

# *Granholm v. Heald*: Are The Grapes Really Free?

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“This is the best day for wine-lovers since the invention of the corkscrew.”<sup>1</sup>

## I. LEGAL BACKGROUND

In January 2003, Florida’s Tampa Bay Buccaneers were preparing to battle California’s Oakland Raiders in Super bowl XXXVII. In the excitement leading up to the game, Florida governor Jeb Bush and California governor Gray Davis entered into a very public ‘gentleman’s agreement’ about the outcome of the football game. If the Raiders won, Governor Bush would send Governor Davis a case of Florida citrus products and dinner at the Columbia Restaurant in Tampa, Florida. If the Bucs won, Governor Davis would send Governor Bush, among other things, a case of California wine.<sup>2</sup> When the Bucs defeated the Raiders, Davis found he could not honor the agreement because Florida law prohibited the direct shipping of alcohol to its residents.<sup>3</sup> Direct shipping in this situation refers to the shipping of wine or distilled spirits from one consumer to another if that shipment crosses state lines. Direct shipping also affects a winery shipping wine directly to a consumer who lives in another state.

The governor’s public relations problem highlighted an important constitutional question that landed before the United States Supreme Court almost two years later when wine journalists from Michigan sued for right to have wine shipped directly to them from outside the state.<sup>4</sup>

At the time of the governors agreement, the case of *Heald v. Engler*<sup>5</sup> had been working its way through the state and federal court system for two years.

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1. Clint Bolick, legal counsel for the Washington, D.C.-based Institute for Justice. 16 May 2005, [www.forbes.com](http://www.forbes.com).

2. Emert, Carol. *Bush Can’t Pop Davis’ Bottle: Wine Delivery Snafu Screws Up Governor’s Super Bowl Bet*, San Francisco Chronicle, Jan. 30, 2003.

3. *Id.*

4. *Granholm v. Heald*, 125 S. Ct. 1885, 1902 (U.S. 2005).

5. *Heald v. Engler*, No. 00-CV-71438-DT, 2001 U.S. Dist. LEXIS 24826 (2001) (defendant’s motion for summary judgment granted), *rev’d*, 342 F.3d 517 2003 U.S. App. LEXIS 17965 (6<sup>th</sup> Cir. Mich. 2003), *aff’d*, 125 S Ct. 1885, (U.S. 2005).

Plaintiffs Ray and Eleanor Heald, Michigan residents and wine journalists, filed a lawsuit challenging Michigan's alcohol distribution system as unconstitutional under the Commerce Clause.<sup>6</sup> The purpose of the Commerce Clause is to allow for free trade among the states.<sup>7</sup> Joined in their suit by Domaine Alfred, a small winery located on the central coast of California, the Healds argued that restricting their access to wines hindered their ability to do their jobs and gave in-state wineries an unfair edge over out-of-state wineries. In addition to delegating authority to Congress to enact laws affecting interstate commerce, the Commerce Clause also serves as a *limit on state action*. The State of Michigan argued that Section 2 of the Twenty-first Amendment abrogated all other rights under the Commerce Clause, citing *State Board of Equalization v Young*.<sup>8</sup>

The Twenty-first Amendment, passed in 1933, repealed the Eighteenth Amendment, also known as Prohibition. Section 2 of this Amendment provides that “[T]ransportation or importation into any state. . . for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited.”<sup>9</sup>

The impossibility of honoring Governor Davis' side of the agreement illustrated the conflict between these Constitutional provisions.

## II. FROM THE BARREL TO THE TABLE

There are many forms of alcohol in the U.S.; wine gave rise to this controversy. Defined as the “. . . product of juice or must of sound, ripe grapes. . . or other fruit. . .,”<sup>10</sup> wine can be made from many things, but the most common choice in the United States is the grape. What traditionally was grown and fermented for home consumption in backyards and basements across the United States has grown into an enormous commercial enterprise. In 1975, 368 million gallons of wine were commercially available, valued at \$3.3 billion.<sup>11</sup> Twenty five years later, the commercial marketplace bottled or boxed 558 million gallons of wine, valued at \$19.6 billion.<sup>12</sup>

Many states require that before a consumer can purchase a bottle of wine from his local store, a distributor/wholesaler must first purchase that bottle from a winery, then sell it to the shopkeeper for retail sale. Some states have separate tiers of distributors and wholesalers - not just one “middle man”, but

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6. *Id.*

7. U.S. Const., art. I, § 8.

8. *State Board of Equalization v. Young*, 299 U.S. 59 (U.S. 1936).

9. U.S. Const. amend. XXI, § 2.

10. 26 U.S.C.S. § 5381 (2005).

11. [http://www.wineinstitute.org/communications/statistics/consumption1934\\_99.html](http://www.wineinstitute.org/communications/statistics/consumption1934_99.html).

12. *Id.*

three – each with its own interest and profits to protect. The more complicated this system became in each state, the more the distributors consolidated. One consequence of this consolidation was that it was not cost-effective for small wineries to use distributors, due to the high costs of delivering product to the consumer. Specialized licenses were offered to *in-state* wineries shipping to in-state consumers, permitting them to operate outside the distribution system.

Another effect of this system was that consumers of wine could not order wine directly from most individual wineries. This disparity became more pronounced with the evolution of e-commerce and the use of the Internet for the purchase of consumables.

After evaluating summary judgment motions for both parties, the District Court granted the defendant's motion on the grounds that Michigan's system was appropriately addressing the 'core concerns' of the Twenty-first Amendment.<sup>13</sup> The court found that Michigan's regulations could be upheld, "[S]o long as they implicate the core concerns of the Twenty-first Amendment, including temperance, raising revenue and 'ensuring orderly market conditions.'" <sup>14</sup> The Sixth Circuit Court of Appeals reversed and remanded this decision, finding that although the core concerns of the Twenty-first Amendment might have been satisfied, the district court should have addressed plaintiff's argument that there was a Commerce Clause violation.

The United States Supreme Court granted certiorari on this case, consolidating it with two others – *Mich. Beer & Wine Wholesaler's Ass'n. v. Heald*<sup>15</sup> and *Swedenburg v. Kelly*<sup>16</sup>.

At the heart of the issue in these companion cases was 1) did Michigan or New York laws violate the Commerce Clause of the U.S. Constitution? And 2) if they did, was the existence of the Twenty-first Amendment sufficient to override the purpose of the Commerce Clause?

### III. COMMERCE CLAUSE

Article I, § 8 of the United States Constitution grants Congress the power to ". . . regulate commerce . . . among the several states. . ." <sup>17</sup> "The Commerce Clause even without implementing legislation by Congress is a limitation upon the power of the States." <sup>18</sup>

The U.S. Constitution has its origins in the promotion of a minimally involved national government – one currency and one set of federal laws. A

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13. *Heald*, 125 S. Ct. 1885.

14. *Id.*

15. *Mich. Beer & Wine Wholesaler's Ass'n. v. Heald*, 124 S. Ct. 2389 (U.S. 2004).

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

17. U.S. Const. art. I, § 8.

18. *Camps Newfound v. Town of Harrison*, 520 U.S. 564, 571 (U.S. 1997).

consequence of this system and its evolution is the recognition of the importance of a unified, national economy.

States are not permitted to favor their own residents at the expense of other U.S. citizens. In this case, the plaintiffs argued that the differing treatment of in-state businesses over out-of-state businesses was discrimination under the Commerce Clause. Where such discrimination exists, the court must evaluate whether the state's regulations "[A]dvance a legitimate local purpose that cannot adequately be served by reasonable nondiscriminatory alternatives."<sup>19</sup>

Michigan's distribution system required that out-of-state wineries not only use a distributor in Michigan, but also take additional steps under the auspices of collecting taxes and preventing minors from purchasing alcohol over the Internet. Among the several steps was the requirement that an out-of-state winery establish a warehouse in Michigan. In-state wineries did not need to comply with any of the same regulations – simply obtaining a permit from the state allowed them to ship directly to in-state consumers. Michigan argued that their system protected the 'core concerns' of the Twenty-first Amendment as established in *North Dakota v. United States*.<sup>20</sup> *North Dakota* held that laws regulating for the benefit of 'core concerns' would generally be upheld, ". . . In the interest of promoting *temperance, ensuring orderly market conditions, and raising revenue* . . ."<sup>21</sup> Plaintiffs argued that Michigan's laws existed not just to address "core concerns" but to protect Michigan businesses at the expense of out-of-state businesses.

The United States Supreme Court agreed with the plaintiffs, saying that "[E]ven 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 unfeasible. . ."<sup>22</sup> One state cannot unfairly regulate an industry so as to protect businesses within its borders by solely relying on the Twenty-first Amendment

#### TWENTY-FIRST AMENDMENT

Having found that Michigan's law violated the Commerce Clause, the Supreme Court next evaluated the interplay between the Commerce Clause and the Twenty-first Amendment.

The Twenty-first Amendment met with fierce resistance when it was proposed. Each state had a different opinion about what (if anything) was wrong with Prohibition and how to best improve the situation. The compromise

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19. *New Energy Co. of Ind. v. Limbach*, 486 U.S. 269 (U.S. 1988).

20. *North Dakota v. United States*, 495 U.S. 423, 109 L. Ed. 420, 110 S. Ct. 1986 (1990).

21. *Id.*

22. *Heald*, 125 S. Ct. 1885.

reached was committed to paper in § 2 of the Amendment, which reads “[T]ransportation 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.”<sup>23</sup> Early cases that challenged the constitutionality of this statement only strengthened its perceived stranglehold on the market.<sup>24</sup> This statement has been interpreted to mean that states can control the flow of liquor across their borders, not just within them. While different cases give different reasons, an often cited defense of this amendment and its continued application has been the right of each state to regulate for the benefit of the core concerns, as established in *North Dakota*.

One of the issues noted by both the Sixth Circuit and the U.S. Supreme Court in this case was that, although Michigan repeatedly cited loss of tax revenue and potential sales to minors to justify its wine regulations, the record contained no evidence that Michigan’s current system was the only way to accomplish its goals. Plaintiffs were not asking to be exempt from paying taxes on wines shipped to them (the raising revenue concern), they were simply asking for equal access. The Court found the argument concerning minors ordering and receiving alcohol over the Internet had alternative methods of regulation, including signature requirements for wine shipments. Justice Kennedy highlighted what the majority viewed as a critical flaw in Michigan’s argument by saying, “. . . 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 the regulations limiting *only out-of-state* direct shipments.”<sup>25</sup>

Michigan’s argument did not persuade the U.S. Supreme Court that the state’s individual rights to regulate these core concerns should prevail over the protections intended in the Commerce Clause. Had this case concerned a product other than alcohol, individual states and their distributors could not have created their own Prohibition on an industry of another state. The Commerce Clause was intended to give Congress the power to prevent trade wars between the states; it now seems that one industry has managed to illustrate what appeared to be a constitutionally sanctioned trade war. “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,” writes Justice Kennedy.<sup>26</sup>

Ultimately, a divided Court found that although the States have broad

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23. U.S. Const. amend XXI, § 2 (emphasis added).

24. *Ziffrin, Inc. v Reeves*, 308 U.S. 132 (U.S. 1939), *Indianapolis Brewing Co. v Liquor Control Commission*, 305 U.S. 395 (U.S. 1939).

25. *Heald*, 125 S. Ct. 1885 (emphasis added).

26. *Heald*, 125 S. Ct. 1885.

power to regulate liquor under the Twenty-first Amendment, “[T]his 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.”<sup>27</sup> The Court reached this decision after finding that the States had not met the burden of proving that the discrimination established by the respondents was “demonstrably justified”.<sup>28</sup> This does not mean that states have lost the power to regulate distribution of alcohol provided by the Twenty-first Amendment. State borders open to direct shipping can still be closed to the masses. According to this opinion, the decision about whether or not to open the border remains up to the individual states.

#### HAVE THE GRAPES REALLY BEEN FREED BY THIS DECISION?

The common perception of the Michigan decision is that all states must allow direct shipping. While this decision has created an opportunity for the wine industry, it remains unclear who will open their borders to direct shipping or close the option entirely and require that all alcohol be purchased in person.

Immediately following the Court’s opinion, Nida Samona, head of the Michigan Liquor Control Commission, indicated that Michigan’s response would be to *tighten* restrictions.<sup>29</sup> In a conference call with reporters, Ms. Samona expressed her opinion that “[T]here shouldn’t be any shipment of wine or other alcohol product, it should be purchased, directly, face to face.”<sup>30</sup>

Introduced on June 16, 2005, Mich. H.B. 4959 would revise the definition of “wine maker” under current state law to a person licensed to ship wine to a wholesaler *only*, and would revoke a current system that allows for in-state wineries producing less than 200,000 cases of wine per year to ship directly to consumers.<sup>31</sup>

In New York, A.B. 7379 was introduced on April 14, 2005.<sup>32</sup> After moving quickly through the Assembly and Senate, New York Governor Pataki signed a bill into a law and that take effect on August 11, 2005.<sup>33</sup> The new law provides that an out-of-state winery that has obtained the proper license and permit to collect taxes may ship up to thirty six cases of wine to a New York resident each calendar year.<sup>34</sup> The law also provides for annual permits at a cost of \$125.00 each and includes a method for collecting and remitting sales

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27. *Id.*

28. *Chemical Waste Management, Inc. v. Hunt*, 504 U.S. 334, 344 (1939).

29. Zagaroli, Lisa and Bethel, Alison. *Michigan to Push Online Wine Ban*, The Detroit News, May 17, 2005.

30. *Id.*

31. <http://www.legislature.mi.gov/documents/2005-2006/billanalysis/house/htm>

32. <http://public.leginfo.state.ny.us>

33. *Id.*

34. N.Y. Alco. Bev. Cont. Article 6, § 79(c). (2005)

tax.

As of August 1, 2005, twenty-seven states have either passed laws or have legislation in process to allow for direct shipment of wine to consumers of legal drinking age.<sup>35</sup> New York consumers are preparing to add out-of-state wines to their cellars and Michigan consumers are waiting to see how successful the Liquor Commission's effort will be in restricting their access to wines, even those produced in their own state.

As previously discussed, the choice is ultimately up to the individual state. States are not required to open their markets to direct shipping, but if they do, they must play fair. As Justice Kennedy stated, "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."<sup>36</sup>

Can former Governor Davis honor his bet? Not at the moment, because Florida still prohibits direct shipment of wine. By the time the Raiders and the Buccaneers play in another Super Bowl, however, the outcome of the wager could be different.

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35. *Jersey's ban on Internet wine sales is unjustified*, The Star-Ledger, July 17, 2005.

36. *Heald*, 125 S. Ct. 1885.