January 24, 2007

The Honorable Bill Cotty
Member, House of Representatives
8807 Two Notch Road
Columbia, South Carolina 29223

Dear Representative Cotty:

We received your letter addressed to Attorney General Henry McMaster concerning the impact of the recent United States Supreme Court ruling in Granholm v. Heald, 544 U.S. 460 (2005) on South Carolina statutes. You state: "The state permits in-state wineries to ship directly to consumers, but prohibits out-of-state wineries from doing the same. Out-of-state wineries that account for 99% of the wine shipment, have to sell to a wholesaler who collects the excise taxes and can only sell to licensed retailers." Accordingly, you ask for an Attorney General's opinion "regarding the South Carolina statutes that are in conflict with the ruling [in Granholm v. Heald]." You add: "My primary concerns are with § 61-4-720 and § 61-4-730 of the South Carolina Code, as amended."

Law/Analysis

As you mentioned in your letter, in 2005 the United States Supreme Court decided the case of Granholm v. Heald, 544 U.S. 460 (2005). Several out-of-state wineries and state residents brought this case challenging Michigan's and New York's laws pertaining to the distribution of alcohol, claiming that such laws violate the Commerce Clause of the United States Constitution. Id. According to the Court's opinion, both Michigan and New York regulate the sale of alcoholic beverages through three-tiered systems. Id. at 466. Under Michigan's law, producers or distillers of alcohol must sell only to licensed in-state wholesalers, wholesalers may only sell to retailers, and retailers may sell to consumers. Id. at 469. However, Michigan provides for an exception for in-state wineries, "which are eligible for 'wine maker' licenses that allow direct shipment to in-state consumers." Id.

New York also has a three-tiered system that provides for an exception for in-state wineries, which allows them to sell directly to consumers in New York. Id. at 470. In addition, New York also permits out-of-state wineries that produce wine from grapes grown in New York to obtain a license that allows them to ship wine directly to consumers in New York. Id. But, as part of the requirement for obtaining a license, the out-of-state winery must establish "'a branch

factory, office or storeroom within the state of New York.'" Id. (quoting N.Y. Alco. Bev. Law Ann. § 3(37)).

The Court cited the following as the test to determination whether the Michigan and New York laws violate the Commerce Clause: "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.'" Id. at 472 (quoting Oregon Waste Sys., Inc. v. Dep't of Envt'l Quality of Oregon., 511 U.S. 93, 99 (1994)). Employing this test, the Court determined these bodies of law "deprive citizens of their right to have access to the markets of other States on equal terms." Id. at 473. Specifically, with regard to the Michigan law, the Court noted that by requiring out-of-state wineries to proceed through the three-tier system, from which the in-state wineries are exempt, increases "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." Id. at 474. The Court determined the New York law also showed clear evidence of discrimination in its in-state presence requirement, which the Court commented "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.'" Id. at 475 (quoting Halliburton Oil Well Cementing Co. v. Reily, 373 U.S. 64, 72 (1963)). The Court noted the ineligibility of out-of-state wineries to obtain a farm winery license also showed evidence of further discrimination. Id.

Upon finding that the Michigan and New York laws discriminated against interstate commerce, the Court further addressed the states' argument that their laws are "saved by § 2 of the Twenty-first Amendment . . . ." Id. at 476. This provision states: "'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.'" Id. (quoting U.S. Const. amend. XXI, § 2). In response, the Court stated:

> 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.

Id. at 484-85. The Court concluded:

> State policies are protected under the Twenty-first Amendment when they treat liquor produced out of state the same as its domestic equivalent. The instant cases, in contrast, involve straightforward attempts to discriminate in favor of local producers. The discrimination is contrary to the Commerce Clause and is not saved by the Twenty-first Amendment.

Id. at 489.

Despite finding the states' laws are not saved by the Twenty-First Amendment, the Court continued its Commerce Clause analysis by considering "whether either state regime 'advances a legitimate local purpose that cannot be adequately served by reasonable nondiscriminatory alternatives.'" Id. at 490 (quoting New Energy Co. of Indiana v. Limbach, 486 U.S. 269, 278 (1988)). The states presented two arguments in this regard. One, they argued these laws keep alcohol out of the hands of minors and two, they facilitate the collection of taxes. Id. First, with regard to the threat of increased alcohol consumption by minors, the Court determined the states provided little evidence of this threat.

> 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.'"

Id. (citations omitted). In addition, the Court noted that under Michigan's and New York's laws, minors may order wine from in-state wineries.

> 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.

Id. Furthermore, "the States can take less restrictive steps to minimize the risk that minors will order wine by mail. For example, the Model Direct Shipping Bill developed by the National Conference of State Legislatures requires an adult signature on delivery and a label so instructing on each package." Id. at 490-91.

Next, the states argued that allowing out-of-state wineries to ship directly to their consumers interferes with their collection of taxes on imported wines. Id. at 491. The Court also rejected this argument in finding Michigan and many other states do not rely on wholesalers to collect taxes. Id. Rather, taxes are collected directly from the wineries on all wine shipped to in-state wholesalers. Id. As for New York, the Court noted:

> their concerns are not wholly illusory, their regulatory objectives can be achieved without discriminating against interstate commerce. 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.

Id. Moreover, the Court commented on the fact that federal laws "supply incentives for wineries to comply with state regulations" in finding "[t]hese federal remedies, when combined with state licensing regimes, adequately protect States from lost tax revenue." Id. at 492.

Accordingly, the Court found Michigan and New York did not meet their burden in showing the discrimination under the statutes is justified. Id. Thus, it proclaimed the Michigan and New York laws in question unconstitutional due to their violation of the Commerce Clause. Id. "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." Id. at 493.

Chapter 4 of title 61 of the South Carolina Code sets forth the regulatory framework for the sale of beer and wine in South Carolina. According to this framework, South Carolina, like Michigan and New York, employs a three-tier distribution system for the sale of wine. Under this system, wholesalers may only purchase wine from licensed manufactures or importers of wine and manufacturers may only sell wine to a person holding a wholesale permit. S.C. Code Ann. § 61-4-310 (Supp. 2005); S.C. Code Ann. § 61-4-735(A) (Supp. 2005). Wholesalers in turn, may only sell wine to other licensed wholesalers or to licensed retailers. Id. However, sections 61-4-720 and 61-4-730 of the South Carolina Code (Supp. 2005), which you refer to in your letter, provide exemptions to this general rule. Section 61-4-720 states:

> Notwithstanding another provision of law, a licensed winery located in this State is authorized to sell wine produced on its premises with a majority of the juice from fruit and berries which are grown in this State with an alcoholic content of sixteen percent or less on the winery premises and deliver or ship this wine to consumer homes in or outside the State. These wineries are authorized to provide, with or without cost, wine taste samples to prospective customers.

Furthermore, section 61-4-730 adds:

> Permitted wineries which produce and sell wine produced on its premises with a majority of the juice from fruit and berries which are grown in this State may sell the wine at retail, wholesale, or both, and deliver or ship the wine to the purchaser in the State. Wine must be delivered between 7:00 a.m. and 7:00 p.m.

Based upon your letter, we gather you are concerned with whether or not these provisions violate the Commerce Clause, as did the Michigan and New York statutes in Granholm. Before we address this concern, we must keep in mind that "[a]ll statutes are presumed constitutional and will, if possible, be construed so as to render them valid." Horry County School Dist. v. Horry County, 346 S.C. 621, 631, 552 S.E.2d 737, 742 (2001). Furthermore, we recognize that only a court, not this Office, may deem a statute unconstitutional. Op. S.C. Atty. Gen., July 19, 2006. Thus, unless and until a court renders these statutes unconstitutional, they remain valid and enforceable. Op. S.C. Atty. Gen., October 27, 2006.

Sections 61-4-720 and 61-4-730 allow in-state wineries to bypass the general three-tier distribution system and allow wineries to sell wine directly to retailers and consumers, so long as a majority of the juice from the fruit comes from berries grown in the State. Section 61-4-720, in particular allows wine producers not only to sell wine to consumers on their premises, but allows them to ship wine to consumers at their homes. Based on our reading of these statutes, we find them similar to those ruled unconstitutional by the Supreme Court in Granholm. These statutes allow local wineries to sell wine to retailers and consumers, but do not afford the same privilege to out-of-state wineries. Because the statutes expressly apply these exemptions to in-state wineries, they appear facially discriminatory because they treat in-state and out-of-state wineries differently in a way that benefits the in-state wineries and burdens the out-of-state wineries. Therefore, we opine that a court, like the Supreme Court in Granholm, would likely find these statutes violate the Commerce Clause.

As we noted above, the Court in Granholm considered whether the Michigan and New York statutes, despite their discriminatory nature, served a legitimate local purposes that could not be adequately served by reasonable nondiscriminatory alternatives. Granholm, 544 U.S. at 490. In that case, the Court concluded the states did not meet their burden of proving the discrimination under the Michigan and New York statutes is justified. Id. The Court rejected the arguments that these statutes were the only way to keep alcohol out of the reach of minors and to facilitate collection of taxes. Id. at 490-92.

Many cases arose after Granholm challenging state laws governing the sale of wine by out-of-state wineries. While many of the statutes challenged differ from those addressed in Granholm and our South Carolina laws, we find their discussions regarding whether these statutes served a legitimate local purpose to be of interest in our analysis. For example, the United States District Court for the Western District of Washington addressed a Washington statute exempting in-state wineries and breweries from Washington's three-tiered distribution system, thereby allowing these wineries and breweries to distribute directly to retailers and consumers. Costco Wholesale Corp. v. Hoen, 407 F.Supp.2d 1247 (W.D .Wash., 2005). The District Court, relying on Granholm, found the Washington statutes exempting in-state wineries and breweries impermissibly discriminatory under the Commerce Clause. Id. at 1252. That Court also addressed arguments asserted by the defendants, the Liquor Control Board and the Washington Beer and Wine Wholesalers Association, claiming these statutes serve two local

purposes justifying their discriminatory nature. Id. First, the defendants argued these statutes ensure the orderly distribution of beer and wine. Id. The Court rejected this argument stating:

> The Court finds that Defendants have not produced sufficient evidence to create a genuine issue of material fact on whether discrimination against out-of-state producers is demonstrably justified to ensure orderly distribution of beer and wine. Defendants' arguments are largely speculative and conclusory. Much like in Granholm, Defendants provide "little concrete evidence for the sweeping assertion that they cannot police direct shipments by out-of-state" producers. Granholm, 125 S.Ct. at 1907. The state must provide "more than mere speculation to support discrimination against out-of-state goods." Id. Under these standards, Defendants have not made a sufficient showing to avoid summary judgment.

Id. at 1253.

Second, the defendants argued the laws were necessary to facilitate the collection of taxes. Id. Again, the Court concluded that the defendants did not provide sufficient evidence to support this claim. Id. at 1254. Furthermore, the Court suggested that Washington revoke the exemption for in-state wineries and breweries as a non-discriminatory alterative to the current law, stating "that would address Defendents' professed concerns about ensuring orderly distribution of beer and wine and facilitating tax collection . . . ." Id.

Recently, in Cherry Hill Vineyard, LLC v. Baldacci, Civil No. 05-156-B-W, slip op. (D. Me. July 27, 2006), the United States District Court for the District of Maine addressed the constitutionality of a Maine statute allowing out-of-state wineries to sell directly to consumers only if they established an in-state location. The Court analyzed the Maine statute in light of Granholm, but for various reasons came to the conclusion that the statute did not violate the Commerce Clause. Id. Furthermore, the Court rejected the plaintiff's argument that "if local retailers can make direct sales that are readily feasible, as a practical matter, then out-of-state retailers must be afforded a similarly practical means of entering into direct transactions with Maine consumers." Id. at 9.

> If the requirement of "face-to-face" or "on-premises" transactions were applied to an innocuous article of interstate commerce such as clothing, which is not subject to any age restriction or other public health restriction (let alone the Twenty-first Amendment), then it would be difficult to understand what rational basis might exist for prohibiting mail order purchases. But here the patently obvious circumstances are that the subject matter of the statutory scheme is wine, wine is an alcoholic beverage that is contraband

> when placed in certain minors' hands, and the State has concluded that mail order transactions cannot reliably be policed in order to protect certain minors from themselves. It is not for this Court to second-guess that policy determination in favor of the plaintiffs' free market perspective. Were it the case that Maine, like New York or Michigan, had concluded that the risk to minors was tolerable and had authorized in-state retailers to sell alcohol to consumers in Maine by mail order, then it would follow that Maine could not bar out-of-state retailers from participating in that market without running afoul of the Commerce Clause. That is precisely the holding of Granholm. But because Maine has not authorized any local retailers to fill orders for wine that are not made on the retailer's premises by individuals of legal drinking age and because the Commerce Clause does not require Maine to permit mail order purchases of wine simply because it is the most practical means of affording remote, out-of-state wineries with access to Maine consumers, the on-premises restriction on sales simply does not impose any cognizable burden on interstate commerce that could possibly outweigh the putative local benefit of regulating minors' access to alcohol.

Id. Accordingly, the Maine District Court, under these circumstances, recognizes that the protection of minors can be a legitimate local purpose for which no non-discriminatory alternative is available.

From the decisions cited above, certainly there are many local purposes that one could assert to justify the discriminatory nature of a law. While the Court in Granholm and the Court in Costco rejected these arguments due to the defendants' failure to provide evidence sufficient to justify the discrimination, the Court in Cherry Hill Vineyard found the defendant's arguments persuasive. From these opinions, we gather that the determination of whether a legitimate local purpose exists, which cannot be served by less discriminatory alternatives, involves an analysis of the purported local purposes and the less discriminatory means by which these local purposes may be served. We cannot fathom all of the local purposes and the alternatives to them within the scope of an opinion of this Office. Moreover, the analysis involved in considering the purposes that may be asserted would require us to delve into a factual analysis. As we have stated on numerous occasions, only a court, not this Office, may resolve questions of fact. See Op. S.C. Atty. Gen., September 21, 2006 ("As we acknowledge in numerous opinions, this Office does not have the jurisdiction of a court to investigate and determine factual issues."). Therefore, we must defer to a court to determine whether or not the discriminatory nature of sections 61-4-720 and 61-4-730 are justified.

Conclusion

Based on our reading of the Supreme Court's decision in Granholm, finding statutes similar to sections 61-4-720 and 61-4-730 discriminatory and in violation of the Commerce Clause, we believe a court would find these provisions of the South Carolina Code impermissibly discriminate against interstate commerce. However, we acknowledge that under certain circumstances, such discrimination may be justified presuming the discriminatory statute serves a legitimate local purpose that cannot be adequately served by nondiscriminatory means. While the Court in Granholm found insufficient evidence of the justifications asserted by the defendants in that case, a court addressing the same or different arguments may conclude otherwise in this instance. Nonetheless, whether the statutes in questions serve such a legitimate local purpose is a question of fact, which may only be resolved by a court. As such, we are unable to express an opinion as to the constitutionality of these two provisions. However, because courts generally look to legislative findings in considering the constitutionality of a statute, we suggest that an amendment to sections 61-4-720 and 61-4-730 to include the policy supporting these provisions could prove helpful if these statutes are challenged in court.

Very truly yours,

Cydney M. Milling
Assistant Attorney General

REVIEWED AND APPROVED BY:

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Robert D. Cook
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