



## Government Affairs Extra

# The Future of Direct Shipping

BY  
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In September 2018, the U.S. Supreme Court granted a petition for a *writ of certiorari* (i.e., the Court agreed to hear a case) brought before the Court by the Tennessee Wine and Spirits Retailers Association (Tennessee Retailers) in *Tennessee Wine and Spirits Retailers Association v. Byrd*. The petition requested that the Court review the lower court's decision upholding a finding that Tennessee's two-year residency requirement for retail license applicants is unconstitutional. Specifically, the question Tennessee retailers posed to the Court is whether the 21st Amendment of the U.S. Constitution gives states the authority to, consistent with the so-called "Dormant" Commerce Clause of the Constitution, regulate sales of alcohol beverages by imposing residency requirements on retail (or wholesale) license applicants. The court began hearing oral arguments on January 16.

As a bit of legal background, under the Dormant Commerce Clause, state statutes and regulations generally may not favor in-state interests or discriminate against out-of-state interests. The 21st Amendment of the U.S. Constitution, which gave states the authority to regulate sales of alcohol within their borders, acts as a partial limitation of Dormant Commerce Clause principles when the issue involves a state law regulating alcohol. In other words, when it comes to alcohol, the states can argue that their authority under the 21st Amendment limits the application of the Dormant Commerce Clause.

But the Dormant Commerce Clause is designed to prevent states from engaging in economic protectionism, and the 21st Amendment does not shield all state actions from Dormant Commerce Clause scrutiny. Although Supreme Court cases from the 1930s, shortly after the passage of the 21st Amendment, suggested that the exemption of state alcohol laws from Commerce Clause scrutiny was very broad, opinions since then have limited the protection the 21st Amendment gives to state alcohol laws.

### THE *BYRD* CASE

A Tennessee alcohol beverage law requires an applicant for a retail license to have been a resident of the state for at least the two-year period immediately preceding the application. For corporate applicants, the requirement applies to any of the corporation's officers, directors, or stockholders. Moreover, to renew a license, the law requires Tennessee residency for at least 10 consecutive years.

After two prospective retail applicants who did not meet the residency requirement—including the Tennessee affiliate of Total Wine Spirits & Beer—sought licenses in Tennessee, the state's attorney general preemptively filed a declaratory judgment action in state court to attempt to have the court declare the residency requirements constitutional. The case was removed to federal court, and the district court found the requirements unconstitutional under the Dormant Commerce Clause. Tennessee Retailers then appealed to the U.S. Court of Appeals for the Sixth Circuit.

### THE SIXTH CIRCUIT'S OPINION

In February 2018, the Sixth Circuit reviewed the Tennessee law and, affirming the district court decision that invalidated Tennessee's residency requirements, held that "a three-tier system can still function" without the two-year durational residency restriction imposed by the state. The majority opinion provided an overview of Supreme Court guidance on the tension between the Dormant Commerce Clause and the 21st Amendment, focusing in particular on the *Bacchus Imports v. Dias* (1984) and *Granholm v. Heald* (2005) decisions.

The court concluded that the non-discrimination Commerce Clause principles articulated in those cases are not limited to alcohol beverage producers and their products. Accordingly, the court held that the 21st Amendment does not exempt state laws concerning wholesalers and retailers from scrutiny under the Commerce Clause. In terms of the Tennessee residency requirements in particular, the court found that the 21st Amendment did not protect the requirements

from Commerce Clause scrutiny and, without the protection of the 21st Amendment, the court found the requirements unconstitutional.

### THE CIRCUIT SPLIT

In July 2018, Tennessee Retailers submitted a petition for a *writ of certiorari* to the Supreme Court. Although the Supreme Court grants only a small number of the petitions it receives each year, it accepts a 21st Amendment-related case for review roughly every decade or so. If the party seeking a petition for a *writ of certiorari* can demonstrate to the Court that a "circuit split" exists (i.e., that different U.S. Courts

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of Appeals disagree with one another on a particular legal issue), the Court is more likely to grant a petition so that it can restore uniformity of legal interpretations.

Tennessee Retailers was able to build a persuasive case for the Supreme Court to grant the petition, as over the last decade several cases have demonstrated a circuit split relating to the residency question. At the heart of the different appellate courts' split in this case is whether the non-discrimination principle of the Dormant Commerce Clause, which the Supreme Court clearly applied to wine producers and products in the 2005 *Granholm v. Heald* decision, also applies to state laws regulating the wholesale and retail tiers of the industry.

Two federal appellate courts (including *Byrd*) applied the non-discrimination rule to strike down state residency requirements for alcohol beverage licensees. One other appellate court has upheld residency restrictions, and two other appellate courts have taken a similar approach and upheld other kinds of restrictions on retailers, finding that the non-discrimination rule applies only to producers and products, and not to the two other tiers of the industry. This split in the circuit courts has created uncertainty for courts and regulators throughout the nation, and for the alcohol industry generally.

**POTENTIAL IMPACTS OF BYRD**

The Supreme Court's review of the *Byrd* case will address the constitutional validity of the Tennessee law imposing residency requirements on retail alcohol beverage license applicants. It remains to be seen whether the Court will go further to also address more fundamental questions about state powers under the 21st Amendment of the U.S. Constitution. But the stakes of *Byrd* reach far beyond residency. If the Supreme Court reverses the Sixth Circuit on broad grounds and finds that state laws regulating wholesalers and retailers are not subject to challenge under the Dormant Commerce Clause, *Byrd* would maintain the status quo with respect to direct shipping of beer.

If the Court affirms *Byrd* on the broad principle that the Commerce Clause's non-discrimination principles apply to state laws regulating wholesalers and retailers (as opposed to only producers), then many state laws prohibiting out-of-state retailers from shipping alcohol beverages (including beer) to in-state consumers could be vulnerable to an attack on constitutional grounds. Most states authorize in-state retailers to ship alcohol directly to a consumer's home, so application of non-discrimination principles could force states to extend similar privileges to out-of-state retailers.

As a final note, several other cases currently being litigated in courts around the country also have the potential to shape the future of alcohol direct shipping. For example, in late September

2018 a federal district court in Michigan struck down a state statute that allowed only in-state retailers to direct-ship alcohol beverages to Michigan consumers and prohibited out-of-state retailers from exercising that privilege. Whether that case survives an appeal likely will depend on the Supreme Court's decision in *Byrd*, indicating that the outcome of this case could have significant implications for the future of the direct-to-consumer market for alcohol beverages in the U.S.

The *Byrd* case will take some time to resolve, and a decision will likely come down in mid-2019.

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