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The United States has long been founded upon capitalistic economic principles. Codified in the United States Constitution Article 1 Section 8, the Commerce Clause instills in Congress the power to "regulate commerce […] among the several states."[1] Consequently, states are prohibited from imposing discriminatory taxes, tariffs or regulations that inhibit interstate commerce. Idealistically, this Congressional power should lead to one much stronger and larger economy as a nation by promoting a healthy and competitively balanced market place.

In the current technological age, the advancement of the Internet has lead to the largest and most open marketplace. This enables retailers to expand their market from a local one to a national one throughout the United States. As a result, consumers can have direct access through e-commerce to wholesalers, distributors, third party sellers and producers giving the consumer a near infinite amount of products at their disposal. Transactions in this marketplace occur continuously throughout the day and are usually without conflict.

However, certain products are regulated by an individual State before being available for purchase by the consumer. In particular, alcoholic beverages are strictly regulated by the state, most notably through a Three Tier system. There is a strong public interest to maintain these regulations, such as driving while under the influence, alcohol related violence underage drinking, and efficient tax collection. Consequently, the States regulation of alcohol has imposed barriers to out-of-state shipments through Internet sales, in violation of the Commerce Clause.

Out-of-state shipment of alcoholic beverages to consumers in a different state has become an issue with the increasing popularity of limited production wines and direct-to-consumer shipping. The number of small wineries has vastly increased and these entrepreneurs have taken to using the internet's endless marketplace to directly reach consumers outside of their local marketplace, and in essence, circumventing State imposed regulations for the sale of alcohol. In response, States have attempted to stop the flow from these vineyard-to-consumer transactions through statutes requiring alcoholic beverage producers to use a wholesaler or distributor before reaching the consumer. This system, which restricts the flow of interstate commerce, is rooted in both the antiquated Eighteenth Amendment, the banning of alcohol sales, and the Twenty-First Amendment, regulating the transportation alcohol across state lines. As our nation progresses, these regulations have no doubt impeded interstate commerce stifling our growth as a national economy and our founding capitalistic principles.

The History of Alcohol Sales Regulation in the United States

Governmental Taxation and public interests are the fundamental purpose for imposing regulations on alcohol. Prior to prohibition, there was a strong interest for States to regulate the manufacturing of alcohol and its sale within the state.[2]These regulations however were not to effect interstate commerce.[3]The United States was in a transition during the late nineteenth century. States prohibited the sale and consumption of alcohol while others did not, leading to illicit importation and bootlegging of alcohol. Citizens of a dry state would

[1]U.S. Const. art. I, § 8, cl. 3

[2]*Thurlow v. Massachusetts*, 46 U.S. 504, 577 (1847); *Mugler v. Kansas*, 123 U.S. 623, 661-63 (1887).
[3]*Id*.

legally purchase alcohol out of state and smuggle it across the state line.[4] In response, dry states imposed regulations banning the transportation of alcohol, which in 1888, the Supreme Court held was an impediment to interstate commerce.[5]These regulations were invalidated and importation was permitted so long as the alcohol remained packaged and was not resold.[6]In response to *Bowman v. Chi. & Nw. Ry.* and *Leisy v. Hardin,* and in effort to return this regulatory power to states, Congress enacted the Wilson Act in 1891.[7]

The Wilson Act came under scrutiny in *Rhodes v. Iowa*, as the Supreme Court considered the ambiguous meaning of the phrase "upon arrival" in the Statute.[8]The Court decided that the regulations of the Wilson Act could only be imposed after delivery of liquor and when there was an attempt to resell it.[9] Based upon the Courts' reasoning the shipper should not be subject to penalty.[10]Specifically, an individual may have been lawfully acting in a State that did not ban alcoholic beverages, while they would be violating regulations imposed by a dry state.[11]

To eradicate these inconsistencies and issues of bootlegging, the Webb-Kenyon Act was enacted.[12]The Webb-Kenyon Act served a limited purpose. The Supreme Court held that there was a legitimate public interest to enforce inconsistent state laws, between wet and dry states, even if there was an impediment to interstate commerce.[13]Permitting these strict regulations of alcohol was precedent necessary for Congress to ratify the Eighteenth Amendment banning the sale, but not the possession or consumption of alcoholic beverages.[14]Ultimately, the Eighteenth Amendment was repealed by the Twenty-first Amendment in

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[4]James Alexander Tanford, *E-Commerce in Wine* 3 J.L. Econ. & Pol'y 275 (2007)
[5]See *Bowman v. Chi. & Nw. Ry.,* 125 U.S. 465, 499-500 (1888).
[6]*Leisy v. Hardin*, 135 U.S. 100 (1890).
[7]27 U.S.C. §122. ("[All] intoxicating liquors transported into any State or Territory shall upon arrival in such State or Territory be subject to the operation and effect of the laws of such State or Territory enacted in the exercise of its police powers, to the same extent and in the same manner as though such liquors had been produced in such State or Territory, and shall not be exempt there from by reason of being introduced therein in original packages or otherwise.")

[8]*Rhodes v. Iowa,* 170 U.S. 412 (1898)
[9]*Id.*
[10]*Id.*
[11]*Id*.
[12]27 U.S.C. §122. ("That the shipment or transportation of any spirituous or other intoxicating liquor of any kind, from one State into any other State which is intended, by any person interested therein, to be received, possessed, sold, or in any manner used, either in the original package or otherwise, in violation of any law of such State is hereby prohibited.")

[13]See *Seaboard Air Line Ry. v. North Carolina*, 245 U.S. 298, 303 (1917).

[14] US. Const. Amends. XXI 18. ("Section 1. After one year from the ratification of this article the manufacture, sale, or transportation of intoxicating liquors within, the importation thereof into, or the exportation thereof from the United States and all the territory subject to the jurisdiction thereof for beverage purposes is hereby prohibited.

Section 2. The Congress and the several States shall have concurrent power to enforce this article by appropriate legislation.

Section 3. This article shall be inoperative unless it shall have been ratified as an amendment to the Constitution by the legislatures of the several States, as provided in the Constitution, within seven years from the date of the submission hereof to the States by the Congress.")

1933, and in effect reaffirming the Webb-Kenyon Act strictly regulating the shipping of alcohol from state to state through taxation and licensing.[15]

Despite these congressional efforts, the Supreme Court surmised that an additional taxation to transport alcoholic was unconstitutional and discriminatory towards out of state alcohol producers.[16]The reasoning was that in state producers received greater protection and competitive advantage under the State Regulation.[17]In the aftermath of the Twenty-first Amendment, States were granted greater power in the regulation of alcohol and began to implement a Three Tier system for distribution.[18] These statutes and regulatory schemes could not be substantively discriminatory towards out of state goods as required by the dormant Commerce Clause.[19]

The typical system consists of the first tier in the chain is the federally licensed manufacturer or producer of the alcoholic beverage[20], the second tier is the state licensed wholesaler and/or distributor, and the third

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[15] US. Const. Amends. XXI *("***Section 1.** The eighteenth article of amendment to the Constitution of the United States is hereby repealed.

Section 2. 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.

Section 3. This article shall be inoperative unless it shall have been ratified as an amendment to the Constitution by conventions in the several States, as provided in the Constitution, within seven years from the date of the submission hereof to the States by the Congress.")

[16]*State Bd. of Equalization of Cal. v. Young's Mkt. Co.*, 299 U.S. 59 (1936)

[17]*Id.*

[18]*Granholm v. Heald*, 544 U.S. 460, 484-85, 125 S. Ct. 1885, 161 L. Ed. 2d 796 (2005) (the goal 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 non-uniform laws in order to discriminate against out-of-state goods.")

[19]*Id.*

[20]27 U.S.C.A. § 203 ("In order effectively to regulate interstate and foreign commerce in distilled spirits, wine, and malt beverages, to enforce the twenty-first amendment, and to protect the revenue and enforce the postal laws with respect to distilled spirits, wine, and malt beverages:
(a) It shall be unlawful, except pursuant to a basic permit issued under this subchapter by the Secretary of the Treasury--
(1) to engage in the business of importing into the United States distilled spirits, wine, or malt beverages; or
(2) for any person so engaged to sell, offer or deliver for sale, contract to sell, or ship, in interstate or foreign commerce, directly or indirectly or through an affiliate, distilled spirits, wine, or malt beverages so imported.
(b) It shall be unlawful, except pursuant to a basic permit issued under this subchapter by the Secretary of the Treasury--
(1) to engage in the business of distilling distilled spirits, producing wine, rectifying or blending distilled spirits or wine, or bottling, or warehousing and bottling, distilled spirits; or
(2) for any person so engaged to sell, offer or deliver for sale, contract to sell, or ship, in interstate or foreign commerce, directly or indirectly or through an affiliate, distilled spirits or wine so distilled, produced, rectified, blended, or bottled, or warehoused and bottled.
(c) It shall be unlawful, except pursuant to a basic permit issued under this subchapter by the Secretary of the Treasury--
(1) to engage in the business of purchasing for resale at wholesale distilled spirits, wine, or malt beverages; or

tier is the state licensed alcoholic beverage retailer.[21]Often the Three Tier system is correlated to a statute, which explicitly bans out-of-state shipments of alcohol in favor of in-state products.[22]Similar to the North Carolina statute, a number of states have imposed strong barriers to interstate commerce by constructing statutes that facially discriminate an out-of-state alcohol producer in favor of an in-state alcohol producer.[23]Although States have the authority to regulate liquor[24], perhaps it is time to reevaluate these regulatory schemes as out-of-state alcohol producers' have the ability to reach consumers with their products through online marketplaces and direct-to-consumer shipping.

Overview of E-Commerce and Direct-to-Consumer Shipping E-Commerce has become one of the most prominent forms of consumer transaction across the globe. E-Commerce is defined as "business that is transacted by transferring data electronically, especially over the Internet."[25] In 2011, e-commerce transactions accounted for $2.7 trillion of total shipments from manufacturers, nearly half of the $5.5 trillion of total sales.[26] The online marketplace allows greater access to more products while providing savings to consumers by bypassing wholesalers.[27] This is especially true in the case of producers of alcoholic beverages.

In 2013, the United States was the home to more than 8,000 wineries[28], 2,483 craft breweries, an additional 55 macro-breweries[29], and more than 350 distilleries[30]. The rapid growth of these industries is due in large part to the Internet. These boutique wineries, craft breweries and distilleries have limited resources and much more limited production. However, their products have become highly sought after by consumers across the country because of websites, message boards, and trading forums. These online communities comprised of enthusiasts who rate, trade, and discuss the artisan quality of these alcohol

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(2) for any person so engaged to receive or to sell, offer or deliver for sale, contract to sell, or ship, in interstate or foreign commerce, directly or indirectly or through an affiliate, distilled spirits, wine, or malt beverages so purchased.")

[21]*See* AR ADC 006.02.2-2.13.1. ("The three-tier system of alcohol distribution consists of the three broad categories of the marketing chain. Alcoholic beverage manufacturers, including distilleries, breweries, importers or rectifiers, whether or not they hold a permit issued by the Arkansas Alcoholic Beverage Control Division, are considered the first tier of the distribution system. Alcoholic beverage wholesalers, licensed by the State of Arkansas, are considered the second tier of distribution. Alcoholic beverage retailers, licensed by the State of Arkansas, are considered the third tier of distribution.")

[22]See N.C. Gen. Stat. Ann. § 18B-102.1. ("It is unlawful for any person who is an out-of-state retail or wholesale dealer in the business of selling alcoholic beverages to ship or cause to be shipped any alcoholic beverage directly to any North Carolina resident who does not hold a valid wholesaler's permit under Article 11 of this Chapter.")

[23]*Granholm,* at 494.

[24]*Healy v. Beer Inst., Inc.*, 491 U.S. 324, 342, 109 S. Ct. 2491, 105 L. Ed. 2d 275 (1989)

[25]E-commerce. (n.d.). *The American Heritage Abbreviations Dictionary, Third Edition*. Retrieved October 15, 2013, from Dictionary.com website http://dictionary.reference.com/brose/e-commerce

[26] U.S. Census Bureau, *E-stats* (May 23, 2013)

[27] Federal Trade Commission, FTC Statement Before U.S. House of Representatives on Energy and Commerce Concerning E-Commerce Wine Sales and Direct Shipment (2003)

[28] Chet Klingensmith, *North American Winery Total Passes 8,000* (February 4, 2013), http://www.winesandvines.com/template.cfm?section=news&content=111242.

[29] Brewers Association, http://www.brewersassociation.org/pages/business-tools/craft-brewing-statistics/number-of-breweries (Last visited October 15, 2013)

[30] The American Distilling Institute, http://www.distilling.com/PDF/craft.pdf (Last visited October 15, 2013).

products.[31]These sites, in turn, act as the producers' best marketing tool by generating a national intrigue for beverages outside of the original local marketplace.

In 1977, alcoholic beverages accounted for $2,263,512,000 worth of tax revenue amongst all states combined, with Florida leading the country with over $185 million in revenue.[32] In 2011, that amount has tripled to more than $6 billion dollars per year of tax revenue with Texas receiving over $870 million of tax revenue.[33]Clearly there is a strong state interest in regulating the alcoholic beverage industry.[34]The revenue is collected by State Governments through the issuance of licenses to producers, wholesalers, and retailers as well by way of sales tax.[35] States disfavor "vertical integration" between the three tiers because this eliminates the need for additional licensing.[36] Further, wholesalers and retailers disfavor direct-to-consumer shipping because it affects their business.[37] Consumers stand to receive the most gain as they have access to a larger selection of higher quality products a reduced cost.[38] The issue for these Craft Producers is not demand, but how can they reach this nationwide market place.

A staple of the craft brewing industry is the "Reserve Society". The typical reserve society allows for a limited number of consumers to purchase a membership that entitles them to later purchase limited production specialty beers that will be released during the coming year.[39]Included in the upfront cost are beers that cannot be obtained by any means other than ordering them through the online society.[40] Many of these societies allow for either direct-to-consumer shipping if the consumer lives within the same state as the brewer, or the consumer may pick up at the brewery itself.[41] However, the goal of these societies is to reach a larger market and most members live out of state. What this leads to is "trusteeing". This occurs when an out of state consumer may designate an instate resident as a trustee.[42] This trustee will pick up or have the beer shipped to them on behalf of the original consumer. The trustee will then ship the beer to the original consumer who purchased it through the breweries e-commerce site.[43]

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[31] For example, see Wine Traders Club, http://www.winetradersclub.com/, Beer Advocate, http://www.beeradvocate.com/, Ratebeer, http://ratebeer.com/, Whisky, http://www.whisky.com/.
[32] State & Local Government Finance Data Query System. http://slfdqs.taxpolicycenter.org/pages.cfm. The Urban Institute-Brookings Institution Tax Policy Center. Data from U.S. Census Bureau, Annual Survey of State and Local Government Finances, Government Finances, Volume 4, and Census of Governments (1977-2011). Date of Access: (29-Jul-2013).
[33]*Id*.
[34]*North Dakota v. United States*, 495 U.S. 423, 432, 110 S.Ct. 1986, 109 L.Ed.2d 420 (1990) there is a strong state interest in "promoting temperance, ensuring orderly market conditions, and raising revenue".)
[35] Jon Leibowitz, *Competition in the Information Society Uncorked and Unplugged*, 2005 WL 3645313 (F.T.C.).
[36]*Id*.
[37]FTC Staff Report, *Possible Anticompetitive Barriers to E-Commerce: Wine* (July 2003), *available at* http://www.ftc.gov/os/2003/07/winereport2.pdf (Hereinafter referred to as "The Wine Report")
[38]*Id*. ("If consumers use the least expensive method of direct shipping (ground service), they could save an average of 8-13% on wines costing more than $20.00 per bottle, and an average of 20-21% on wines costing more than $40.00 per bottle.")
[39] The Bruery Reserve Society, http://www.thebruery.com/reservesociety/2014.html (Last visited November 12, 2013).
[40]*Id*.
[41]*Id*.
[42]*Id*.
[43] Don Russell, *Beer Clubs and the Privileges of Memberships*, http://articles.philly.com/2013-09-06/news/41804669_1_beer-drinkers-ratebeer-com-small-breweries (September 6, 2013).

Because of State statutes which regulate through the Three Tier system, the brewery is unable to simply ship directly to the out of state buyer, who instead must use an intermediary third party in good faith. These societies provide up front financing for these small businesses and can be pivotal to its future success and sustainability.[44] As the number of breweries continues to grow, a unified method of alcohol regulation allowing for direct to consumer shipment would greatly advance the craft beer industry, which has already shown to be one of the fastest growing industries in the country.

In the wine industry, direct-to-consumer shopping has become extremely prevalent and continues to grow each year.[45] In 2012, 3.1 million cases of wine were shipped from wineries directly to consumers.[46] Wine shipped directly to consumers accounted for over $1.46 billion of revenue in 2012, up by 10% from 2011, and 24% from 2010.[47] Over 50% of the wineries using direct-to-consumer commerce have an annual case production between 5,000- 49,000.[48]Interestingly, California, which is considered to be the American leaders of the wine industry, leads all other states in shipments of out of state wine received, accounting for 32% of the market share.[49] New York, Illinois, Minnesota, Oregon, Florida combine to account for approximately 60% of shipments, while all remaining states account for approximately 8%.[50]

Again, the benefits of direct-to-consumer shipping cannot be underestimated and greatly benefits the consumer in terms of convenience, selection, and saving.[51] In *Beskind v. Easley,* the court found that "wine sold through the three-tiered system is more expensive than the same or comparable wine sold in-state [directly to consumers] because wine distributed through the three-tiered structure is subjected to two 'mark-ups' in price that local wine does not face."[52] Each time a wine passes through one of the tiers, the price increases, with the wholesale mark up accounting for approximately an 18-25% price increase to consumers.[53]The benefits of direct-to-consumer shipping are vast, and it is apparent that taxation is the primary motivation for the continuance of the Three Tier regulatory system and discriminatory statutes.[54]

The Constitutionality of Direct to Consumer Shipping Regulations: Granholm and Beyond

The Supreme Court attempted to provide some clarity on discriminatory state imposed alcohol regulation in *Granholm v. Heald.* The matter involved a Michigan statute and a New York statute that prevented out-of-state wineries to ship directly to consumers in violation of the dormant commerce clause.[55] Both Michigan and New York imposed the Three Tier system of alcohol regulation.[56] In

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[44]*Id*.
[45] Jeff Carroll, Pawel Smolarkiewicz, Lynne Skinner, *Direct to Consumer Wine Shipping Report* 2013 http://www.winesandvines.com/pdf/2013Direct-to-Consumer-Shipping-Report.pdf.
[46]*Id*.
[47]*Id*.
[48]*Id*.
[49]*Id*.
[50]*Id*.
[51]*Id*.
[52] Beskind v. Easley, 325 F.3d 506, 515 (4th Cir. 2003).
[53] The Wine Report at 22.
[54]1990) ("The justifications [...] for the legislation as non-discriminatory bases for the statute are not "directly" related to the promotion of temperance. Taxation, inspection and the maintenance of local jobs have, possibly, a tangential, attenuated, connection with temperance in the sense that regulation of the liquor industry may limit the accessibility of alcohol to some degree; but any relation to the promotion of temperance which may be traced to that source is hardly the direct promotion of temperance which is required to invoke the Twenty-first Amendment.")

[55]*Granholm v. Heald*, 544 U.S. 460, 484-85, 125 S. Ct. 1885, 161 L. Ed. 2d 796 (2005)
[56]*Id*.

Michigan, a winery could obtain a "wine maker" license for the minor fee of $25, which would allow them to ship directly to out-of-state consumers.[57] In contrast, an Out-of-state winery could apply for an "outside seller of wine" license, which costs $300; however, this license required the wineries to sell only to wholesalers.[58] Similarly, New York's regulatory scheme allowed in state wine producers to ship directly to consumers out-of-state while restricting an out-of-state competitors' ability to ship to consumers in state.[59] Specifically, for an out of state winery to ship directly to a consumer in New York, seventy-five percent of the grapes used in production had to be grown in New York to become a licensed New York Winery.[60]Additionally, the winery needed to establish "a branch factory, office or storeroom within the state".[61]

In his decision, Justice Kennedy opined that these regulations explicitly discriminated against out-of-state wineries in clear favor of in-state wineries.[62]He reasoned that under the Commerce Clause, a state law discriminating against interstate commerce must be found to be invalid per se because out-of-state manufacturers were not able to compete under equal conditions.[63] In essence, the New York regulation all but mandated that an out-of-state winery have a physical presence in the state if they wished to ship directly to a consumer.[64]

Similarly, the Michigan statute outwardly created an unfair competitive advantage in favor of in state wineries by allowing direct-to-consumer shipping while strictly prohibiting an out-of-state winery to ship into Michigan.[65] In Justice Kennedy's opinion, he disagreed with both States' arguments that the statutes were valid under Section 2 of the Twenty-First Amendment.[66]Instead, he focused on the tax motivation of the statutes.[67] Justice Kennedy recognized that while states did have a strong interest in regulating alcohol and could do so with the Three Tier system, direct-to-consumer shipping was a growing industry, which could still be efficiently regulated.[68]

Justice Kennedy continued his analysis of the statutes and whether they "advance[d] a legitimate local purpose that cannot be adequately served by reasonable nondiscriminatory alternatives."[69] The States first argued that there was a legitimate state interest in preventing consumption of alcohol by minors and direct-to-consumer shipping of wine limited their ability to police this concern.[70] The States concern was

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[57]*Id*. *See also* Mich. Comp. Laws Ann. § 436.113 ("Wine maker" means any person licensed by the commission to manufacture wine and to sell that wine to a wholesaler, to a consumer by direct shipment, at retail on licensed winery premises, to sell the wine to a retailer, and as provided for in section 537.")
[58]*Id*. *See also* Mich. Comp. Laws Ann. § 436.1109 ("Outstate seller of wine" means a person licensed by the commission to sell wine which have not been manufactured in this state to a wholesaler in this state in accordance with rules promulgated by the commission and to sell sacramental wine as provided in section 301.")
[59]*Id*.
[60]*Id*.
[61]*Id*. *See also* N.Y. Alco. Bev. Cont. Law Ann. §76-a(3), 76-a(6)(a), §3(20-a), §3(37).
[62]*Id*. ("This discrimination substantially limits the direct sale of wine to consumers, an otherwise emerging and significant business.")
[63]*Id*.
[64]*Id*.
[65]*Id*. (Laws of this type "deprive citizens of their right to have access to the markets of other States on equal terms.")
[66]*Id*.
[67]*Id*.
[68]*Id*.
[69]*Id*. quoting New *Energy Co. of Ind. V. Limbach*, 486 U.S. 289, 278 (1988).
[70]*Id*.

that the Internet provided minors an avenue around being properly verified, granting easier to alcohol.[71] Justice Kennedy turned to the Wine Report prepared by the FTC for guidance and States that permitted direct-to-consumer shipping did not have an increase in minors obtaining alcohol illegally.[72] In the Wine Report, the FTC had determined that wine was not the drink of choice of minors because the cost was more prohibitive than attempting to purchase, or having a person of age purchase, beer or hard liquor through illicit means.[73] Further, Justice Kennedy stated that even if a minor had purchased the wine over the Internet that upon delivery the Model Direct Shipping Bill requires an adult signature before the exchange of alcohol can occur.[74] Therefore, the risk of an increase in underage drinking was found not to be a legitimate state concern validating the discriminatory statutes.[75]

The second argument promulgated by the States was that direct-to-consumer shipping undermined their ability collect taxes.[76] Justice Kennedy first looked to the Michigan regulatory scheme, where wholesalers did not collect the taxes from out of state wineries, but rather the state itself "collects taxes directly from out-of-state wineries on all wine shipped to in-state wholesalers."[77] Believing that Michigan efficiently regulated the Three Tier system, Justice Kennedy saw no reason why they would be unable to regulate direct-to-consumer shipping under similar conditions and that there was no legitimate state interest in this instance.[78]Justice Kennedy found that New York could have alleviated any concerns simply by requiring an out-of-state winery to obtain a permit in order to ship into the state.[79]Further, because a winery must be federally licensed, a winery must comply with state tax regulations and therefore the fear of losing tax revenue is not a legitimate state interest as a wineries failure to do so would result in the loss of a license.[80]

The *Granholm* decision was meant to provide clarity on the direct-to-consumer shipping issue, but Justice Steven's in his dissent left the door open for debate. He believed that alcoholic beverages were not ordinary consumer products and required greater State enforced regulations such as the New York and Michigan statute.[81]Since *Granholm*, several other Federal Circuits have been weighed in on the issued. In the Sixth Circuit, Kentucky had imposed a regulation that while facially neutral discriminated against out-of-state wineries from shipping directly to a consumer.[82] In *Cherry Hill Vineyards, LLC., v. Lilly*, an Oregon winery challenged Kentucky's regulations of "small farm wineries"[83] which allowed any in-state or out-of-state winery to apply for a direct-to-consumer shipping license.[84] The license would allow any

[71]*Id*. ("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.")
[72]*Id*. citing to the Wine Report
[73]*Id*. citing to the Wine Report
[74]*Id*.
[75]*Id*.
[76]*Id*.
[77]*Id*. at 491 *quoting* Mich. Admin. Code Rule 436.1725(2) (1989) ("Each outside seller of wine shall submit ... a wine tax report of all wine sold, delivered, or imported into this state during the preceding calendar month").
[78]*Id*.
[79]*Id*.
[80]*Id*.
[81]*Id*.
[82]*Cherry Hill Vineyards, LLC. v. Lilly*, 553 F.3d 423 (6th Cir. 2008).
[83] KRS § 241.010(46) defines a small farm winery as one producing no more than 50,000 gallons of wine per year.
[84]*Cherry Hill Vineyards, LLC. v. Lilly*, 553 F.3d 423 (6th Cir. 2008).

winery of this size to ship two cases of wine per customer per visit to the winery, imposing the same limitations on both in-state and out-of-state wineries.[85]

The State argued that there was no unfair competitive advantage to out-of-state wineries.[86]The Plaintiffs argued the statute itself was discriminatory because of the in-person purchasing requirement; feasibly a Kentucky consumer who wished to purchase their wine would have to physically go to Oregon to place the order for shipment.[87] This requirement all but forces an out-of-state winery to first supply a wholesaler with their product before a consumer in Kentucky can purchase it.[88]Conversely, a Kentucky winery was at a greater advantage because of their in-state presence.[89] The necessity of an out-of-state winery having to use a wholesaler leads to an increased price to consumers, putting them in an unfair competitive position against a cheaper in-state alternative.[90] The Court agreed with the wineries argument that although the regulation was neutral on it's' face, the practical effect of the in-person requirement to purchase greatly disadvantaged out-of-state producers.[91] Similar to *Granholm,* the defendants' argued there was a strong state interest in preventing underage drinking, which was the function of the in-person requirement and tax collection.[92] However, the court rejected these arguments because there are reasonable means of verifying the age of a purchaser and collecting taxes through a condition of the direct shipping permit.[93]

More Recently in the Second Circuit, an out-of-state retailer challenged a New York Statute, which permitted an in-state retailer to obtain a permit to deliver alcohol directly to consumers, while an out-of-state retailer could not obtain such a permit without a presence in the state.[94] The Court rejected the Plaintiffs' argument that the statute discriminated against interstate commerce because of the in-state presence requirement.[95]The Plaintiffs' reliance on *Granholm* was misguided, while *Granholm* concerned in-state products receiving favoritism by being able to circumvent the Three Tier system, here the products in question have already passed through the first two regulatory tiers of the system before reaching the consumer.[96] The Court held that the regulation was valid under the dormant Commerce Clause and there was no discrimination because in-state and out-of-state retailers were on equal competitive grounds.[97]

Similarly, in the Fifth Circuit a Texas regulation regarding differential treatment of home deliveries which allowed in-state retailers to ship directly to Texans, while banning out-of-state retailers from doing so was valid under the Commerce Clause.[98] As in the Second Circuit, the Court refused to extend the holding of

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[85]*Id. quoting* KRS § 243.155(2)(g) (that wine may be ship to customer in Kentucky if "the wine is purchased by the customer in person at the small farm winery, the wine is shipped by licensed common carrier; and the amount of wine shipped is limited to two (2) cases per customer per visit.")
[86]*Id*.
[87]*Id*. ("Under Kentucky's in-person requirement, even if a winery has established a relationship with an individual consumer or a restaurant and has verified their age and shipping address, the customer must travel to the winery each time he or she wishes to execute a purchase.")
[88]*Id*.
[89]*Id*.
[90]*Id*.
[91]*Id*.
[92]*Id*.
[93]*Id*.
[94]*Arnold's Wines, Inc. v. Boyle*, 571 F.3d 185 (2d Cir. 2009).
[95]*Id*.
[96]*Id*.
[97]*Id*.
[98]*Wine Country Gift Baskets.com v. Steen*, 612 F.3d 809 (5th Cir. 2010)

Granholm to cases involving alcohol retailers and delivery, finding in favor of the Texas Three Tier system.[99]

In 2010, the constitutionality of direct-to-consumer shipping regulations was at issue in New Jersey.[100]The Third Circuit determined that a New Jersey statute allowing in-state, but not out-of-state, wineries to bypass wholesalers and sell directly to retailers and consumers was facially discriminatory under the *Granholm* analysis.[101] The Court then invalidated statute, which mandated that only one gallon of wine could be transported by an individual from out of state, unless that individual had a permit to do.[102] Similarly, New Jersey's reciprocity provision was for invalidated for not serving a legitimate public interest.[103]Interestingly, the Court ultimately found that New Jersey's ban on direct-to-consumer shipping to be constitutional.[104] The Court reasoned that New Jersey's ban on direct shipping was facially neutral and did not have a discriminatory effect on interstate commerce because in-state and out-of-state wineries were on equal competitive grounds.[105]

The First Circuit was confronted with the issued in *Family Winemakers of California v. Jenkins*. A Massachusetts Statute[106] prescribed the terms by which either an in-state or out-of-state small production winery could ship directly to consumers.[107] The regulation was facially neutral, however, its' practical effect provided in-state wineries with a distinct competitive advantage; all wineries within Massachusetts were within the 30,000 gallon production limits allowing them to bypass the Three Tier system.[108] By contrast, large scale wineries accounting for 98% of the market share were subject to price increases by passing through Massachusetts's Three Tier regulatory system.[109] The Court surmised, using the *Granholm* analysis, that the statute was unconstitutional due to the discriminatory competitive advantage to in-state producers while unnecessarily burdening most out-of-state wineries.[110]

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[99]*Id*.
[100]*Freeman v. Corzine*, 629 F.3d 146, 151-52 (3d Cir. 2010)
[101]*Id*.
[102]*Id*. *see* N.J. Stat. § 33:1–2(a) ("[a]lcoholic beverages intended in good faith solely for personal use may be transported, by the owner thereof ... from a point outside this State to the extent of ... one gallon of wine ... within any consecutive period of 24 hours; provided, however, that except pursuant to and within the terms of a license or permit issued by the director, no person shall transport into this State or receive from without this State into this State, alcoholic beverages where the alcoholic beverages are transported or received from a state which prohibits the transportation into that state of alcoholic beverages purchased or otherwise obtained in the State of New Jersey.")
[103]*Id*.
[104]*Id*. ("We reject [plaintiffs'] challenge to the direct shipping ban.")
[105]*Id*.
[106]Mass. Gen. Laws Ann. ch. 138, § 19F ("The commission may issue to an applicant, who: (1) operates a winery whose total annual production, including that of its affiliates, franchises and subsidiaries, is 30,000 gallons of wine or more; provided, however, any wine or wine product fermented from other than grapes shall not be included in the aforementioned 30,000 gallon figure; and (2) is authorized by the appropriate licensing authority to manufacture, export and sell wine, a large winery shipment license to sell and ship wine or winery products produced by the winery directly to consumers; provided that the winery has not contracted with or has not been represented by a wholesaler licensed under section 18 for the preceding 6 months.")
[107]592 F.3d 1 (1st Cir. 2010).
[108]*Id.*
[109]*Id.* (Large scale wineries who "produced between 30,001 and over 100 million gallons per year … accounted for 98 percent of all wine produced in the United States.")
[110]*Id.*

The Seventh Circuit tackled similar direct-to-consumer issues when an Indiana statute was called into question. [111] In essence, the statute allowed both in-state and out-of-state wineries to ship directly to Indiana consumers provided that the purchaser's age was verified in person once and that the winery did not act as a wholesaler.[112] The State argued that the statute served a legitimate purpose by protecting the integrity of the Three Tier System.[113] While the statute was reasonable on its' face, it effectively precluded California, Oregon and Washington from shipping directly to Indiana consumers because of their two-tier distribution systems which allow producers to sell directly to retailers within their respective states.[114]The Court concluded that due to the proportion of wine which is supplied by California, Oregon, and Washington, the effect of the statute created an unfair competitive advantage for Indiana Wineries that could ship directly-to-consumers.[115] Unlike in the Sixth Circuit holding in *Cherry Hill Vineyards*, the onetime face-to-face purchasing requirement to verify consumers' age did not disadvantage out-of-state wineries in the marketplace.[116]

The Fourth Circuit was concerned with the constitutionality of a Virginia regulation of personal importation, sale, and distribution of alcoholic beverage unless the alcohol went through the Three Tier system.[117] A common thread among these decisions is that the Three Tier Systems is constitutional and

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[111]Ind. Code Ann. § 7.1-3-26-7 ("Sec. 7. (a) The commission may issue a direct wine seller's permit to an applicant who meets all of the following requirements:
(1) The applicant is domiciled and has its principal place of business in the United States.
(2) The applicant is engaged in the manufacture of wine.
(3) The applicant holds and acts within the scope of authority of an alcoholic beverage license or permit to manufacture wine that is required:
(A) in Indiana or the state where the applicant is domiciled; and
(B) by the Tax and Trade Bureau of the United States Department of the Treasury.
(4) The applicant qualifies with the secretary of state to do business in Indiana and consents to the personal jurisdiction of the commission and the courts of Indiana.
(5) The applicant files a surety bond with the commission in accordance with IC 7.1-3-1, or deposits cash in an escrow account with the commission, in the amount required of an applicant for a vintner's permit under IC 7.1-3-1-7.
(6) The applicant:
(A) has not distributed wine through a wine wholesaler in Indiana within the one hundred twenty (120) days immediately preceding the applicant's application for a direct wine seller's permit and does not distribute wine through a wine wholesaler in Indiana during the term of the direct wine seller's permit; or
(B) has operated as a farm winery under IC 7.1-3-12.
(7) The applicant completes documentation regarding the applicant's application required by the commission.
(b) The commission may issue a direct wine seller's permit to an applicant who:
(1) meets the requirements under subsection (a); and
(2) holds a permit issued under this title that allows the sale of an alcoholic beverage at retail.")
[112]*Baude v. Heath*, 538 F.3d 608, 612 (7th Cir. 2008).
[113]*Id.*
[114]*Id.* ("California, Oregon, and Washington, which produce 93% of this nation's wine, have two-tier systems in which retailers buy from producers without a middleman.")
[115]*Id.*
[116]*Id.*
[117]Va. Code Ann. § 4.1-310 ("No alcoholic beverages, other than wine or beer, shall be imported, shipped, transported or brought into the Commonwealth, other than to distillery licensees or winery licensees, unless consigned to the Board… The provisions of this chapter shall not prohibit (i) any person from bringing, in his personal possession, or through United States Customs in his accompanying baggage, into

serves a legitimate purpose.[118] Here, the Virginia regulation was held to be valid because the one-gallon limit of out-of-state alcohol imported into Virginia for personal consumption actually favored interstate commerce because this alcohol would not be subject to the Three Tier system and subsequent price increases.[119] The Court found there was a legitimate state interest to promote its Three Tier regulation and since Virginia wineries were subject to the same shipping restrictions as an out-of-state producer, the statute was not discriminatory.[120]

The most recent decision in the line of *Granholm* cases occurred on September 23, 2013 in the Eighth Circuit. Unlike other states, Missouri had a Four Tier regulatory scheme.[121] Specifically, the first tier was the producer of the alcoholic beverage; the second tier was a state licensed solicitor that would procure the alcohol for the third tier of wholesalers who would provide the product to the fourth tier retailers.[122] In order to obtain a Missouri wholesale license, a corporation was required to be a "resident corporation".[123] This requirement was similar to the New York regulation in *Granholm* requiring that the corporation had a physical presence in the state and be incorporated in Missouri.[124] The action was brought by a Florida Corporation, Southern Wine and Spirits of America ("SWSA"), a large scale distributor of alcoholic beverages operating in 32 states.[125] A subsidiary of SWSA which was incorporated Missouri sought a wholesaler license, but was denied because the parent corporation lacked a physical state presence.[126]

The Court held that there was no violation of the dormant Commerce Clause in this instance due to the strong state interest in maintaining the integrity of the Three Tier system in accordance with *Granholm*.[127] Unlike *Granholm,* the physical presence requirement for a wholesaler versus a producer helps to achieve the goal of efficient regulation.[128] The Court reasoned that since wholesalers did not sell alcohol directly to the public and effectively acted as a middleman, there was no burden to interstate.[129] Therefore, there were no unfair competitive advantage favoring in-state wholesalers because they too would be subject to the licensing and in state presence requirement to operate in Missouri.[130]

Fixing an Imperfect System Although *Granholm* attempted to clarify these direct-to-consumer issues and bring uniformity to the wine industry, there are still conflicting opinions in line with Justice

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the Commonwealth not for resale, alcoholic beverages in an amount not to exceed one gallon or four liters if any part of the alcoholic beverages being transported is held in metric-sized containers, (ii) the shipment or transportation into the Commonwealth of a reasonable quantity of alcoholic beverages not for resale in the personal or household effects of a person relocating his place of residence to the Commonwealth, or (iii) the possession or storage of alcoholic beverages on passenger boats, dining cars, buffet cars and club cars, licensed under this title, or common carriers engaged in interstate or foreign commerce.")

[118] *See* North Dakota v. United States, 495 U.S. 423 (1990) (holding that the Three Tier system is "unquestionably legitimate".)

[119] *Brooks v. Vassar*, 462 F.3d 341, 344-45 (4th Cir. 2006).

[120] *Id*.

[121] See generally Mo.Rev.Stat. §§ 311.180(1), 311.200.

[122] *S. Wine & Spirits of Am., Inc. v. Div. of Alcohol & Tobacco Control*, 731 F.3d 799, 802 (8th Cir. 2013).

[123] *Id.*

[124] *Id.* see also note 57 *supra*.

[125] *Id.*

[126] *Id.*

[127] *Id.*

[128] *Id.*

[129] *Id.*

[130] *Id.*

Steven's opinion that alcohol is not a an ordinary consumer product and requires heighten levels of regulation.[131] Additionally, the Three Tier system has consistently been regarded both constitutionally sound as well as a necessary tool in promoting state interests.[132] As reported by the FTC, the wine industry is vibrant in a large part due to e-commerce and direct-to-consumer shipping but state regulations greatly hinder future growth at this time.[133]

One proposed solution has come in the form of reciprocity laws.[134] As of June 27, 2012, only seven states completely ban all forms of direct-to-consumer shipping.[135]In general, reciprocity laws regulate the shipment of wine from one state directly to a consumer in a second state provided that the second state is permitted to ship to the original state in a similar fashion.[136] The holding in *Granholm* seems to promote the idea of reciprocity, there is an incentive to both the State and winery to work together and allow for direct-to-consumer shipping. These regulations have proven to be effective with almost no increased instances of shipping to minors and increased underage drinking.[137]Further, States are well within their rights to collect taxes and require a license or permit to ship directly to an in-state consumer.[138] These facts seem to completely negate any concerns of states in terms of tax evasion or lost revenue.[139]

Even if a state is concerned with a private courier, such as Fed-Ex or UPS, and their ability to adequately verify age,[140]the US Postal service is in the process of changing their policies banning shipment of alcohol.[141] The Twenty-First Amendment effectively banned the use of using the Postal Service to ship alcohol.[142]The proposed changes would be a great step forward towards a unified national system regulating the shipment of alcohol. In effect, the national government would police any State concern of tax collection or underage drinking. The Postal Service would earn approximately $225 million in new revenue.[143] The proposed regulations would allow a federally licensed winery or brewery to legally ship

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[131]*Granholm* at 493.
[132]*Supra* Note 111
[133]*The Wine Report* at 3. ("State bans on interstate direct shipping represent the single largest regulatory barrier to expanded e-commerce in wine. More than half the states prohibit or severely restrict out-of-state suppliers from shipping wine directly to consumers. Many of these same states, however, allow intrastate direct shipping, such as from in-state wineries and retailers.")
[134] Paul Franson, *Direct Shipping Laws Outlined By State, http://www.winesandvines.com/template.cfm?content=102427&section=news,* June 27, 2012
[135]*Id.*
[136]*Possible Anticompetitive Barriers to E-Commerce: Wine* at 6.
[137] See chart in *The Wine Report* at 32 – 33.
[138]*Id.* at 38. ("Most of these states report few, if any, problems with tax collection. Nebraska, for example, reports that they "have also not, as yet, had any problems with the collection of excise tax[es]." North Dakota reports that "Taxes are collected. No problems to date that we are aware of." To the extent that states have problems with out-of-state suppliers, they have addressed the problem in less restrictive ways than banning all interstate direct shipping.")
[139]*Granholm supra* note 52.
[140]*Fed-Ex Alcohol Shipping Regulations*, http://www.fedex.com/us/developer/product/WebServices/MyWebHelp_August2010/Content/Proprietary_Developer_Guide/Alcohol_Shipping.htm.
[141] Ashley Hupfl, *Sen. Schumer Fights to End Alcohol Mail Restrictions*, http://www.usatoday.com/story/news/nation/2013/10/30/mail-alcohol-restrictions-proposal/3316837/, October 30, 2013.
[142]*Id.*
[143]*Id.*

to consumers' ages twenty-one and over, effectively rendering the underage drinking and tax evasion argument moot.[144]

The Future Alcoholic Beverages have a storied history in the United States acting as both a unifier and a divider of people. The Framers of the Constitution undoubtedly saw its effects, but could not have anticipated what the future would bring as the Nation continued to grow. Seemingly, the federal government's recognition of the growth of the alcohol industry that can be regulated by relatively simple means dispels Justice Steven's notion that alcohol is not an ordinary consumer product. Rather, it recognizes the nationwide market place due in large part to e-commerce. Access to a wider variety of brands and styles of wine and beer promoting interstate commerce appear to be in conformity with the founding principles of the United States favor change.

Granholm and the Circuit decisions that followed began laying the framework for a national system of direct-to-consumer shipping. This would not mean an abolishment of Three Tier Systems currently regulated by States. Instead, one federal shipping system working in tandem with state regulations would prove to be beneficial to the Government, Producers, and Consumers. Governments are well within their right to promote public safety and regulate the sale of alcohol, and it behooves producers to comply with these regulations or risk losing their license. The greatest benefit however is to the consumers who will be able to purchase higher quality products at a reduced cost, and in turn boosting the economy as a whole. One thing is clear, without the facilitation of the Internet and e-commerce; the alcoholic beverage market would not have experienced such substantial growth in a short time period. At time where anything can be purchased at the click of a button, introducing alcohol sales into the regular stream of e-commerce is a natural progression in the technological age.

[144] *Id.*