725, 760 (1981) ("we need not know how unequal the Tax is before concluding that it unconstitutionally discriminates").

But here, the discrimination is not a smidgeon, it is whopping. The appeals court trivialized the additional costs of separate bricks-and-mortar business establishments in two states (which could of course be more if other states join the parade)[19], and they are noxious enough. But it overlooked totally the fact that even if an out-of-state winery managed to open a New York winery in order to avail itself of direct shipping opportunities, it *still would be foreclosed from the easiest direct sales and shipping options, which are available only to wines made from New York grapes*.

[19] "[T]he practical effect of the statute must be evaluated . . . also by considering . . . what effect would arise if not one, but many or every State adopted similar legislation." *Healy*, 491 U.S. at 336; *Carbone*, 511 U.S. at 406 (O'Connor, J., concurring in the judgment).

As the chart on the next page illustrates, New York provides three options for direct shipping. It reserves the easiest for farm wineries – a status that most New York wineries hold (J.A. 206) – while applying far more cumbersome requirements to others. The discrimination could not be more palpable: ABC Laws §76-a5 (Pet. App. 93a) provides, "No licensed farm winery shall manufacture or sell any wine not produced exclusively from grapes or other fruits or agricultural products grown or produced in New York state."[20] Similarly, many of the direct sales and shipping options for commercial wineries in New York are limited to the sale of "New York State labeled wine." *See* ABC Laws §§76(2)(a) (tastings); 76(4) and 77(4)(b)(4) (allowing sales and deliveries of New York state labeled wines from other wineries and at dinner theaters); 76(5) (allowing sales at state and county fairs and farmers markets); 77(5) (allowing sales on Sundays and at the state fair). So that even if the State does have a legitimate purpose in forcing out-of-state wines to establish business operations in New York, out-of-state wineries still would be subject to blatant facial discrimination.

[20] Nor could the intended favoritism be more clear. In empowering the State Liquor Authority to issue implementing regulations, §§76a(4)(d) (Pet. App. 93a) and 77(4)(f) (J.A. 14-15) commands the authority to "promote the expansion and profitability of wine production and tourism in New York."

DIRECT SHIPPING OPTIONS		
OPTION	**NEW YORK WINERIES**	**OUT-OF-STATE WINERIES**
Farm wineries exemption (ABC Law § 76-a(6)(b))	Wineries located on New York farms may ship wine produced exclusively from New York grapes directly to consumers using their own trucks or trucks hired from others.	Unavailable.
Wine by wire (ABC Law § 76(5))	Wineries located "within the state" may have their wine delivered by other wineries located "within the state."	Unavailable.
Commercial wineries exemption (ABC Law §§ 76(4) and 105-9)	Commercial wineries may obtain a retail sales license to sell at retail and deliver "New York state labeled wines." Delivery must be in their own trucks or in trucks hired from a company registered with the State Liquor Authority.	Out-of-state wineries must obtain a winery license and establish a branch office and warehouse in New York. ABC Law §§ 3(37), 96. Wine must then be shipped from out-of-state winery and consigned to in-state warehouse. *Id.* §§ 3(37), 102(1)(c) and (d). (J.A. 159-60.) Winery must then obtain a certificate, issued in the liquor authority's "discretion and upon such terms and conditions as it may prescribe," authorizing the retail sale of wine to a "householder for consumption in his home." ABC Law § 77(2). The winery may then deliver to such individuals using a trucking company licensed by the State to transport alcoholic beverages. *Id.* § 105(9). The warehouse must be fully staffed, in premises separate from other businesses and dedicated solely to wine distribution. ABC Law § 3(37). (J.A. 159-60; 2d. Cir. J.A. 347, 35-60.)

In other words, the New York law frees in-state wineries from the three-tier system altogether, while out-of-state wineries are forced to become *part of the three-tier system*. New York wineries may sell and ship wine directly to consumers *as wineries*; out-of-state wineries only may do so if they assume all three roles in the distribution process: winery, wholesaler, and retailer.

Just as a "preferred right of access" to a state's resources is discriminatory, *see, e.g. City of Philadelphia v. New Jersey*, 437 U.S. 617, 627 (1978), so too is a preferred right of access to its consumers. As this Court set down the rule in *Oregon Waste*, 511 U.S. at 99, "'discrimination' simply means differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter. If a restriction on commerce is discriminatory, it is virtually *per se* invalid."

Here, New York regulates direct wine shipments not by one set of rules but by two: one set, which imposes hardly any impediments at all, that are applicable only to domestic wine products; while a second, far more cumbersome regime applies to all others. *Compare Kassel v. Consolidated Freightways, Inc.*, 450 U.S. 662 (1981) (differential rules struck down). As the Fifth Circuit so aptly put it in striking down Texas' discriminatory direct shipment rules, "To paraphrase the Bard, that which we call discrimination by any other name would still smell as foul." *Dickerson*, 336 F.3d at 398 (finding that the "numerous ways in which in-state wineries are exempt" demonstrates that the system "is neither evenhanded nor incidental"); *see also* Pet. App. 52a-57a (district court findings of discrimination and protectionism). The discrimination is here blatant, overtly protectionist, and invalid under the Commerce Clause.

II. THE 21st AMENDMENT PROVIDES NO SHELTER FOR LAWS THAT DISCRIMINATE AGAINST INTERSTATE COMMERCE.

A. The Commerce Clause and 21st Amendment Must Be Construed in Tandem.

1. The court of appeals rested its decision upon a claim as sweeping as it is unsupportable: that if the exercise of state power is "within the ambit" of 21st Amendment authority, "it is exempted from the effect of the dormant Commerce Clause" (Pet. App. 13a). Whatever superficial appeal that assertion might hold disappears quickly upon examination of the amendment's history and of this Court's efforts to harmonize rather than cannibalize constitutional provisions.

Section 2 of the 21st Amendment did restore states' powers to regulate the "transportation or importation" of intoxicating liquors within their borders. "[T]he 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." *Calif. Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 110 (1980). The use of a three-tier system to implement such a system is "unquestionably legitimate." *North Dakota v. United States*, 495 U.S. 423, 432 (1990). Indeed, a state may lawfully "require that *all* liquor sold for use in the State be purchased from a licensed in-state wholesaler." *Id.* at 447 (Scalia, J., concurring in the judgment) (emphasis added).

However, this is merely the beginning of the 21st Amendment, not its end. For in exercising their authority over "how to structure the liquor distribution system," *Midcal*, 445 U.S. at 110, the Constitution, acts of Congress, and this Court's precedents all make it clear that a state must choose one set of governing rules, not two. Or, to borrow Justice Scalia's phrase, it may require *all* of its liquor to pass through a three-tier system, but not merely that which is sold by out-of-state producers. There is no question that the states' 21st Amendment powers are broad. But the decision below rests upon the premise that those powers are plenary, creating a sort of Commerce Clause-free zone, which they do not.

Before Prohibition, this Court construed the Commerce Clause to forbid state interference with interstate shipment of alcohol *at all*. *See, e.g.*, *Leisy v. Hardin*, 135 U.S. 100 (1989). In the Wilson Act, 27 U.S.C. §121, Congress allowed states to regulate sales of imported alcohol to the same extent they chose to regulate domestically produced alcohol. Then, to eliminate the loophole in the Wilson Act that allowed producers to consummate the "sale" of alcohol outside a state and then transport it into the state, Congress enacted the Webb-Kenyon Act, 27 U.S.C. §122, which made it clear that states could exclude alcohol altogether. Those affirmative actions by Congress narrowed the scope of the Commerce Clause but did not eliminate it. *See, e.g.*, *Scott v. Donald*, 165 U.S. 58, 100 (1897) ("the State cannot, under the [Wilson Act] . . . , establish a system which, in effect, discriminates between interstate and domestic commerce").

In repealing Prohibition, Congress constitutionalized the provisions of the Wilson and Webb-Kenyon Acts in section 2 of the 21st Amendment. *See Craig v. Boren*, 429 U.S. 190, 205 (1976); *Fla. Dep't of Bus. Reg. v. Zachy's Wine and Liquor*, 125 F.3d 1399, 1401 (11th Cir. 1997). In so doing, Congress re-extended to the states broad authority to regulate alcohol, but it did not expunge the nondiscrimination principle. To the contrary, Congress expressly reaffirmed it by re-enacting the Wilson Act, 27 U.S.C. §121, subsequent to the passage of the 21st Amendment. The law's nondiscrimination command could not be more explicit in providing that all alcoholic products "transported into any State . . . shall . . . be subject to the operation and effect of the laws of such State . . . *to the same extent and in the same manner as though such liquids or liquors had been produced in such State.*" (Emphasis added).[21]

2. By ignoring not only the context and intent of section 2 of the 21st amendment but also the Commerce Clause itself, the court below 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. Only a generation removed from its ratification, the Court in *Gibbons v. Ogden*, 22 U.S. 1, 231 (1824), remarked that, "If there was any one object riding over every other in the adoption of the constitution, it was to keep the commercial intercourse among the States free from all invidious and partial restraints."

Far from fading into a quaint historical relic, the Commerce Clause is more salient today than ever. The advent of the Internet and its vast, unprecedented promise of consumer freedom are juxtaposed against the predictable efforts of middlemen who resort not to the marketplace but to the coercive power of the state to protect their economic hegemony, to the detriment of producers and

[21] Indeed, the State respondents, in their opening Second Circuit brief below (at 6), correctly observed that the Wilson Act "removed the privileged status enjoyed by interstate sellers, *without authorizing states to discriminate against them*" (emphasis added).

consumers alike. *See, e.g.*, Newkirk and Atkinson, "Buying Wine Online, Rethinking the 21st Amendment for the 21st Century," *Progressive Policy Inst.*, January 2003 (available at http://www.ppionline.org/ppi_ci.cfm?knlgAreaID=140&subsecID=900055&contentID=251266); Smith, "Consumer Protection or Veiled Protectionism? An Overview of Recent Challenges to State Restrictions on E-Commerce," 15 *Loy. Consumer L. Rev.* 359 (2003). All too often, states are willing to shelter their own firms from competition. It is to preserving an unfettered national marketplace that the Commerce Clause is devoted.

The 21st Amendment restored state control over alcohol, but did not obliterate the core Commerce Clause concern against discrimination. As this Court aptly put it in *Hostetter v. Idlewild Bon Voyage Liquor Corp.*, 377 U.S. 324, 331-32 (1964), the notion that the 21st Amendment "has somehow operated to 'repeal' the Commerce Clause . . . [is] an absurd oversimplification."[22] By limiting its constitutional inquiry to the 21st Amendment, the court of

[22] This Court's early cases, *see*, *e.g.*, *State Board of Equalization of California v. Young's Market Co.*, 299 U.S. 59 (1936), which involved neither discrimination nor a trade barrier, are sometimes construed to have more broadly interpreted the 21st Amendment in the Commerce Clause context; but in any event, more recent cases consistently have applied precisely the "two-tier" analysis the appeals court below rejected. *See, e.g.*, Silvernail, "Smoke, Mirrors, and Myopia: How the States Are Able to Pass Unconstitutional Laws Against the Direct Shipping of Wine in Interstate Commerce," 44 *So. Tex. L. Rev.* 499 (2003); Molnar, "Under the Influence: Why Alcohol Direct Shipment Laws are a Violation of the Commerce Clause," 9 *U. Mia. Bus. L. Rev.* 169 (2001); Kozusko, "The Fight to 'Free the Grapes' Enters Federal Court: Constitutional Challenges to the Validity of State Prohibitions on the Direct Shipment of Alcohol," 20 *J. L. & Com.* 75 (2000); Shanker, "Alcohol Direct Shipment Laws, the Commerce Clause, and the Twenty-first Amendment," 85 *Va. L. Rev.* 353 (1999).

appeals indulged in precisely the "absurd oversimplification" this Court spurned four decades earlier in *Hostetter*. New York again argues that the 21st Amendment power is plenary. It was wrong in *Hostetter*, and it is wrong here.

3. The appeals court's sweeping view of the 21st Amendment would divest Congress of its power to restrain anticompetitive acts of states with regard to alcohol. Plainly, it has not. In an unbroken line of cases, this Court has affirmed and applied congressional authority in such fashion. *See*, *e.g.*, *Brown-Forman*, 476 U.S. at 585; *Capital Cities*, 467 U.S. at 715-16; *Midcal*, 445 U.S. at 108-09. Nor is congressional power unexercised in the context presented here, given the clear command of nondiscrimination embodied in the Wilson Act.

4. The same principle controls in the interplay between the dormant Commerce Clause and the 21st Amendment. "When a state statute directly regulates or discriminates against interstate commerce or when its effect to favor in-state economic interests over out-of-state economic interests, we have generally struck the statute down without further inquiry." *Brown-Forman*, 476 U.S. at 579. Indeed, in the very case upon which respondents rely so heavily, *North Dakota v. United States*, 495 U.S. 423 (1990)[23], Justice Scalia hastened to make the very same

[23] That case involved the imposition by the state of certain nondiscriminatory regulations on the federal government's shipments of alcohol to military installations. The Court held that where the State imposes a single set of alcohol importation regulations, the federal government, like everyone else, may be held to comply – a proposition with which petitioners emphatically agree. Justice Scalia made the point that the case would be markedly different if the State imposed two sets of rules, not one. *North Dakota*, 495 U.S. at 444. Then it would be like this case.

point. *Id.* at 444 (Scalia, J., concurring in the judgment) ("All agree in this case that state taxes or regulations that discriminate . . . are invalid"); *id.* at 448 ("That is not to say, of course, that the State may enact regulations that discriminate"). Where a barrier to interstate commerce is presented, the law's "discriminatory character eliminates the immunity afforded by the Twenty-first Amendment." *Healy v. Beer Inst.*, 491 U.S. 324, 344 (1989) (Scalia, J., concurring).

The paradigm case for analyzing facially discriminatory barriers to commerce in alcohol is *Bacchus.* There, liquor distributors challenged an exemption by the State of Hawaii of a locally produced brandy from an otherwise applicable excise tax.[24] The exemption was passed, like the New York farm winery exemption here, to benefit local industry.

The Court engaged in the two-part analysis rejected by the appeals court below, declaring that the "question in this case" is "whether the principles underlying the

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[24] The analysis is the same whether the discrimination takes the form of taxation or some other type of regulation. Both taxes and regulations inevitably have an effect on the flow of commerce, as this Court repeatedly has recognized. *See, e.g.*, *Oregon Waste Sys. v. Dep't on Environ. Qual.*, 511 U.S. 93 (1994); *Chemical Waste Mgmt. v. Hunt*, 504 U.S. 334 (1992); *cf. Bacchus*, 468 U.S. at 268 n.8 ("Our cases make clear that discrimination between in-state and out-of-state goods is as offensive to the Commerce Clause as discrimination between in-state and out-of-state taxpayers"). It would make no sense for the Court to strike down a protectionist tax on alcohol while sustaining an even more onerous protectionist regulation on importation, for the effects – and the states' possible justifications – are the same. *Cf. North Dakota v. United States,* 495 U.S. at 444 (Scalia, J., concurring in the judgment) ("All agree in this case that state *taxes or regulations* that discriminate . . . are invalid") (emphasis added).

Twenty-first Amendment are sufficiently implicated . . . to outweigh the Commerce Clause principles that would otherwise be offended." *Bacchus*, 468 U.S. at 275. It began by examining whether the motive for the exemption was economic protectionism, a finding that "may be made on the basis of discriminatory purpose or discriminatory effect." *Id.* at 270 (citations omitted). As here (Pet. App. 54-55a), the purpose of the exemptions was to advance local industry, and the exemption discriminated against out-of-state products. The Court concluded that the 21st Amendment considerations did not outweigh Commerce Clause concerns, because "one thing is certain: The central purpose of [section 2] was not to empower States to favor local liquor industries by erecting barriers to competition." *Id.* at 276.

Hence, respondents have it exactly backward: state action related to transportation and importation of alcohol is not shielded from Commerce Clause scrutiny; rather, state action promoting economic protectionism, as manifested by discriminatory trade barriers, is removed from what is otherwise the 21st Amendment's safe harbor for neutral state regulation of trade in alcohol.

Far from aberrational, the *Bacchus* two-part analysis is precisely the framework applied in all such cases of modern vintage, regardless of the type of regulatory impediment at issue. *See, e.g.*, *Healy*, 491 U.S. at 288 n.14; *Brown-Forman*, 476 U.S. at 579; *Capital Cities*, 467 U.S. at 714; *Midcal*, 445 U.S. at 113; *Hostetter*, 377 U.S. at 333-34. *See also Beskind v. Easley*, 325 F.3d 506, 514 (4th Cir. 2003); *Dickerson*, 336 F.3d at 396; *Bainbridge v. Turner*, 311 F.3d 1104, 1108-09 (11th Cir. 2002); *Mt. Hood Bev. Co. v. Sebastiani Vineyards, Inc.*, 63 P.3d 779, 786 (Wash. 2003). Indeed, this Court found no impediment to invalidating, in the face of states' 21st Amendment "core powers" assertions, discriminatory purchase rules in *Craig v. Boren*, 429 U.S. 190 (1976) or advertising restrictions in *44 Liquormart v. Rhode Island*, 517 U.S. 484 (1996). The glaring exception to this uniform analytical approach is the court of appeals ruling below.

5. The Court of Appeals calls into question all of the law that accords equal dignity to the Commerce Clause and section 2. This body of law readily satisfies the criteria for adherence to *stare decisis* as set forth in *Planned Parenthood of Southeastern Pennsylvania v. Casey*, 505 U.S. 833, 854-55 (1992); *see also United States v. IBM Corp.*, 517 U.S. 843, 856 (1996). No difficulty exists in the practical workability of the nondiscrimination principle: a state has merely to choose a single set of rules regarding direct shipment and apply them to both domestic and out-of-state wineries. Indeed, when this lawsuit began, direct shipping of wine was forbidden by 31 states and permitted only in 19. In just five years, seven states including Mrs. Swedenburg's Virginia have moved into the direct shipment category, so that now over half the states allow direct shipping.[25] The FTC reports that those states are able fully to satisfy their legitimate regulatory concerns without recourse to discriminatory trade barriers. *See* FTC Report at 26-40.

Abandoning the rule of nondiscrimination would impose severe hardship on small wineries such as Mrs. Swedenburg's and Mr. Lucas' that rely heavily upon direct

[25] As discussed in Part IB, *supra*, it is primarily the political influence of the liquor distributors that has prevented New York from abandoning its protectionist regime.

shipments to sell their product. That rule is far from discarded doctrine; indeed, it represents an unbroken line of precedent for 150 years (and applied consistently in the context of alcohol for at least 40 years since *Hostetter*). Those precedents in turn have been faithfully applied by a majority of appeals courts that have decided the question. All of those reasons counsel strongly in favor of adherence to *stare decisis*.

6. In sum, the question posed by the Court has been decided repeatedly and correctly. The desires of Mrs. Swedenburg and Mr. Lucas and their New York customers to transact with one another should be determined by equal and impartial rules, not by rules established to protect local economic interests. The essential jurisprudential mandate of according meaning to all parts of the Constitution, the animating history of both the Commerce Clause and the 21st Amendment, affirmative congressional expression, *stare decisis*, and complementary constitutional provisions all militate in favor of maintaining the rule that discriminatory trade barriers find no shelter in the 21st Amendment.

B. New York's Discriminatory Trade Barrier Cannot Find Sanctuary Within the 21st Amendment.

Though it paid lip service to it, the court below failed to adhere to this Court's command in *Hostetter*, 377 U.S. at 332, that "[b]oth the Twenty-first Amendment and the Commerce Clause are parts of the same Constitution," and courts should consider "each in the light of the other." *Id.* As the Court emphasized in *Midcal*, 445 U.S. at 109, the judicial task in this area is a "pragmatic effort to harmonize state and federal powers"; not to excise one constitutional provision to the aggrandizement of the other.

In defiance of the command to accord dignity to both the Commerce Clause and 21st Amendment, the Second Circuit substituted a kind of constitutional one-stop shopping, concluding that New York's direct shipment ban falls within the powers conferred by the 21st Amendment and therefore that it was "exempted" from the Commerce Clause (Pet. App. 16a-29a).[26] Such an approach, according plenary weight to section 2 of the 21st Amendment, nullifies the dormant Commerce Clause, for in the context of alcohol distribution it would preclude nothing that the state might do, including naked economic protectionism. As such a result is starkly contrary to the rule of *Bacchus* and this Court's other precedents harmonizing the two provisions, the Court should examine the New York regulatory scheme in light of both constitutional provisions, not just one.

Respondents, by contrast, contend that striking down protectionist direct shipment bans would eviscerate the 21st Amendment. Hardly: such a ruling would disturb but little the state's broad regulatory powers over alcohol distribution. Consider the many legislative alternatives available to New York that it bypassed in favor of its discriminatory direct shipment ban:

- The State may, of course, prohibit the sale of alcohol altogether.

[26] By contrast, the district court carefully analyzed the direct shipment ban under both the Commerce Clause and the 21st Amendment (Pet. App. 51a-64a).

• If it were serious about exercising regulatory control, New York could, like several other states, assume direct control through a state system of alcohol distribution outlets.

• The State could require that *all* wine, not just wine delivered from out-of-state wineries, pass through the three-tier system, and/or be subjected to whatever nondiscriminatory regulations it deems appropriate.[27]

• The State could, like other states, create a permit system that would allow direct interstate shipment of wine subject to whatever nondiscriminatory conditions the state might deem appropriate, such as a permit requirement, reasonable fees, taxation, and protections against sales to minors.[28]

All of these policy choices pass muster under the Commerce Clause. It is only because New York bypassed such choices and instead embraced a discriminatory distribution system that its actions are constitutionally suspect. It took one fatal step too far, going beyond even-handed regulation to discriminatory regulation – an act that "eliminates the immunity afforded by the Twenty-first Amendment." *Healy,* 491 U.S. at 344 (Scalia, J., concurring). Such a policy choice in light of nondiscriminatory alternatives reveals the State's protectionist motivations.

[27] *See, e.g.*, *Bridenbaugh v. Freeman-Wilson,* 227 F.3d 848, 853 (7th Cir. 2000), *cert. denied*, 532 U.S. 1002 (2001) (the state "insists that every drop of liquor pass through its three-tiered system").

[28] New York law authorizes the state respondents to create such a permit system, *see* ABC Laws §105-9 (Pet. App. 98a), but respondents have so far chosen not to exercise that discretion.

Because the Second Circuit failed to apply strict scrutiny, or really any meaningful Commerce Clause scrutiny at all, the Second Circuit truncated two essential parts of the State's burden under strict scrutiny: articulating an important state interest and demonstrating that no less-burdensome alternatives could serve those interests. *See, e.g.*, *Hughes*, 441 U.S. at 337; *Hunt*, 432 U.S. at 353. As will appear, the State's defenses are pretextual and cannot satisfy strict scrutiny.

1. What is the legitimate goal that the State seeks to serve with its in-state premises requirement? Purportedly, the court of appeals inferred, to "ensure accountability" (Pet. App. 28a).[29] After all, "[r]equiring New York officials to traverse the country to ensure that direct sales to consumers (no matter how small) comply with New York law would render the regulatory scheme useless" (Pet. App. 28a).

Such a justification for discriminatory trade barriers was expressly rejected in *Dean Milk*, 340 U.S. at 354-35. Regardless, the underlying premise isn't so: "physical presence," in terms of a bricks-and-mortar business establishment, simply is not necessary to establish accountability to the state. The state has available to it far less-burdensome regulatory mechanisms to ensure accountability.

First, the Tax and Trade Bureau (formerly BATF) has authority to revoke a winery's license if it violates state alcohol control laws (BATF Industry Circular 96-3; J.A.

[29] Respondents also cite "orderly market conditions," which the 7th Circuit characterized as "a euphemism for reducing competition and facilitating tax collection." *Bridenbaugh*, 227 F.3d at 851.

196-97; 2d Cir. J.A. 3581-82). In other words, just like New York wineries, out-of-state wineries are subject to severe penalties if they violate New York laws. Moreover, the 21st Amendment Enforcement Act, 27 U.S.C. §122a (Pet. App. 76a), solved the conundrum voiced by the appeals court, investing in state attorneys general the power to seek injunctions against unlawful acts by out-of-state wineries in their own federal courts.[30] Taken together, those protections reflect an affirmative exercise of federal regulatory authority to satisfy state concerns and thereby implicitly remove any justification for protectionist state trade barriers.

The State overlooked the simplest, least restrictive, and most effective means of ensuring accountability: requiring a permit as a condition of direct interstate shipping. Such an effort would put out-of-state and domestic wineries on the same footing: to borrow the appeals court's phraseology, it would make both licensed by and accountable to the State. The State Liquor Authority already possesses authority to issue such permits (*see* ABC Laws §105-9 (Pet. App. 98a)), but has chosen not to exercise it. The State cannot be heard to say, as the Second Circuit found (Pet. App. 25a-28a), that there really is a level regulatory playing field because all wineries that ship directly to consumers must be licensed by and accountable to the state – and then defeat the Commerce

[30] In subsection (e), Congress noted that this authority extends only to the enforcement of laws that reflect "a valid exercise of power vested in the States – (1) under the twenty-first . . . amendment to the Constitution . . . as such . . . amendment is interpreted by the Supreme Court of the United States including interpretations in conjunction with other provisions of the Constitution." 27 U.S.C. §122a(e).

Clause merely by choosing not to make such a permit available.

Such a permit is precisely the means employed by states that permit and regulate direct interstate shipping; and those states report that such methods fully satisfy legitimate state regulatory interests. FTC Report at 26-40.

Such evenhanded regulation serves the State's interests under the 21st Amendment even as it promotes the values underlying the Commerce Clause. As the FTC has found in the specific context of New York (*see* FTC Letter, *supra*), a permit system allowing direct interstate wine shipments would benefit wine producers and consumers, while satisfying legitimate State concerns.

2. Taxation, along with protectionism, unquestionably was on the mind of the legislators who tightened the vice-grip on direct interstate wine shipments in 1970 and when Gov. Pataki vetoed reform legislation in 1995. But is a constitutional maxim that "revenue generation is not a local interest that can justify discrimination against interstate commerce." *C&A Carbone*, 511 U.S. at 393.

Respondents have made completely contradictory arguments in this regard. They insist on the one hand that taxation is a "core concern" under the 21st Amendment, *see North Dakota v. United States,* 495 U.S. 423 (1990); and on the other that states are somehow not allowed to tax direct interstate shipments of alcohol. Those assertions can't both be true: either taxation is a core concern, and therefore the State *can* tax direct interstate shipments of alcohol pursuant to their 21st Amendment powers; or it is not and the State cannot. It is absurd to argue, as respondents do, that the 21st Amendment encompasses the broader power of discriminatory trade barriers, but not the lesser power of equal taxation.

Whether or not the State possesses the tax power, it is plain that what the State cannot do is to discriminate. *See Bacchus*, 468 U.S. at 270; *North Dakota*, 495 U.S. at 448 (Scalia, J., concurring) ("That is not to say, of course, that the State may enact regulations that discriminate"). "States have broad discretion to configure their systems of taxation as they deem appropriate. All we intimate here is that their discretion in this regard, as in all others, is bounded by any relevant limitations of the Federal Constitution, in these cases the negative Commerce Clause." *Oregon Waste*, 511 U.S. at 108 (citations omitted).

But the fact is that several states *do* tax direct interstate wine shipments. *See, e.g.*, La. Rev. Stat. Ann. §26:359(B)(1); N.H. Rev. Stats. Ann. §178:14-a(V); Nev. Rev. Stat. Ann. §369.462. Wineries that engage in direct shipping remit taxes to states that require them (J.A. 46-47; 2d Cir. J.A. 3596). The FTC reports that states are successfully collecting taxes on direct wine shipments. FTC Report at 38-40. Indeed, far from taxation providing a rationale for forbidding direct interstate shipping, states may find that they are *losing* tax revenues by such protectionist policies.[31] At bottom, while revenue interests plainly can serve as a justification for state regulation, they cannot serve as an excuse for discrimination; or to avoid less-burdensome alternatives, such as those that other states have adopted

[31] Indeed, that appears to be the reason for the about-face by Gov. George Pataki, who vetoed a 1995 bill authorizing direct shipping based in part on tax revenue concerns; but eight years later, now supports such legislation, citing the prospect of increased tax revenues. *See* Wax, "State Foresees $3M Yearly in Wine Bill," *Newsday* (Jan. 23, 2004).

to the betterment of producers, consumers, and the states themselves.

3. We expect that the Court will be flooded with good-faith *amicus* briefs raising concerns about underage access to alcohol. With such concerns we strongly empathize. But we urge the Court to focus on the *legal* issues evoked by the deployment of a discriminatory regime ostensibly to serve legitimate purposes; to wit, whether the proffered reason actually motivated the legislature and whether less-burdensome alternatives exist. If the Court does so, it will see why not a single standing court decision has credited temperance concerns as a legitimate justification for discriminatory direct shipment bans, and why the district court below likewise rejected it (Pet. App. 58a).

Respondents cannot meet their burden here for three independent reasons: (1) no evidence exists that direct shipping would exacerbate the problem of underage drinking; (2) the same concerns would apply to in-state direct shipping, so that differential treatment of the two renders the defense pretextual; and (3) less-burdensome means exist to serve the state's professed interests.

The entire legislative history of the 1970 law tightening direct interstate shipment access and the 1995 legislation that would have lifted the ban lacks virtually any reference to concern over underage drinking. (2d Cir. J.A. 367-436, 437-536).

The reason, as the FTC Report at 26-38 makes clear, is that underage access through direct shipping is not a problem in the states that permit (and regulate) it.[32] That is because while direct shipping efficiently serves the interests of adult wine enthusiasts who want to find a particular wine that they enjoy, it is a very clumsy and inefficient way for minors to obtain alcohol, particularly in light of (unfortunately) abundant alternatives. Young drinkers prefer beer and wine coolers, not premium wine (2d Cir. J.A. 2914-18, 2920-21, 2923-26, 2967-68, 3037-38, 3049, 3055-57); and they can obtain it easily with fake IDs or by having adult friends purchase it. For wine ordered by telephone or over the Internet, by contrast, customers must produce an adult identification at time of purchase. They must order it with a credit card. They must wait an unspecified period of time for delivery. The package is marked to require adult identification upon delivery (thereby creating a second identification checkpoint). And the young person would have to be home without a parent (or the college campus would have to

[32] Apart from the FTC report, which surveyed and heard testimony from enforcement officials and found no problem with underage access in direct shipment states, there is *no* study examining effects of direct shipping on underage access. Widely reported sting operations have taken place in states that *forbid* direct interstate shipping, thereby not testing enforcement methods of states that allow and regulate it. A National Academy of Sciences study that reported widespread use of the Internet by minors to order alcohol relied on a study that, in fact, related entirely to minors ordering alcohol from *liquor stores*; i.e., through the three-tier system. *See* Bonnie and O'Connell, eds., *Reducing Underage Drinking: A Collective Responsibility* (2004) at 174; Fletcher, et al., "Alcohol Home Delivery Services: A Source of Alcohol for Underage Drinkers," 61 *J. Studies Alcohol* 81 (2000). Respondents often cite to a study showing greater wine consumption in states with more permissive alcohol laws – as if there is something wrongful in itself about wine consumption. Correlation does not equal causation – and no studies that respondents have produced (including reports by their own expert witnesses) have examined, much less established, any direct link between direct shipping and underage access. By contrast, in terms of underage access, the three-tier system leaks like a sieve.

permit delivery) in order to complete the transaction. These are industry standards that have been adopted in many jurisdictions (J.A. 44; 2d Cir. J.A. 3529-32, 3581, 3596).

In New York, the statistics of record are glaringly clear: 16,000 and zero. The first is the number of reported instances of underage access through the three-tier system over a five-year period; the second is the number of reported instances of underage access through direct shipping outside the sting context during the same period (2d Cir. J.A. 537-38).

Moreover, the State's concerns about underage access through direct shipping ring hollow when one examines the regulatory treatment of in-state wineries engaged in direct shipping, which in its full sweep and scope amounts to *none whatsoever* (J.A. 43-44). By contrast, the vetoed 1995 direct interstate shipping bill would have required safeguards against underage access (2d Cir. J.A. 449-53).

The same regulatory concerns with regard to underage access should apply to in-state and out-of-state wineries. Even absent state regulation, a winery can lose its federal license, and its ability to operate at all, if it violates state laws (BATF Industry Circular; J.A. 196-97; 2d Cir. J.A. 3581-82). In light of the existence of less-burdensome alternatives (recognized even by the New York Legislature in 1995) when it attempted to allow limited and regulated interstate direct shipping, the State cannot explain why it needs to erect a discriminatory trade barrier in order to serve its legitimate objectives. It cannot do so because its true objective was protectionism. However laudable the ostensible goal, it cannot provide cover for the real one.

CONCLUSION

By a decision in favor of Mrs. Swedenburg and her fellow petitioners, this Court will reaffirm that the founding principles of our nation – especially the guarantee of free trade among the states – will continue to resonate in the Internet era. Though technology has made so much possible, it is still small craftspersons like Mrs. Swedenburg, along with their customers, who benefit most from the wisdom of the Framers enshrined in our Constitution. Protectionist schemes never disappear; but they will be held in check only if the Court binds states to their legitimate authority.

For the foregoing reasons, petitioners respectfully request that the Court reverse the decision of the Court of Appeals and remand the case to the District Court for implementation of its original Order.

Respectfully submitted,

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