

long as the State is "acting as a market participant, rather than as a market regulator."

Respondents are doing exactly what the market-participant doctrine says they cannot: While acting as market participants by operating a fee-for-service business enterprise in an area in which there is an established interstate market, respondents are also regulating that market in a discriminatory manner and claiming that their special governmental status somehow insulates them from a dormant Commerce Clause challenge.

The fallacy in the Court's approach can be illustrated by comparing a law that discriminates in favor of an in-state facility, owned by a corporation whose shares are publicly held, and a law discriminating in favor of an otherwise identical facility that is owned by the State or municipality. Those who are favored and disfavored by these two laws are essentially the same with one major exception: The law favoring the corporate facility presumably benefits the corporation's shareholders, most of whom are probably not local residents, whereas the law favoring the government-owned facility presumably benefits the people of the enacting State or municipality. I cannot understand why only the former law, and not the latter, should be regarded as a tool of economic protectionism. Nor do I think it is realistic or consistent with our precedents to condemn some discriminatory laws as protectionist while upholding other, equally discriminatory laws as lawful measures designed to serve legitimate local interests unrelated to protectionism.

For these reasons, I cannot accept the proposition that laws discriminating in favor of state-owned enterprises are so unlikely to be the product of economic protectionism that they should be exempt from the usual dormant Commerce Clause standards.

Thus, if the legislative means are themselves discriminatory, then regardless of how legitimate and nonprotectionist the underlying legislative goals may be, the legislation is subject to strict scrutiny. Similarly, the fact that a discriminatory law "may [in some sense] be directed toward any number of legitimate goals unrelated to protectionism" does not make the law nondiscriminatory. The existence of such goals is relevant, not to whether the law is discriminatory, but to whether the law can be allowed to stand even though it discriminates against interstate commerce. And even then, the existence of legitimate goals is not enough; discriminatory legislation can be upheld only where such goals cannot adequately be achieved through nondiscriminatory means.

Equally unpersuasive is the Court's suggestion that the flow-control laws do not discriminate against interstate commerce because they "treat in-state private business interests exactly the same as out-of-state ones." Again, the critical issue is whether the challenged legislation discriminates against interstate commerce. If it does, then regardless of whether those harmed by it reside entirely outside the State in question, the law is subject to strict scrutiny. Indeed, this Court has long recognized that "a burden imposed by a State upon interstate commerce is not to be sustained simply because the statute imposing

it applies alike to the people of all the States, including the people of the State enacting such statute."

The dormant Commerce Clause has long been understood to prohibit the kind of discriminatory legislation upheld by the Court in this case.

c. *Analysis if a Law Is Deemed Discriminatory (casebook, p. 411)*

GRANHOLM v. HEALD

544 U.S. 460 (2005)

Justice KENNEDY delivered the opinion of the Court.

These consolidated cases present challenges to state laws regulating the sale of wine from out-of-state wineries to consumers in Michigan and New York. The details and mechanics of the two regulatory schemes differ, but the object and effect of the laws are the same: to allow in-state wineries to sell wine directly to consumers in that State but to prohibit out-of-state wineries from doing so, or, at the least, to make direct sales impractical from an economic standpoint. It is evident that the object and design of the Michigan and New York statutes is to grant in-state wineries a competitive advantage over wineries located beyond the States' borders.

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

I

Like many other States, Michigan and New York regulate the sale and importation of alcoholic beverages, including wine, through a three-tier distribution system. Separate licenses are required for producers, wholesalers, and retailers. As relevant to today's cases, though, the three-tier system is, in broad terms and with refinements to be discussed, mandated by Michigan and New York only for sales from out-of-state wineries. In-state wineries, by contrast, can obtain a license for direct sales to consumers. The differential treatment between in-state and out-of-state wineries constitutes explicit discrimination against interstate commerce.

This discrimination substantially limits the direct sale of wine to consumers, an otherwise emerging and significant business. From 1994 to 1999, consumer spending on direct wine shipments doubled, reaching \$500 million per year, or three percent of all wine sales. The expansion has been influenced by several related trends. First, the number of small wineries in the United States has significantly increased. By some estimates there are over 3,000 wineries in the country. At the same time, the wholesale market has consolidated. Between 1984 and 2002, the number of licensed wholesalers dropped from 1,600 to 600. The increasing winery-to-wholesaler ratio means that many small wineries do

not produce enough wine or have sufficient consumer demand for their wine to make it economical for wholesalers to carry their products. This has led many small wineries to rely on direct shipping to reach new markets. Technological improvements, in particular the ability of wineries to sell wine over the Internet, have helped make direct shipments an attractive sales channel.

Approximately 26 States allow some direct shipping of wine, with various restrictions. Thirteen of these States have reciprocity laws, which allow direct shipment from wineries outside the State, provided the State of origin affords similar nondiscriminatory treatment. In many parts of the country, however, state laws that prohibit or severely restrict direct shipments deprive consumers of access to the direct market.

The wine producers in the cases before us are small wineries that rely on direct consumer sales as an important part of their businesses. Domaine Alfred, one of the plaintiffs in the Michigan suit, is a small winery located in San Luis Obispo, California. It produces 3,000 cases of wine per year. Domaine Alfred has received requests for its wine from Michigan consumers but cannot fill the orders because of the State's direct-shipment ban. Even if the winery could find a Michigan wholesaler to distribute its wine, the wholesaler's markup would render shipment through the three-tier system economically infeasible.

Under Michigan law, wine producers, as a general matter, must distribute their wine through wholesalers. There is, however, an exception for Michigan's approximately 40 in-state wineries, which are eligible for "wine maker" licenses that allow direct shipment to in-state consumers. Out-of-state wineries can apply for a \$300 "outside seller of wine" license, but this license only allows them to sell to in-state wholesalers.

New York's licensing scheme is somewhat different. It channels most wine sales through the three-tier system, but it too makes exceptions for in-state wineries. As in Michigan, the result is to allow local wineries to make direct sales to consumers in New York on terms not available to out-of-state wineries.

We consolidated these cases and granted certiorari on the following question: "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 § 2 of the Twenty-first Amendment?"

II

A

Time and again this Court has held that, in all but the narrowest circumstances, state laws violate the Commerce Clause if they mandate "differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter." This rule is essential to the foundations of the Union. The mere fact of nonresidence should not foreclose a producer in one State from access to markets in other States. States may not enact laws that burden out-of-state producers or shippers simply to give a competitive advantage to in-state

businesses. This mandate "reflect[s] 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 rule prohibiting state discrimination against interstate commerce follows also from the principle that States should not be compelled to negotiate with each other regarding favored or disfavored status for their own citizens. States do not need, and may not attempt, to negotiate with other States regarding their mutual economic interests. Rivalries among the States are thus kept to a minimum, and a proliferation of trade zones is prevented.

Laws of the type at issue in the instant cases contradict these principles. They deprive citizens of their right to have access to the markets of other States on equal terms. The perceived necessity for reciprocal sale privileges risks generating the trade rivalries and animosities, the alliances and exclusivity, that the Constitution and, in particular, the Commerce Clause were designed to avoid. The current patchwork of laws—with some States banning direct shipments altogether, others doing so only for out-of-state wines, and still others requiring reciprocity—is essentially the product of an ongoing, low-level trade war. Allowing States to discriminate against out-of-state wine "invite[s] a multiplication of preferential trade areas destructive of the very purpose of the Commerce Clause."

B

The discriminatory character of the Michigan system is obvious. Michigan allows in-state wineries to ship directly to consumers, subject only to a licensing requirement. Out-of-state wineries, whether licensed or not, face a complete ban on direct shipment. The differential treatment requires all out-of-state wine, but not all in-state wine, to pass through an in-state wholesaler and retailer before reaching consumers. These two extra layers of overhead increase the cost of out-of-state wines to Michigan consumers. The cost differential, and in some cases the inability to secure a wholesaler for small shipments, can effectively bar small wineries from the Michigan market.

The New York regulatory scheme differs from Michigan's in that it does not ban direct shipments altogether. Out-of-state wineries are instead required to establish a distribution operation in New York in order to gain the privilege of direct shipment. The New York scheme grants in-state wineries access to the State's consumers on preferential terms. The suggestion of a limited exception for direct shipment from out-of-state wineries does nothing to eliminate the discriminatory nature of New York's regulations. In-state producers, with the applicable licenses, can ship directly to consumers from their wineries. Out-of-state wineries must open a branch office and warehouse in New York, additional steps that drive up the cost of their wine. For most wineries, the expense of establishing a bricks-and-mortar distribution operation in 1 State, let alone all 50, is prohibitive. It comes as no surprise that not a single out-of-state winery has availed itself of New

York's direct-shipping privilege. We have "viewed with particular suspicion state statutes requiring business operations to be performed in the home State that could more efficiently be performed elsewhere." New York's in-state presence requirement runs contrary to our admonition that States cannot require an out-of-state firm "to become a resident in order to compete on equal terms."

III

State laws that discriminate against interstate commerce face "a virtually per se rule of invalidity." *Philadelphia v. New Jersey* (1978). The Michigan and New York laws by their own terms violate this proscription. The two States, however, contend their statutes are saved by § 2 of the Twenty-first Amendment, which provides: "The transportation or importation into any State, Territory, or possession of the United States for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited."

The States' position is inconsistent with our precedents and with the Twenty-first Amendment's history. Section 2 does not allow States to regulate the direct shipment of wine on terms that discriminate in favor of in-state producers.

A

Before 1919, the temperance movement fought to curb the sale of alcoholic beverages one State at a time. The movement made progress, and many States passed laws restricting or prohibiting the sale of alcohol. This Court upheld state laws banning the production and sale of alcoholic beverages, *Mugler v. Kansas* (1887), but was less solicitous of laws aimed at imports. In a series of cases before ratification of the Eighteenth Amendment the Court, relying on the Commerce Clause, invalidated a number of state liquor regulations.

These cases advanced two distinct principles. First, the Court held that the Commerce Clause prevented States from discriminating against imported liquor. Second, the Court held that the Commerce Clause prevented States from passing facially neutral laws that placed an impermissible burden on interstate commerce.

B

The ratification of the Eighteenth Amendment in 1919 provided a brief respite from the legal battles over the validity of state liquor regulations. With the ratification of the Twenty-first Amendment 14 years later, however, nationwide Prohibition came to an end. Section 1 of the Twenty-first Amendment repealed the Eighteenth Amendment. Section 2 of the Twenty-first Amendment is at issue here. Michigan and New York say the provision grants to the States the authority to discriminate against out-of-state goods. The history we have recited does not support this position. To the contrary, it provides strong support for the view that

§ 2 restored to the States the powers they had. The aim of the Twenty-first Amendment was to allow States to maintain an effective and uniform system for controlling liquor by regulating its transportation, importation, and use. The Amendment did not give States the authority to pass nonuniform laws in order to discriminate against out-of-state goods, a privilege they had not enjoyed at any earlier time. Our more recent cases, furthermore, confirm that the Twenty-first Amendment does not supersede other provisions of the Constitution and, in particular, does not displace the rule that States may not give a discriminatory preference to their own producers.

C

The modern § 2 cases fall into three categories. First, the Court has held that state laws that violate other provisions of the Constitution are not saved by the Twenty-first Amendment. The Court has applied this rule in the context of the First Amendment, *44 Liquormart, Inc. v. Rhode Island* (1996); the Establishment Clause, *Larkin v. Grendel's Den, Inc.* (1982); the Equal Protection Clause, *Craig v. Boren* (1976); the Due Process Clause, *Wisconsin v. Constantineau* (1971); and the Import-Export Clause, *Department of Revenue v. James B. Beam Distilling Co.* (1964).

Second, the Court has held that § 2 does not abrogate Congress' Commerce Clause powers with regard to liquor. The argument that "the Twenty-first Amendment has somehow operated to 'repeal' the Commerce Clause" for alcoholic beverages has been rejected.

Finally, and most relevant to the issue at hand, the Court has held that state regulation of alcohol is limited by the nondiscrimination principle of the Commerce Clause. "When a state statute directly regulates or discriminates against interstate commerce, or when its effect is to favor in-state economic interests over out-of-state interests, we have generally struck down the statute without further inquiry."

IV

Our determination that the Michigan and New York direct-shipment laws are not authorized by the Twenty-first Amendment does not end the inquiry. We still must consider whether either State regime "advances a legitimate local purpose that cannot be adequately served by reasonable nondiscriminatory alternatives." The States offer two primary justifications for restricting direct shipments from out-of-state wineries: keeping alcohol out of the hands of minors and facilitating tax collection. We consider each in turn.

The States, aided by several amici, claim that allowing direct shipment from out-of-state wineries undermines their ability to police underage drinking. Minors, the States argue, have easy access to credit cards and the Internet and are likely to take advantage of direct wine shipments as a means of obtaining

alcohol illegally. The States provide little evidence that the purchase of wine over the Internet by minors is a problem. Indeed, there is some evidence to the contrary. A recent study by the staff of the FTC found that the 26 States currently allowing direct shipments report no problems with minors' increased access to wine. This is not surprising for several reasons. First, minors are less likely to consume wine, as opposed to beer, wine coolers, and hard liquor. Second, minors who decide to disobey the law have more direct means of doing so. Third, direct shipping is an imperfect avenue of obtaining alcohol for minors who, in the words of the past president of the National Conference of State Liquor Administrators, "'want instant gratification.'" Without concrete evidence that direct shipping of wine is likely to increase alcohol consumption by minors, we are left with the States' unsupported assertions. Under our precedents, which require the "clearest showing" to justify discriminatory state regulation, this is not enough.

Even were we to credit the States' largely unsupported claim that direct shipping of wine increases the risk of underage drinking, this would not justify regulations limiting only out-of-state direct shipments. As the wineries point out, minors are just as likely to order wine from in-state producers as from out-of-state ones.

The States' tax-collection justification is also insufficient. Increased direct shipping, whether originating in state or out of state, brings with it the potential for tax evasion. With regard to Michigan, however, the tax-collection argument is a diversion. That is because Michigan, unlike many other States, does not rely on wholesalers to collect taxes on wines imported from out-of-state. Instead, Michigan collects taxes directly from out-of-state wineries on all wine shipped to in-state wholesalers. If licensing and self-reporting provide adequate safeguards for wine distributed through the three-tier system, there is no reason to believe they will not suffice for direct shipments.

New York and its supporting parties also advance a tax-collection justification for the State's direct-shipment laws. In particular, New York could protect itself against lost tax revenue by requiring a permit as a condition of direct shipping. This is the approach taken by New York for in-state wineries. The State offers no reason to believe the system would prove ineffective for out-of-state wineries. Licensees could be required to submit regular sales reports and to remit taxes. Indeed, various States use this approach for taxing direct interstate wine shipments, and report no problems with tax collection.

In summary, the States provide little concrete evidence for the sweeping assertion that they cannot police direct shipments by out-of-state wineries. Our Commerce Clause cases demand more than mere speculation to support discrimination against out-of-state goods. The "burden is on the State to show that 'the discrimination is demonstrably justified.'" The Court has upheld state regulations that discriminate against interstate commerce only after finding, based on concrete record evidence, that a State's nondiscriminatory alternatives will prove unworkable. See, e.g., *Maine v. Taylor* (1986). Michigan and New York have not satisfied this exacting standard.

States have broad power to regulate liquor under § 2 of the Twenty-first Amendment. This power, however, does not allow States to ban, or severely limit, the direct shipment of out-of-state wine while simultaneously authorizing direct shipment by in-state producers. If a State chooses to allow direct shipment of wine, it must do so on evenhanded terms. Without demonstrating the need for discrimination, New York and Michigan have enacted regulations that disadvantage out-of-state wine producers. Under our Commerce Clause jurisprudence, these regulations cannot stand.

Justice STEVENS, with whom Justice O'CONNOR joins, dissenting.

The New York and Michigan laws challenged in these cases would be patently invalid under well settled dormant Commerce Clause principles if they regulated sales of an ordinary article of commerce rather than wine. But ever since the adoption of the Eighteenth Amendment and the Twenty-first Amendment, our Constitution has placed commerce in alcoholic beverages in a special category. Section 2 of the Twenty-first Amendment expressly provides that "[t]he transportation or importation into any State, Territory, or possession of the United States for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited."

Today many Americans, particularly those members of the younger generations who make policy decisions, regard alcohol as an ordinary article of commerce, subject to substantially the same market and legal controls as other consumer products. That was definitely not the view of the generations that made policy in 1919 when the Eighteenth Amendment was ratified or in 1933 when it was repealed by the Twenty-first Amendment. On the contrary, the moral condemnation of the use of alcohol as a beverage represented not merely the convictions of our religious leaders, but the views of a sufficiently large majority of the population to warrant the rare exercise of the power to amend the Constitution on two occasions. The Eighteenth Amendment entirely prohibited commerce in "intoxicating liquors" for beverage purposes throughout the United States and the territories subject to its jurisdiction. While § 1 of the Twenty-first Amendment repealed the nationwide prohibition, § 2 gave the States the option to maintain equally comprehensive prohibitions in their respective jurisdictions.

In the years following the ratification of the Twenty-first Amendment, States adopted manifold laws regulating commerce in alcohol, and many of these laws were discriminatory. So-called "dry states" entirely prohibited such commerce; others prohibited the sale of alcohol on Sundays; others permitted the sale of beer and wine but not hard liquor; most created either state monopolies or distribution systems that gave discriminatory preferences to local retailers and distributors. The notion that discriminatory state laws violated the unwritten prohibition against balkanizing the American economy—while persuasive in contemporary times when alcohol is viewed as an ordinary article of commerce—would have seemed strange indeed to the millions of

Americans who condemned the use of the "demon rum" in the 1920's and 1930's. Indeed, they expressly authorized the "balkanization" that today's decision condemns. Today's decision may represent sound economic policy and may be consistent with the policy choices of the contemporaries of Adam Smith who drafted our original Constitution; it is not, however, consistent with the policy choices made by those who amended our Constitution in 1919 and 1933.

My understanding (and recollection) of the historical context reinforces my conviction that the text of § 2 should be "broadly and colloquially interpreted." Indeed, the fact that the Twenty-first Amendment was the only Amendment in our history to have been ratified by the people in state conventions, rather than by state legislatures, provides further reason to give its terms their ordinary meaning. Because the New York and Michigan laws regulate the "transportation or importation" of "intoxicating liquors" for "delivery or use therein," they are exempt from dormant Commerce Clause scrutiny.

Justice THOMAS, with whom THE CHIEF JUSTICE, Justice STEVENS, and Justice O'CONNOR join, dissenting.

A century ago, this Court repeatedly invalidated, as inconsistent with the negative Commerce Clause, state liquor legislation that prevented out-of-state businesses from shipping liquor directly to a State's residents. The Webb-Kenyon Act and the Twenty-first Amendment cut off this intrusive review, as their text and history make clear and as this Court's early cases on the Twenty-first Amendment recognized. The Court today seizes back this power, based primarily on a historical argument that this Court decisively rejected long ago in *State Bd. of Equalization of Cal. v. Young's Market Co.* (1936). Because I would follow *Young's Market* and the language of both the statute that Congress enacted and the Amendment that the Nation ratified, rather than the Court's questionable reading of history and the "negative implications" of the Commerce Clause, I respectfully dissent.

I

The Court devotes much attention to the Twenty-first Amendment, yet little to the terms of the Webb-Kenyon Act. This is a mistake, because that Act's language displaces any negative Commerce Clause barrier to state regulation of liquor sales to in-state consumers.

The Webb-Kenyon Act immunizes from negative Commerce Clause review the state liquor laws that the Court holds are unconstitutional. The Act "prohibit[s] any 'shipment or transportation' of alcoholic beverages 'into any State' when those beverages are 'intended, by any person interested therein, to be received, possessed, sold, or in any manner used . . . in violation of any law of such State.' State laws that regulate liquor imports in the manner described by the Act are exempt from judicial scrutiny under the negative Commerce Clause, as this Court has long held. The Webb-Kenyon Act's language, in other words, "prevent

[s] the immunity characteristic of interstate commerce from being used to permit the receipt of liquor through such commerce in States contrary to their laws."

The Michigan and New York direct-shipment laws are within the Webb-Kenyon Act's terms and therefore do not run afoul of the negative Commerce Clause. Those laws restrict out-of-state wineries from shipping and selling wine directly to Michigan and New York consumers. Any winery that ships wine directly to a Michigan or New York consumer in violation of those state-law restrictions is a "person interested therein" "intend[ing]" to "[s]ell" wine "in violation of" Michigan and New York law, and thus comes within the terms of the Webb-Kenyon Act.

II

[T]he state laws the Court strikes down are lawful under the plain meaning of § 2 of the Twenty-first Amendment, as this Court's case law in the wake of the Amendment and the contemporaneous practice of the States reinforce.

The state laws at issue in these cases fall within § 2's broad terms. They prohibit wine manufacturers from "transport[ing] or import[ing]" wine directly to consumers in New York and Michigan "for delivery or use therein." Michigan law does so by requiring all out-of-state wine manufacturers to distribute wine through licensed in-state wholesalers. New York law does so by prohibiting out-of-state wineries from shipping wine directly to consumers unless they establish an in-state physical presence, something that in-state wineries naturally have. The Twenty-first Amendment prohibits out-of-state wineries from shipping wine into Michigan and New York in violation of these laws. In holding that the Constitution prohibits Michigan's and New York's laws, the majority turns the Amendment's text on its head.

Though the majority dismisses this Court's early Twenty-first Amendment case law, it relies on the reasoning, if not the holdings, of our more recent Twenty-first Amendment cases. But the Court's later cases do not require the result the majority reaches. Moreover, I would resolve any conflict in this Court's precedents in favor of those cases most contemporaneous with the ratification of the Twenty-first Amendment.

[M]y interpretation of the Twenty-first Amendment would not free States to regulate liquor unhampered by other constitutional restraints, like the First Amendment and the Equal Protection Clause. As this Court explained in *Craig v. Boren* (1976), the text and history of the Twenty-first Amendment demonstrate that it displaces liquor's negative Commerce Clause immunity, not other constitutional provisions.

The Twenty-first Amendment and the Webb-Kenyon Act displaced the negative Commerce Clause as applied to regulation of liquor imports into a State. They require sustaining the constitutionality of Michigan's and New York's direct-shipment laws.