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Supreme Court Hears Oral Arguments in NY and MI Cases - My Analysis

Last Tuesday, the Supreme Court heard arguments in the appeals of the NY and Michigan decisions. A decision should be handed down sometime this coming spring.

Arguing for the NY plaintiffs was Clint Bolick (Bolick) of the Institute for Justice. Representing the MI plaintiffs was Stanford professor Kathleen Sullivan (Sullivan). Defending the MI laws was Solicitor General Thomas Casey (Casey), with NY Solicitor General Caitlin Halligan (Halligan) supporting NY's laws.

The Post-Argument Media:

I would initially note that many of the analyses you have probably read concerning the oral argument need to be taken with a grain of salt - for a couple of reasons.

First, it has become clear over the past five years that I have dealt with this issue that the media is largely ignorant of the history of alcohol control in the United States, the scope of power granted states by the 21st Amendment, and the nature of and need for the complicated regulatory systems employed by the states in controlling the distribution of alcohol. Nor is there a desire by most in the media to see beyond the simplistic issue of rare wine sales to oenophiles and understand the potentially destructive consequences to alcohol control in this country if the legal framework espoused by the plaintiffs in these cases prevails, a danger Justice Kennedy obviously recognized from the first question from the bench.

Second, the order of the argument contributed to certain misconceptions and misperceptions about what actually occurred. The plaintiffs in the cases went first, and faced a torrent of criticism concerning the underpinnings of their legal arguments, their understanding of the history of the 21st Amendment, and the scope of the relief they were seeking. If you were to have seen just that portion of the argument, you would have come to the conclusion that the case was over and that the states would easily prevail. However, the states went second and faced their own series of difficult questions. As a result, much of the criticism of the plaintiffs' argument was forgotten or omitted by the media which emphasized the latter period of questioning - questioning which was more consistent with the prevailing media bias. But as you will see from my legal analysis below, those questions - which voiced the concerns of the justices who asked them - and the answers given by counsel for the plaintiffs - will in the end make it very difficult for the plaintiffs to obtain a decision to their liking.

Summary of the Arguments:

The basic premise put forward by the plaintiffs in these cases is that while the 21st Amendment did to some degree shield states from the scrutiny of the "dormant

commerce clause," it did not delete pre-21st Amendment jurisprudence which disallowed "discrimination" by the states in structuring their regulatory systems. The plaintiffs rely predominantly on *Bacchus*, a 1984 case dealing with Hawaii's tax treatment which favored a locally produced wine, which held that "[t]he central purpose of the provision (Section 2 of the 21st Amendment) was not to empower States to favor local liquor industries by erecting barriers to competition. It is also beyond doubt that the Commerce Clause itself furthers strong federal interests in preventing economic Balkanization. . . State laws that constitute mere economic protectionism are therefore not entitled to the same deference as laws enacted to combat the perceived evils of an unrestricted traffic in liquor. Here, 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." (parenthetical supplied).

The states and wholesaler intervenors counter that the 21st Amendment was designed to overcome commerce clause challenges which had stymied their efforts to control imports until just prior to Prohibition (the Webb-Kenyon Act, upon which the 21st Amendment was modeled, was upheld by the Supreme Court in 1917 - just prior to the institution of Prohibition), that its very words supply the power to control imports as states have done, that *Bacchus* is inapposite since it did not deal with importation control but with a tax, that bans on direct shipment are entitled to deference since they are designed to "combat the perceived evils of an unrestricted traffic in liquor," and that the evidence in the cases demonstrates that the laws in question are not "mere economic protectionism."

Bolick's Argument:

One of the biggest concerns voiced by wholesalers and the states arising out of this litigation is that the legal framework promoted by the plaintiffs is very broad and that virtually no import control now existing could withstand scrutiny were the courts to accept that perspective. Justice Kennedy, the first of the justices to ask a question, immediately recognized that issue.

He asked Bolick whether the entire three-tier licensing system would necessarily be rendered invalid under his interpretation. He asked specifically why a NJ wholesaler could not sell to NY retailers, or vice versa, if such import controls/distinctions were invalid. Bolick argued, unpersuasively, that this issue was limited to wine. I say unpersuasively because Justice Kennedy obviously was not satisfied with his answer and later raised this same point right out of the gates with Kathleen Sullivan noting that while it was a "narrow issue" being litigated, the plaintiffs were asking for a "sweeping rationale" and he was unclear how the three-tier system survives under that rationale.

Justice Breyer followed Justice Kennedy's initial questions with something of an historical recitation wherein he seemed to take the position that Bolick's position concerning the viability of discrimination claims was put down by the Court's decision (Justice Brandeis writing for the majority) in the *Young's Market* case in 1936, where it held that states need not treat importers and domestic industry in the same manner and that to argue to the contrary would be to rewrite the 21st Amendment.

Justice Ginsburg was equally critical of Bolick's assessment of the legislative history

of the Webb-Kenyon Act and the 21st Amendment, noting that Congress could have put into the Act or the Amendment the non-discriminatory language Bolick argued survived the passage/ratification of those laws, but it chose not to do so. Justice Souter asked Bolick whether Congress had drafted and later dropped anti-discrimination language from Webb-Kenyon, as it obviously was not present in that statute. Bolick argued that it would have been redundant to include it but could not answer the question directly.

Justice Kennedy then delved into the issue of tax revenue that the states would lose, both excise taxes and sales tax, if the plaintiffs were to prevail. He noted the *Quill* case and asked how states could require that such taxes be paid in light of that decision. Bolick responded that the taxes could be collected as a condition of a permit.

Justice Souter followed with practical regulatory concerns. He wondered how states could audit compliance without great expense and without the ability to drop in unexpectedly - something that would be impossible across the country. Bolick argued that online compliance checks were sufficient and feasible. Justice Scalia then asked whether the federal government policed compliance with state tax laws and Justice Kennedy asked if such audits by the feds were routine, to which Bolick replied that they did and they were. Of course that is not quite the case. While wineries are subject to the loss of their federal permit if found to have violated state laws concerning the remittance of state taxes, the TTB does not regularly check such records and is more concerned with the payment of federal taxes and fees.

Justice Ginsburg closed out the questioning of Bolick by wondering whether the rationale put forward by the plaintiffs would allow the shipment of alcoholic beverages other than wine. Bolick tried to argue that these cases are limited to wine, but of course the constitution speaks to alcohol and later admissions by Sullivan belied that argument.

Sullivan's Argument:

As noted previously, Justice Kennedy immediately raised the issue of the "sweeping rationale" being sought by the plaintiffs with Sullivan, just as he had with Bolick, noting that virtually any import regulation would be invalid under their interpretation.

Justice Ginsburg, exploring the nature of the relief being sought by the plaintiffs asked whether simply taking away the in-state direct shipping complained of would give them nothing to complain about. Sullivan agreed, but argued that the better result would be to open the market to all comers.

Justice Stevens, echoing Justice Brandeis' decision in *Young's Market*, asked her if Michigan could bar all out-of-state wine, even assuming the only reason were to give a monopoly to local producers. She said no, but Justice Breyer asserted that since Section 2 of the 21st Amendment was meant to end that part of the dormant commerce clause that allows foreign suppliers to be treated better than domestic suppliers, and since the dormant commerce clause was an implication of the commerce clause, if the 21st Amendment did not speak to discrimination, then the dormant commerce clause doesn't apply. "You can't divide the dormant commerce clause into six parts," he explained.

Sullivan did not argue that point, but instead argued that case law since the passage of

the 21st Amendment had superseded that interpretation - essentially saying that the Court had over time written opinions which overturned the original intent and meaning of the 21st Amendment. But Justice Stevens disagreed with her reading of those cases, reminding her that the cases she cited, such as *Boren*, dealt with other constitutional challenges, not challenges under the commerce clause. He asked Sullivan whether Congress could empower states to do what they had done here and she answered yes, but that it had not done so.

Justice Souter, noting the states' argument that this case was different than *Bacchus*, that there was a substantial need for differential treatment, asked what standard should be applied. Sullivan argued that the states must meet a "strict scrutiny" standard and that they could not do so in this case since there were less restrictive alternatives available to the state to ameliorate their concerns. Justice Souter countered that states don't want to travel to other states to enforce their laws and Justice Kennedy asked whether that meant that Michigan must allow out-of-state shipments directly to consumers. Sullivan argued that with a permit system conditioned on tax payments and online compliance checks, the states could achieve a satisfactory level of enforcement.

In another swipe at the sweeping rationale asserted by plaintiffs, Justice Kennedy asked Sullivan whether the reciprocity laws, which restrict direct shipments to consumers to only those in participating states, must also be found invalid. Sullivan hedged saying "possibly," but Justice Stevens seemed incredulous noting that she had to concede that the reciprocity laws are unconstitutional under her interpretation given that under the heightened scrutiny she was recommending, it would be virtually impossible to defend them. Justice Stevens closed out her argument adding that such a result was a "necessary consequence of your rationale."

Casey's Argument:

Justice O'Connor, who had remained silent during the grilling of the plaintiffs' counsel, asked the first question of Casey. It should be noted that O'Connor, Rehnquist and Stevens dissented in the *Bacchus* case, and that they are the only three members of the court still on the bench from the time of that decision. Thus, given their view in that case that the 21st Amendment trumped the dormant commerce clause and allowed discriminatory burdens on interstate commerce, those three justices are viewed as the core of those who would be expected to uphold the NY and MI laws. So when she noted the difficulty in overturning a precedent such as *Bacchus*, and pronounced her opinion that it "cut against the state to some extent," she was undoubtedly looking for Casey to enunciate clearly why it should not apply to the cases at bar. Justices Kennedy and Ginsburg also noted that the language of *Bacchus* seemed to "restore" the anti-discrimination principles of the dormant commerce clause to the 21st Amendment.

Although Casey noted that *Bacchus* spoke to "mere economic protectionism," and that the MI and NY laws were supported by other legitimate concerns of the 21st Amendment including temperance, Casey was less than effective in reciting the evidence in the record in both the NY and MI cases which supported that position, merely noting that there were "affidavits and interrogatories" in the record which spoke to those concerns. Because of that failing, Justice Souter pursued the issue further, asking whether there was sufficient evidence in the case for the Court to rule, and that lacking that evidence, should the court send it back for further evidence gathering. Casey's response wandered into the procedural aspects of the earlier

proceedings.

Justice Kennedy observed that if the dormant commerce clause applied to liquor distribution as *Bacchus* implied, that would create a substantial burden for the states to justify those laws, whether strict scrutiny or some other heightened level of scrutiny. Justice Scalia followed this point by instructing Casey that the burden was his and that he needed to tell them what the evidence was supporting his position. At that point Casey mentioned the stings MI had pursued.

At this point, Breyer appeared to contradict his earlier perspective, arguing that perhaps Section 2 of the 21st Amendment did not eliminate the pre-Wilson Act anti-discrimination prohibition and Justice Kennedy asked what evidence there was that it did. Casey correctly noted that the Webb-Kenyon Act was entitled "An Act Divesting Alcohol of its Interstate Character in Certain Cases," to make the point that it was the intent of Congress to override the dormant commerce clause - and thus the anti-discrimination principles inherent in that doctrine - in that legislation and in the constitutional amendment modeled after that act.

Justice Ginsburg did not question that history, but did feel that Casey was asking to court to reject *Bacchus* outright and rule that alcohol was an exception to the normal operation of the dormant commerce clause - that the 21st Amendment trumped it. Justice Kennedy asked if one of the purposes of the 21st Amendment was to allow for discrimination and Casey answered it was, but O'Connor ended Casey's argument questioning what to make of *Bacchus*, just as she had at the beginning.

Halligan's Argument:

Halligan began by noting that the 21st Amendment expressed a consensus that alcohol was different and thus needed to be treated differently. Justice Kennedy asked her if that meant that she was taking the position that even "mere protectionism" was sufficient to justify the sale of only NY wines, in a reference to the wording of the *Bacchus* case; in other words, was the state taking the position that *Bacchus* was a bad decision and that the dissent in that case had the correct view. Halligan did not address that point directly, indicating that the justifications of the NY and MI laws were valid even in light of *Bacchus*.

Justice Souter addressed the issues of compliance with Halligan, asking her about NY's enforcement efforts and whether those efforts could be effectuated through an online compliance system. Justice Ginsburg asked what merely having an office in NY did for enforcement purposes, and Halligan explained that it was more than just an office, that the product would have to be present in that location and available for inspection.

Justice Scalia was plainly skeptical of NY's argument that it was impossible to enforce against out-of-state licensees as they could against in-state licensee, and Justice Ginsburg questioned why other states which allowed direct shipment did not have such concerns. Halligan made the point that she could not speak for other states, but that simply because other states did not concern themselves with accountability to the extent NY did, that did not make NY's concerns less valid.

Justice Scalia wondered whether there should be a greater level of scrutiny if discrimination were found, but Halligan pointed out that the Court's *North Dakota* decision, which came after *Bacchus*, found that the mere "risk of diversion" was

enough to sustain that state's increased burden on out-of-state suppliers and that the case at bar was no different in that respect.

Justice Stevens noted that if the Court were to apply *Bacchus*, where in-state tax exemptions were prohibited, it would be difficult to sustain the NY laws. But Halligan noted that *Bacchus* was distinguishable in several ways from the cases before the Court, not least of which was that the very language of the 21st Amendment speaks to state control over importation, an issue which was not at stake in *Bacchus*.

Bolick's Rebuttal:

Bolick used his rebuttal time to make an essentially political/equitable argument, talking, inter alia, about the power imbalance between wholesalers and small wineries and the merits of the FTC report. In the course of that argument, Bolick incorrectly stated that there were only 600 wines in distribution in New York when in fact the record shows that over 19,000 brands are actually in distribution. Unfortunately, the format of the arguments did not allow for rebuttal of that misstatement.

But Justice Stevens ended the session by saying that in the end the question really comes down to whether the 21st Amendment allows the disparate treatment the plaintiffs were complaining about.

Legal Analysis/Prediction:

Trying to make a prediction about the outcome of any case before the Supreme Court is a perilous proposition. Nonetheless, I will give it a shot.

Given the dissent by Justices Stevens, Rehnquist and O'Connor in the *Bacchus* decision, it seems likely to me that they will try to defend the NY and MI laws by either trying to overturn that decision or by trying to distinguish these cases from *Bacchus*. While O'Connor did question the states about the implications of *Bacchus*, it is unlikely that she will change her personal view of the 21st Amendment. Her questions about how she and other justices could differentiate that case from the current cases supports the conclusion that she was trying to win over those who would not necessarily vote to overturn *Bacchus*, but understanding the threat imposed by the plaintiffs' interpretation, would need to find a way around *Bacchus* to avoid joining an opinion creating anarchy in the alcohol distribution system.

The *Bacchus* dissent presumably gives the states/intervenors a core of three strong justices to make the case for upholding their laws. Justice Rehnquist's health has been an issue, but the Supreme Court announced yesterday that although his participation in the November cases would be limited, he would be participating fully in the December cases - which includes the alcohol cases. As such, and given his intention to swear in the President at inauguration, it appears that Chief Justice Rehnquist is doing better than previously thought, and that he will be a factor in these cases. The question then becomes who joins with them.

Justice Thomas did not ask any questions, as is his wont. But some aspects of his record lead me to believe he could easily join with Rehnquist, Stevens and O'Connor. First, Justice Thomas has gone on the record criticizing the "dormant commerce clause" as a judicial construct not within the four corners of the constitution. Moreover, he is a social conservative and will be receptive to the argument that easier

access to alcohol with less of an ability to enforce state law regulating its flow is not a good thing. Being a textualist, he will be more likely to find that the actual words of the 21st Amendment mean what they say.

Breyer is a possible joiner because his questioning reflected his understanding that the dormant commerce clause was overridden by the passage of the 21st Amendment and because, although he was concerned about the *Bacchus* language, his historical perspective seems to be towards a stronger interpretation of the powers given states by the 21st Amendment. Moreover, while he was troubled by the *Bacchus* decision, if he truly believes that the dormant commerce clause was trumped by the 21st Amendment, he will have to put precedent over principal to sustain the challenges to the state laws since one can only find discrimination if the dormant commerce clause is relevant. His saying that you can't break the dormant commerce clause into six pieces was perhaps his way of saying the *Bacchus* case was not decided correctly.

Justice Souter could easily join with Rehnquist, Stevens and O'Connor as he seemed to understand there was an important difference between local control and out-of-state control. This would allow him to distinguish *Bacchus*, assuming he doesn't get caught up in second guessing state decisions concerning importation and gives them the deference they deserve, even under *Bacchus*, and certainly under *North Dakota*.

Justice Ginsburg implied that the 21st Amendment did not incorporate anti-discrimination language and that indicated a legislative decision to override such concerns. Like Breyer, she seemed to feel that it is not the constitution which causes the problem for the states, but rather the Court's latter day interpretation of the 21st Amendment in the *Bacchus* case.

Justice Scalia has always been a problematic vote, as he disfavors any type of differential treatment. But he is a strong textualist and federalist and may find it difficult overcoming the direct language of the 21st Amendment. And because of that conflict, I believe it unlikely that he will be at the forefront of an effort to form a majority opinion which would have the effect of essentially nullifying a clearly "enumerated power" of the states.

In the end, it may come down to thinking of Justice Kennedy. Kennedy clearly understands the damage to the orderly distribution of alcohol that the plaintiffs' legal argument would entail. His questioning reflects that the result the plaintiffs want would destroy the state licensing system. But he is also concerned about whether the *Bacchus* case controls here. It seems to me his ultimate decision will depend on whether he is more concerned about the breakdown of the system or if he feels bound by what I believe to be easily distinguishable dicta in *Bacchus*. If he goes with Rehnquist, Stevens and O'Connor, it is likely that he will bring others with him given his understanding of the issue and his leadership on the Court. This is the most probable result in my estimation, and should that occur, you will see the states prevail.

However, because Kennedy understands the issues surrounding alcohol distribution and clearly has an interest in them, I tend to believe he is the only one with *Bacchus* concerns that could also knit together a majority in favor of the plaintiffs. However, although that is a possibility, it is not a prospect the plaintiffs in these cases should wish for.

Why? Because if Justice Kennedy decides that the *Bacchus* case controls - that there

is no way to distinguish it - he will need to gather votes to oppose Rehnquist, Stevens and O'Connor, or to try to get them to join him. But because he clearly understands the dangers inherent in the "sweeping rationale" sought by the plaintiffs, it is unlikely that he would write an opinion which would lead to the very result he fears.

I have long argued that the plaintiffs should be careful what they ask for, because they might get it. In these cases, I think it is unlikely that the Court will give the plaintiffs the "sweeping rationale" they seek - assuming they prevail on the merits - because of the dangers understood and expressed so articulately by Justice Kennedy. Rather, the Court will be much more likely to seek to mute the effect of any such victory for the plaintiffs by playing on the comments of Justice Ginsburg – and the concession by Sullivan - that any discrimination complained of can be cured by simply removing the favoritism, in this case by knocking out the in-state exceptions which are easily severable.

While that decision would be quite disheartening for the plaintiffs, that would just be the beginning of their troubles. It would not be long before follow-on litigation would soon take all reciprocal laws off the books. As Justice Stevens noted, and as Sullivan basically conceded, reciprocal laws must invariably be found to be unconstitutional as well under the plaintiffs' interpretation.

If that occurs, the battle over unregulated and unaccountable direct shipments to consumers would revert to the state legislatures - where this battle should have been fought from the outset.

Until the next time . . .

Craig

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