

# A Post-*Granholm* Analysis of Iowa's Regulatory Framework for Wine Distribution

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*ABSTRACT: Wine-distribution laws across the country have been in considerable flux since the Supreme Court's 2005 decision in Granholm v. Heald, which struck down New York and Michigan laws regulating the direct shipment of wine to consumers as impermissible burdens on interstate commerce. Two Iowa statutes are potential litigation targets in light of Granholm: Iowa's reciprocal-shipment statute, which regulates the direct shipment of out-of-state wine to Iowa consumers, and Iowa's native-wine statute, which provides exclusive privileges for Iowa native-wine manufacturers. This Note concludes that certain provisions of both statutes are likely unconstitutional under a Granholm analysis and recommends that Iowa adopt a direct-shipment permit system to regulate the direct shipment of wine to consumers.*

I. INTRODUCTION.....	667
II. BACKGROUND .....	668
A. U.S. WINE DISTRIBUTION .....	668
B. THE COMMERCE CLAUSE.....	670
C. ALCOHOL REGULATION IN HISTORICAL CONTEXT .....	671
1. Pre-Prohibition Regulation .....	671
2. Twenty-First Amendment Jurisprudence .....	673
D. GRANHOLM V. HEALD .....	676
1. The Court's Analysis .....	676
2. The <i>Granholm</i> Aftermath .....	678
III. IOWA'S WINE-DISTRIBUTION LAWS.....	679
A. OVERVIEW OF WINE REGULATION IN IOWA .....	679
B. IOWA'S RECIPROCAL-SHIPMENT STATUTE.....	680

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1. Statutory Interpretation.....	681
2. Constitutional Analysis.....	682
C. <i>IOWA'S NATIVE-WINE STATUTE</i> .....	683
1. Iowa's Wine Industry.....	683
2. Statutory Interpretation.....	684
3. Constitutional Analysis.....	686
IV. RECOMMENDATIONS FOR STATUTORY CHANGE.....	687
V. CONCLUSION .....	690

## I. INTRODUCTION

The state best known for rolling fields and rows of corn has a budding niche in hilltop chateaus and vines of grapes. Iowa's wine industry has experienced significant growth in the past decade, with vineyards and wineries taking root in nearly all of the state's ninety-nine counties.<sup>1</sup> Between 1999 and 2006, the number of vineyards in Iowa jumped from 15 to more than 325; the number of wineries from 13 to 63; and the number of acres dedicated to grape-growing from 63 to more than 650.<sup>2</sup>

This growth comes during a tumultuous time for wine-distribution laws across the country. In 2005, the Supreme Court struck down Michigan and New York laws regulating the direct shipment of wine to consumers as violations of the dormant Commerce Clause in *Granholm v. Heald*.<sup>3</sup> The Court held that if states allow the direct shipment of wine to consumers, they cannot discriminate against out-of-state wineries in favor of in-state wineries.<sup>4</sup> The decision prompted many states to reconsider how they regulate out-of-state wineries' and retailers' access to in-state consumers; to this day, the nation's dockets continue to fill with litigation challenging the constitutionality of state wine-distribution laws.<sup>5</sup>

*Granholm* illuminated the complex legal and policy dynamics at play in state wine-distribution laws. At *Granholm's* core was a tension between two constitutional doctrines: the dormant Commerce Clause, which prohibits states from enacting laws that place an undue burden on interstate commerce,<sup>6</sup> and Section 2 of the Twenty-first Amendment, which addresses states' power to regulate alcohol within their borders.<sup>7</sup> From a policy perspective, wine-distribution laws implicate many strongly held interests:

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1. PAUL OVROM, IOWA DEP'T OF AGRIC. & LAND STEWARDSHIP, ANNUAL REPORT OF THE IOWA GRAPE AND WINE DEVELOPMENT COMMISSION FOR FISCAL YEAR 2007, at 14 (2007), available at [http://www.iowaagriculture.gov/Horticulture\\_and\\_FarmersMarkets/pdfs/GrapeWineCommFY07AnnualRpt.pdf](http://www.iowaagriculture.gov/Horticulture_and_FarmersMarkets/pdfs/GrapeWineCommFY07AnnualRpt.pdf) (documenting the increase in Iowa's annual wine production from 51,500 gallons in 2002 to 246,000 gallons in 2006); Michael L. White, Iowa State Univ., Univ. Extension, Iowa Grape Expectations (June 2008), <http://www.extension.iastate.edu/NR/rdonlyres/7EA8AF05-9A03-4F07-9DA2-DDD6E59A40D0/80249/608VineWineMap.pdf> (tracking the number of vineyards and wineries in each Iowa county).

2. Iowa State Univ., Univ. Extension, Recent Iowa History, <http://www.extension.iastate.edu/NR/rdonlyres/A04D85D0-1934-4BF6-8010-68DBFA021C6/76483/RecentIowaHistory0002.pdf> (last visited Jan. 21, 2009) (charting the number of acres, vineyards, and wineries in Iowa each year from 1999 to 2006).

3. *Granholm v. Heald*, 544 U.S. 460, 493 (2005).

4. See *infra* Part II.D.1 (analyzing the *Granholm* decision).

5. Lynne Marek, *Legal Battle Over Wine Shipments Has Ripened: High Court Case Fails to Settle a Thorny Issue*, NAT'L L.J., Jan. 21, 2008, available at <http://www.law.com/jsp/article.jsp?id=900005559787> (noting challenges to state laws despite state legislative changes to comply with *Granholm*).

6. See *infra* Part II.B (surveying the dormant Commerce Clause).

7. See *infra* Part II.C (tracing the evolution of the Court's Twenty-first Amendment jurisprudence).

oenophiles want to buy otherwise-inaccessible wine via the Internet, while states worry that direct shipment increases the risk of underage drinking; small wineries want to reach geographically remote customers, while the business of alcohol wholesalers depends on wine traveling through the three-tier system and not directly to consumers.<sup>8</sup>

This Note addresses two Iowa wine statutes that are potential litigation targets in light of *Granholm* and its aftermath: Iowa's reciprocal-shipment statute and Iowa's native-wine statute. To contextualize the analysis of the two statutes, Part II provides an overview of U.S. wine distribution and the Commerce Clause before tracing state alcohol regulation from its pre-Prohibition roots to the Court's 2005 decision in *Granholm*. Part III begins with a synopsis of wine regulation in Iowa and continues with the statutory and constitutional analysis of the native-wine and reciprocal-shipment laws. This Note determines that certain provisions of each statute are likely unconstitutional in light of *Granholm*. Part IV recommends that the Iowa legislature consider redacting certain provisions of the native-wine statute and institute a direct-shipment permit system to regulate the direct shipment of wine to Iowa consumers.

## II. BACKGROUND

### A. U.S. WINE DISTRIBUTION

The majority of states, including Iowa, regulate the licensing and distribution of alcoholic beverages through a "three-tier" system.<sup>9</sup> The three-tier system is comprised of manufacturers, wholesalers, and retailers.<sup>10</sup> Wine distribution generally proceeds as follows: licensed wine manufacturers (i.e., vintners) sell their products to licensed wholesalers; wholesalers pay excise taxes and deliver wine to licensed retailers; retailers then sell directly to the public and collect sales taxes where applicable.<sup>11</sup> State and federal "tied-house" restrictions prohibit vertical integration between the tiers—for example, manufacturers and wholesalers normally cannot make retail sales.<sup>12</sup>

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8. See FED. TRADE COMM'N, POSSIBLE ANTICOMPETITIVE BARRIERS TO E-COMMERCE: WINE 3–5 (2003) [hereinafter FTC WINE REPORT], available at <http://www.ftc.gov/os/2003/07/winereport2.pdf> (surveying the interests implicated in the direct-shipment debate).

9. *Id.* at 5–6 (noting that states developed the three-tier system after the repeal of Prohibition to facilitate state tax collection, to limit sales to minors, and to prevent organized crime from meddling in alcohol distribution).

10. *Id.*

11. *Id.* at 5. Federal regulations require wine manufacturers to obtain a permit from the Alcohol and Tobacco Tax and Trade Bureau to sell their wine. 27 C.F.R. § 1.21 (2008).

12. See IOWA CODE § 123.45 (2007) (prohibiting manufacturers and wholesalers of alcoholic beverages from holding a retail permit or having any interest in the operation of retail licensees); *id.* § 123.186 (adopting the substance of 27 C.F.R. pt. 6 relating to prohibited transactions between wholesalers and retailers); *Auen v. Alcoholic Beverages Div.*, Iowa Dep't of

Wine direct-shipment laws regulate whether entities may bypass the three-tier system by shipping wine directly to consumers.<sup>13</sup> States have generally taken one of three approaches in regulating wine direct shipment: (1) prohibition, (2) limited importation, and (3) reciprocity.<sup>14</sup>

Approximately fifteen states prohibit the direct shipment of wine to their residents.<sup>15</sup> Some of these “closed” states make the direct shipment of wine a misdemeanor, while others make it a felony.<sup>16</sup> States prohibit direct shipment to maintain full control over alcohol distribution, justifying the laws as necessary to promote temperance, collect taxes, and dissuade underage drinking.<sup>17</sup>

Approximately thirty-three states employ a limited-importation system, allowing wine manufacturers to ship wine directly to residents, subject to various restrictions.<sup>18</sup> State law may require shippers to obtain a permit, to pay fees, and to use special shipping labels.<sup>19</sup> Other restrictions include on-site purchase requirements and caps on the volume of wine that residents may import annually.<sup>20</sup>

Reciprocity systems permit consumers to receive wine directly from shippers in another reciprocity state while restricting or prohibiting direct shipments from nonreciprocity states.<sup>21</sup> The use of this system has declined precipitously in just the past five years: in 2003, thirteen states employed

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Commerce, 679 N.W.2d 586, 591 (Iowa 2004) (affirming that the legislative intent behind Iowa Code section 123.45 is to “prohibit any ownership interest, no matter how remote or de minimis, by a manufacturer, wholesaler, or other entity in the chain of alcohol beverage distribution and the retailer of these beverages”).

13. FTC WINE REPORT, *supra* note 8, at 7. Consumers normally receive direct shipments at their home or workplace via common carriers such as FedEx or UPS. *Id.*

14. *Id.*

15. Wine Inst., Direct Shipment Map, [http://www.wineinstitute.org/files/direct\\_shipping\\_laws\\_map.pdf](http://www.wineinstitute.org/files/direct_shipping_laws_map.pdf) (last visited Nov. 14, 2008). States that prohibit the direct shipment of wine to consumers include Alabama, Arkansas, Delaware, Kentucky, Maine, Maryland, Massachusetts, Mississippi, Montana, New Jersey, Oklahoma, Pennsylvania, South Dakota, Tennessee, and Utah. *Id.* For an argument that anti-direct-shipment laws are unconstitutional, see Lauren Dunnock, Comment, “Quaffable, But Far from Transcendent”: Maryland’s 21st Century Prohibition, 36 U. BALT. L. REV. 271, 296 (2007).

16. FTC WINE REPORT, *supra* note 8, at 8.

17. Alan E. Wiseman & Jerry Ellig, *How Many Bottles Make a Case Against Prohibition? Online Wine and Virginia’s Direct Shipment Ban* 3 (2003), in FTC WINE REPORT, *supra* note 8, app. A.

18. Wine Inst., *supra* note 15. Limited-importation states include Alaska, Arizona, California, Colorado, Connecticut, Florida, Georgia, Hawaii, Idaho, Illinois, Indiana, Kansas, Louisiana, Michigan, Minnesota, Missouri, Nebraska, Nevada, New Hampshire, New York, North Carolina, North Dakota, Ohio, Oregon, Rhode Island, South Carolina, Texas, Vermont, Virginia, Washington, West Virginia, Wisconsin, and Wyoming. *Id.* The District of Columbia also falls into this category. *Id.*

19. FTC WINE REPORT, *supra* note 8, at 8.

20. See *infra* notes 81–82 and accompanying text (noting recent litigation that challenges such restrictions as impermissible burdens on interstate commerce).

21. FTC WINE REPORT, *supra* note 8, at 7–8. Reciprocity statutes normally set annual limits on the volume of wine that consumers can receive. *Id.*

reciprocity systems;<sup>22</sup> as of late 2008, only Iowa and New Mexico have reciprocity statutes.<sup>23</sup> The reciprocity model came into force in the 1990s and was intended to level the playing field for small wineries by allowing them to bypass the three-tier distribution scheme and take advantage of Internet commerce to make sales to out-of-state consumers.<sup>24</sup> As this Note explores below, the Supreme Court's 2005 decision in *Granholm v. Heald* has prompted almost all of the former reciprocity states to shift to permit-based systems.<sup>25</sup>

### B. THE COMMERCE CLAUSE

As the distribution laws above indicate, the issue of how states regulate out-of-state wineries' access to in-state consumers is an issue of interstate commerce. The Commerce Clause empowers Congress to "regulate commerce with foreign nations, and among the several States."<sup>26</sup> The dormant Commerce Clause is the negative corollary to this affirmative grant of power and prevents states from discriminating against out-of-state commerce absent a substantial, nonprotectionist interest.<sup>27</sup> The Court's modern dormant Commerce Clause analysis is driven by "concern about 'economic protectionism—that is, regulatory measures designed to benefit in-state economic interests by burdening out-of-state competitors.'"<sup>28</sup>

The Supreme Court uses a two-tiered approach to analyze state economic regulation under the dormant Commerce Clause.<sup>29</sup> A state law faces a virtual per se rule of invalidity when it "directly regulates or discriminates against interstate commerce, or when its effect is to favor in-

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22. *Id.* at 7.

23. Wine Inst., *supra* note 15; see N.M. STAT. § 60-7A-3(E) (2008) ("Any individual or licensee in a state which affords New Mexico licensees or individuals an equal reciprocal shipping privilege may ship for personal use . . . not more than two cases of wine . . . per month to any individual not a minor in this state."); *infra* Part III.B (analyzing Iowa's reciprocal-shipment statute). During the 2008 legislative session, the New Mexico legislature rejected a bill that would have replaced the state's reciprocal-shipment statute with a permit system. Posting of Sarah Werner to ShipCompliant Blog, Reciprocity Lives (Well, at Least in New Mexico), <http://shipcompliantblog.com/blog/2008/02/18/reciprocity-lives-well-at-least-in-new-mexico> (Feb. 18, 2008, 10:21).

24. Michael A. Pasahow, *Granholm v. Heald: Shifting the Boundaries of California's Reciprocal Wine Shipping Laws*, 21 BERKELEY TECH. L.J. 569, 575 (2006).

25. See *infra* Part II.D.2 (detailing *Granholm's* aftermath).

26. U.S. CONST. art. 1, § 8, cl. 3.

27. Todd Zywicki & Asheesh Agarwal, *Wine, Commerce, and the Constitution*, 1 N.Y.U. J.L. & LIBERTY 609, 610–12 (2005).

28. Dep't of Revenue of Ky. v. Davis, 128 S. Ct. 1801, 1808 (2008) (quoting New Energy Co. of Ind. v. Limbach, 486 U.S. 269, 273–74 (1988)).

29. Brown-Forman Distillers Corp. v. N.Y. State Liquor Auth., 476 U.S. 573, 578–79 (1986).

state economic interests over out-of-state interests.”<sup>30</sup> A law in this first tier is subject to strict scrutiny and the Court will uphold the law only if it “advances a legitimate local purpose that cannot be adequately served by reasonable nondiscriminatory alternatives.”<sup>31</sup> If a state economic regulation has only “incidental” effects on interstate commerce, the Court employs intermediate scrutiny and will uphold the law unless “the burden imposed on [interstate] commerce is clearly excessive in relation to the putative local benefits.”<sup>32</sup> As discussed below, the litigation over the constitutionality of wine-distribution laws is grounded in the intersection of the dormant Commerce Clause with the Twenty-first Amendment.

### C. ALCOHOL REGULATION IN HISTORICAL CONTEXT

Contemporary wine-distribution laws are much more than isolated statutory exercises in logistics; they are the products of an ongoing debate regarding U.S. alcohol regulation that is as old as the nation itself. Understanding how states historically have regulated alcohol provides the necessary context to understand current litigation over wine-distribution laws.

#### 1. Pre-Prohibition Regulation

State alcohol regulation dates back to the nineteenth century, when the temperance movement prompted many states to pass laws restricting or banning the manufacture and sale of alcoholic beverages within their borders.<sup>33</sup> In initial challenges, the Supreme Court upheld such laws as valid exercises of states’ police powers.<sup>34</sup> However, the Court was less solicitous when the state law in question regulated the importation of out-of-state alcohol for in-state delivery.<sup>35</sup> Iowa, in fact, took center stage in the Court’s pre-Prohibition invalidations of state regulations on imported alcohol.<sup>36</sup>

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30. *Id.* at 579. “[A] law will be regarded as facially discriminatory if its terms draw a distinction between in-staters and out-of-staters.” ERWIN CHEMERINSKY, *CONSTITUTIONAL LAW: PRINCIPLES AND POLICIES* 433 (3d ed. 2006).

31. *Or. Waste Sys., Inc. v. Dep’t of Env’tl. Quality of Or.*, 511 U.S. 93, 101 (1994) (quoting *Limbach*, 486 U.S. at 278).

32. *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970) (“[T]he extent of the burden that will be tolerated will of course depend on the nature of the local interest involved, and on whether it could be promoted as well with a lesser impact on interstate activities.”).

33. *Zywicki & Agarwal*, *supra* note 27, at 613.

34. *See Mugler v. Kansas*, 123 U.S. 623, 660–61 (1887) (upholding Kansas’s constitutional amendment prohibiting the manufacture and sale of intoxicating liquors); *The License Cases*, 46 U.S. (5 How.) 504, 576–77 (1847) (maintaining that if a state found that traffic in “ardent spirits” was “injurious to its citizens, and calculated to produce idleness, vice, or debauchery . . . nothing in the constitution of the United States” prevented that state from “regulating and restraining the traffic, or from prohibiting it altogether”).

35. *Zywicki & Agarwal*, *supra* note 27, at 613.

36. *Leisy v. Hardin*, 135 U.S. 100, 124–25 (1890); *Bowman v. Chi. & Nw. Ry. Co.*, 125 U.S. 465, 474 (1888).

In *Bowman v. Chicago & Northwest Railway Co.*, the Court struck down an Iowa statute that prohibited common carriers from bringing intoxicating liquors from any other state into Iowa without a permit.<sup>37</sup> Just two years later, the Court invalidated Iowa's ban on the sale of imported liquor in *Leisy v. Hardin*.<sup>38</sup> In both cases, the Court struck down the regulations under the original-package doctrine, which immunized interstate goods from state regulation if they remained in their original packages.<sup>39</sup> While the Court has since abandoned the original-package doctrine, these initial cases are notable for the subsequent legislation that they prompted from Congress.

Congress passed the Wilson Act in 1890 in response to the regulatory bind in which the states found themselves following the Court's initial decisions: states could ban production of domestic liquor outright but could not regulate out-of-state liquor if it was in its original package.<sup>40</sup> The Wilson Act allowed states to regulate out-of-state liquor "to the same extent and in the same manner" as domestic liquor.<sup>41</sup> The Court interpreted the Wilson Act as overruling the original-package doctrine and reconciling the state's regulatory authority over alcohol with its obligation to not discriminate against interstate commerce.<sup>42</sup>

The apparent reconciliation was short-lived. After alcohol importers began exploiting a direct-shipment loophole under the Act, the Court confirmed that the Wilson Act only authorized the states to regulate the resale of imported liquor—and did not allow states to ban direct interstate alcohol shipments to consumers for personal use.<sup>43</sup> Congress responded with the Webb–Kenyon Act in 1913, an Act that "[d]ivest[ed] intoxicating

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37. *Bowman*, 125 U.S. at 500 ("[T]he power to regulate or forbid the sale of a commodity, after it has been brought into the State, does not carry with it the right and power to prevent its introduction by transportation from another State.").

38. *Leisy*, 135 U.S. at 124–25 (striking down a ban on the sale of imported liquor).

39. Zywicki & Agarwal, *supra* note 27, at 614.

40. Compare *supra* text accompanying note 34 (noting that the Court upheld some regulations under the states' police powers), with *supra* text accompanying note 39 (noting that the Court struck down regulations under the original-package doctrine).

41. Wilson Act, ch. 728, 26 Stat. 313 (1890) (codified at 27 U.S.C. § 121 (2000)). The Wilson Act provided as follows:

[A]ll fermented, distilled, or other intoxicating liquors . . . transported into any State . . . shall upon arrival in such State . . . be subject to the . . . laws of such State . . . to the same extent and in the same manner as though such liquids or liquors had been produced in such State or Territory, and shall not be exempt therefrom by reason of being introduced therein in original packages or otherwise.

*Id.*

42. *Scott v. Donald*, 165 U.S. 58, 100 (1897) ("[The Wilson Act] was not intended to confer upon any State the power to discriminate injuriously against the products of other States in articles whose manufacture and use are not forbidden, and which are therefore the subjects of legitimate commerce."); Zywicki & Agarwal, *supra* note 27, at 616.

43. *Vance v. W.A. Vandercook Co.*, 170 U.S. 438, 442 (1898); *Rhodes v. Iowa*, 170 U.S. 412, 421 (1898).

liquors of their interstate character” in specified instances.<sup>44</sup> According to the Court, the purpose of the Webb–Kenyon Act was to “prevent the immunity characteristic of interstate commerce from being used to permit the receipt of liquor through such commerce in States contrary to their laws . . . .”<sup>45</sup>

Thus, immediately prior to Prohibition, the U.S. regulatory landscape for alcohol gave states the authority to regulate “purely local affairs,” which typically involved alcohol consumption and manufacturing.<sup>46</sup> In turn, the federal government had exclusive authority over interstate-commerce issues and—per the Wilson and Webb–Kenyon Acts—“helped the states enforce their police powers by subjecting alcohol shipped in interstate commerce to the same rules as alcohol produced and sold locally—no better and no worse.”<sup>47</sup>

The ratification of the Eighteenth Amendment, which instituted national Prohibition, temporarily muted litigation over state alcohol regulations.<sup>48</sup> Fourteen years later, the ratification of the Twenty-first Amendment reignited the century-old debate regarding the states’ regulatory authority over alcohol.<sup>49</sup>

## 2. Twenty-First Amendment Jurisprudence

National Prohibition ended in 1933 as Section 1 of the Twenty-first Amendment repealed the Eighteenth Amendment.<sup>50</sup> However, it was Section 2 of the Twenty-first Amendment—and its interaction with the Commerce Clause—that would stand at the heart of subsequent cases

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44. Webb–Kenyon Act, ch. 90, 37 Stat. 699 (1913) (codified as amended at 27 U.S.C. § 122 (2000)). The Webb–Kenyon Act provided as follows:

That the shipment or transportation . . . of any spirituous, vinous, malted, fermented, or other intoxicating liquor of any kind, from one State . . . into any other State . . . which said [intoxicating liquor] is intended . . . 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.

*Id.*

45. *James Clark Distilling Co. v. W. Md. Ry. Co.*, 242 U.S. 311, 324 (1917). The Webb–Kenyon Act was not without controversy—President Taft vetoed the Act as an unconstitutional delegation of Congress’s powers to regulate interstate commerce, but Congress overrode the veto. Sidney J. Spaeth, Comment, *The Twenty-First Amendment and State Control Over Intoxicating Liquor: Accommodating the Federal Interest*, 79 CAL. L. REV. 161, 173–74 (1991). Both the Wilson Act and the Webb–Kenyon Act remain valid laws today.

46. Zywicki & Agarwal, *supra* note 27, at 620.

47. *Id.*

48. U.S. CONST. amend. XVIII, § 1, *repealed by* U.S. CONST. amend. XXI (“[T]he manufacture, sale, or transportation of intoxicating liquors within, the importation thereof into, or the exportation thereof from the United States . . . is hereby prohibited.”).

49. *Id.* amend. XXI.

50. *Id.* amend. XXI, § 1.

challenging the constitutionality of state alcohol regulations.<sup>51</sup> Section 2 prohibits 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 . . . .”<sup>52</sup>

In its immediate post-Prohibition cases, the Supreme Court interpreted Section 2 as granting states broad power to regulate alcohol within their borders.<sup>53</sup> The Court upheld facially discriminatory alcohol regulations under the rationale that Section 2 allowed states to regulate alcohol without being bound by normal Commerce Clause restrictions.<sup>54</sup> Nevertheless, this broad interpretation was short-lived. In a pair of 1964 decisions, the Court posited that the Commerce Clause could limit a state’s regulatory authority over interstate alcohol commerce.<sup>55</sup> The Court rejected as “an absurd oversimplification” the idea that the Twenty-first Amendment “somehow operated to ‘repeal’ the Commerce Clause” with respect to alcohol regulation.<sup>56</sup>

Two decades later, *Bacchus Imports, Ltd. v. Dias* furnished the Court’s first significant analysis of the interplay between the dormant Commerce Clause and the Twenty-first Amendment.<sup>57</sup> The Court observed that the “central purpose” of the Twenty-first Amendment “was not to empower

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51. *Id.* amend. XXI, § 2. Courts have noted the conflicting interpretations of Section 2. *See, e.g., Bacchus Imps., Ltd. v. Dias*, 468 U.S. 263, 274 (1984) (“No clear consensus concerning the meaning of the provision is apparent.”); *Cal. Retail Liquor Dealers Ass’n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 107 n.10 (1980) (“The sketchy records of the state conventions reflect no consensus on the thrust of § 2 . . . .”). For an historical analysis of Section 2, see generally Aaron Nielson, Recent Development, *No More ‘Cherry-Picking’: The Real History of the 21st Amendment’s § 2*, 28 HARV. J.L. & PUB. POL’Y 281 (2004) (critiquing contemporary judicial interpretations of the Twenty-first Amendment’s history).

52. U.S. CONST. amend. XXI, § 2.

53. *State Bd. of Equalization of Cal. v. Young’s Mkt. Co.*, 299 U.S. 59, 62 (1936) (upholding a California license fee on beer imports while noting that “[p]rior to the Twenty-First Amendment it would have obviously been unconstitutional” because “the fee would be a direct burden on interstate commerce”).

54. *Indianapolis Brewing Co. v. Liquor Control Comm’n*, 305 U.S. 391, 394 (1939) (reiterating that “the right of a state to prohibit or regulate the importation of intoxicating liquor is not limited by the Commerce Clause”).

55. *Hostetter v. Idlewild Bon Voyage Liquor Corp.*, 377 U.S. 324, 332 (1964) (“Both the Twenty-first Amendment and the Commerce Clause are parts of the same Constitution. . . . [E]ach must be considered in the light of the other . . . .”); *Dep’t of Revenue v. James B. Beam Distilling Co.*, 377 U.S. 341, 344 (1964) (striking down a Kentucky tax on imported whiskey because the Twenty-first Amendment does not “operat[e] to permit what the Export-Import Clause precisely and explicitly forbids”).

56. *Hostetter*, 377 U.S. at 331–32.

57. *Bacchus Imps., Ltd. v. Dias*, 468 U.S. 263, 273 (1984) (applying the dormant Commerce Clause to invalidate a Hawaii liquor tax that exempted certain locally produced beverages).

States to favor local liquor industries by erecting barriers to competition.”<sup>58</sup> Thus, if a state law facially discriminated against interstate commerce, the question became “whether the principles underlying the Twenty-first Amendment are sufficiently implicated” by the discriminatory state law “to outweigh the Commerce Clause principles that would otherwise be offended.”<sup>59</sup> Subsequent cases came to refer to this balancing test as the “core concerns” test<sup>60</sup> and to identify the Twenty-first Amendment’s core concerns as promoting temperance, collecting taxes, and ensuring an orderly market.<sup>61</sup>

Nevertheless, the exact contours of the relationship between the Twenty-first Amendment and the dormant Commerce Clause as applied to state alcohol regulation remained undefined. As challenges to state direct-shipment laws worked through the courts, a circuit split soon emerged on the issue of whether states could discriminate against direct shipments from out-of-state wineries to in-state consumers.<sup>62</sup> The Supreme Court granted certiorari to hear two such cases, consolidating separate challenges to

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58. *Id.* at 276 (“State laws that constitute mere economic protectionism are therefore not entitled to the same deference as laws enacted to combat the perceived evils of an unrestricted traffic in liquor.”).

59. *Id.* at 275. The Court invalidated Hawaii’s law because it violated “a central tenant of the Commerce Clause” and was not supported by any “clear concern” of the Twenty-first Amendment. *Id.* at 276.

60. See Gregory E. Durkin, Note, *What Does Granholm v. Heald Mean for the Future of the Twenty-First Amendment, the Three-Tier System, and Efficient Alcohol Distribution?*, 63 WASH. & LEE L. REV. 1095, 1104 & n.42 (2006) (noting cases that had applied the “core concerns” balancing test pre-*Granholm*).

61. *North Dakota v. United States*, 495 U.S. 423, 432 (1990).

62. See *Swedenburg v. Kelly*, 358 F.3d 223, 237 (2d Cir. 2004) (upholding New York’s restrictions on direct shipment of out-of-state wine to in-state consumers as within the State’s Twenty-first Amendment powers); *Beskind v. Easley*, 325 F.3d 506, 519–20 (4th Cir. 2003) (striking down North Carolina laws that allowed in-state wine manufacturers to ship directly to consumers and required out-of-state manufacturers to use the three-tiered distribution system as violative of the Commerce Clause and not saved by Twenty-first Amendment); *Dickerson v. Bailey*, 336 F.3d 388, 410 (5th Cir. 2003) (holding that a Texas law that prohibited out-of-state wineries from shipping directly to consumers violated the Commerce Clause and was not saved by Twenty-first Amendment); *Heald v. Engler*, 342 F.3d 517, 526 (6th Cir. 2003) (holding that Michigan laws preventing out-of-state wineries from shipping directly to consumers violated the dormant Commerce Clause); *Bainbridge v. Turner*, 311 F.3d 1104, 1106 (11th Cir. 2002) (noting that Florida’s prohibition against out-of-state wineries shipping directly to consumers could be upheld against a dormant Commerce Clause challenge if Florida could prove that the statute was closely related to a core concern of the Twenty-first Amendment); *Bridenbaugh v. Freeman-Wilson*, 227 F.3d 848, 854 (7th Cir. 2000) (upholding an Indiana statute that prohibited direct shipments of alcoholic beverages from out-of-state producers to Indiana consumers as constitutional under the Twenty-first Amendment); see also Aaron Nielson, Recent Development, *Good History, Good Law (and by Coincidence Good Policy Too): Granholm v. Heald*, 125 S. Ct. 1885 (2005), 29 HARV. J.L. & PUB. POL’Y 743, 743 n.3 (2006) (detailing the state-law challenges and circuit split prior to *Granholm*).

Michigan and New York wine direct-shipment regulations in the landmark case of *Granholm v. Heald*.<sup>63</sup>

#### D. GRANHOLM V. HEALD

The Supreme Court's 2005 decision in *Granholm v. Heald* provided the Court's most significant analysis to date regarding the relationship between the dormant Commerce Clause and state authority to regulate alcohol under the Twenty-first Amendment.<sup>64</sup> In *Granholm*, out-of-state wineries and in-state wine consumers challenged the constitutionality of Michigan's and New York's laws governing the direct shipment of wine.<sup>65</sup> Michigan banned out-of-state wineries from shipping to Michigan consumers, but allowed in-state wineries to ship to consumers if the in-state wineries had a license.<sup>66</sup> New York allowed out-of-state wineries to ship to New York consumers only if the out-of-state wineries maintained a distribution operation within the state.<sup>67</sup> In a 5–4 decision, the Court held that both states' laws "discriminate against interstate commerce in violation of the Commerce Clause . . . and that the discrimination is neither authorized nor permitted by the Twenty-first Amendment."<sup>68</sup>

#### 1. The Court's Analysis

As a threshold matter, the Court determined that Michigan's and New York's direct-shipment laws discriminated against interstate commerce.<sup>69</sup> Nevertheless, the states contended that Section 2 of the Twenty-first

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63. *Granholm v. Heald*, 544 U.S. 460, 465–66 (2005). The Court granted certiorari on the following question: "Does a State's regulatory scheme that permits in-state wineries directly to ship alcohol to consumers but restricts the ability of out-of-state wineries to do so violate the dormant Commerce Clause in light of § 2 of the Twenty-first Amendment?" *Id.* at 471.

64. *Id.* Many commentators have provided useful critiques of the decision. See generally William Glunz, Comment, *Granholm v. Heald: The Twenty-First Amendment Takes Another Hit—Where Do States Go From Here?*, 40 J. MARSHALL L. REV. 651 (2007) (suggesting courses of action for state regulatory systems); Robert L. Jones III, Note, *Direct Shipment of Alcohol—Well-Aged and Finally Uncorked: The Supreme Court Decides Whether the Twenty-First Amendment Grants States the Power to Avoid the Dormant Commerce Clause*, 28 U. ARK. LITTLE ROCK L. REV. 483 (2006) (analyzing *Granholm* with a focus on Arkansas's direct-shipment laws); Tania K. M. Lex, Case Note, *Of Wine and War: The Fall of State Twenty-First Amendment Power at the Hands of the Dormant Commerce Clause—Granholm v. Heald*, 32 WM. MITCHELL L. REV. 1145 (2006) (focusing on the decision's effects on Twenty-First Amendment jurisprudence).

65. *Granholm*, 544 U.S. at 466.

66. *Id.* at 473–74 (noting that all out-of-state wine had to pass through an in-state wholesaler and retailer in order to reach Michigan customers and that "these two extra layers of overhead increase the cost of out-of-state wines to Michigan consumers" so as to "effectively bar small wineries from the Michigan market").

67. *Id.* at 474 (observing that New York's requirement that out-of-state wineries open a branch office and warehouse in New York was cost-prohibitive for most wineries and an "indirect way of subjecting out-of-state wineries, but not local ones, to the three-tier system").

68. *Id.* at 466.

69. *Id.* at 476.

Amendment saved the laws from invalidity under the Commerce Clause.<sup>70</sup> In analyzing this argument, the Court relied on three principles that it said guided the analysis of Section 2 cases: (1) the Twenty-first Amendment does not “save” state laws that violate other provisions of the Constitution; (2) Section 2 does not abrogate Congress’s powers to regulate alcohol in interstate commerce under the Commerce Clause; and (3) the nondiscrimination principle in the Commerce Clause limits the ability of states to regulate alcohol.<sup>71</sup> The Court’s response to the Section 2 argument was unequivocal: “Section 2 does not allow States to regulate the direct shipment of wine on terms that discriminate in favor of in-state producers.”<sup>72</sup>

After determining that Section 2 did not authorize the discriminatory laws, the Court queried whether either state’s laws advanced a “legitimate local purpose that cannot be served by reasonable nondiscriminatory alternatives.”<sup>73</sup> Michigan and New York put forth two primary justifications for restricting shipments from out-of-state wineries: preventing minors from obtaining alcohol and facilitating state tax collection.<sup>74</sup> Neither purpose was sufficient for the Court. First, the states had little evidence that minors would take advantage of direct shipments by purchasing wine online.<sup>75</sup> Even assuming that direct shipment would increase the risk of underage drinking, the states could take “less restrictive steps to minimize the risk,” such as requiring an adult signature upon delivery.<sup>76</sup> The tax-collection justification was also insufficient because state licensing regimes and existing federal remedies adequately protected the states from lost tax revenue.<sup>77</sup>

Rejecting the proffered justifications of the two states, the Court invalidated both direct-shipment laws as unconstitutional violations of the Commerce Clause. Using language that has caused many states to reevaluate their wine-distribution laws, the Court summarized its ruling: “If a State chooses to allow direct shipment of wine, it must do so on evenhanded

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70. *Granholm*, 544 U.S. at 486–87.

71. *Id.*

72. *Id.* at 476. The Twenty-first Amendment protects state laws that treat out-of-state alcohol on the same terms as in-state equivalents; however, Michigan’s and New York’s direct-shipment regulations involved “straightforward attempts to discriminate in favor of local producers.” *Id.* at 489.

73. *Id.* at 489 (quoting *New Energy Co. of Ind. v. Limbach*, 486 U.S. 269, 278 (1988)). The Court emphasized that it would uphold state regulations that discriminate against interstate commerce “only after finding, based on concrete record evidence, that a State’s nondiscriminatory alternatives will prove unworkable.” *Id.* at 493.

74. *Id.* at 489–92. The Court also rejected the justifications of facilitating orderly markets, protecting public health and safety, and ensuring regulatory accountability. *Id.*

75. *Granholm*, 544 U.S. at 490 (noting that minors would be just as likely to purchase wine from in-state wineries as out-of-state wineries).

76. *Id.* at 491–92. The Court referred to the Model Direct Shipping Bill, developed by the National Conference of State Legislatures, which includes this requirement. *Id.*

77. *Id.*

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.”<sup>78</sup>

## 2. The *Granholtm* Aftermath

*Granholtm*'s reverberations have extended beyond the invalidation of the Michigan and New York laws. Since *Granholtm* only addressed producer-to-consumer shipments, it is unclear whether the decision requires states to place retailers on a similar equal regulatory footing. As such, litigants have challenged state laws that mandate differential treatment for out-of-state retailers in direct-to-consumer shipments<sup>79</sup> and interstate winery-to-retailer sales.<sup>80</sup> Other litigants have challenged specific elements of state direct-shipment laws as placing impermissible burdens on interstate commerce. In particular, these cases address on-site purchase requirements,<sup>81</sup> personal import volume restrictions,<sup>82</sup> and production volume caps that determine which wineries may ship directly to consumers.<sup>83</sup>

On a broader level, *Granholtm*'s analytical framework provides the current lens through which states must reanalyze their wine-distribution laws.<sup>84</sup> Notably, the *Granholtm* Court did not analyze whether Michigan's and New York's justifications for the discriminatory laws were “core concerns” under the Twenty-first Amendment.<sup>85</sup> As courts and commentators have noted, this likely signals that the same “exacting standard” under the

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78. *Id.* at 493.

79. Compare *Arnold's Wines, Inc. v. Boyle*, 515 F. Supp. 2d 401, 413–14 (S.D.N.Y. 2007) (upholding New York's licensing scheme that allowed in-state retailers to ship directly to New York consumers, but not allowing out-of-state retailers the same licensing privilege), with *Siesta Vill. Mkt., LLC v. Perry*, 530 F. Supp. 2d 848, 868 (N.D. Tex. 2008) (striking down similar Texas laws as violations of the Commerce Clause). For a critique of New York's differential treatment of in-state and out-of-state retailers, see Andre Nance, Note, *Don't Put a Cork in Granholtm v. Heald: New York's Ban on Interstate Direct Shipments of Wine Is Unconstitutional*, 16 J.L. & POL'Y 925, 936 (2008).

80. See Durkin, *supra* note 60, at 1110–16 (analyzing whether direct shipment to retailers differs from direct shipment to consumers).

81. See *Baude v. Heath*, 538 F.3d 608, 611 (7th Cir. 2008) (upholding the so-called “face-to-face” clause in Indiana's alcohol regulations that allows consumers to have wine directly shipped to them only if they personally visit the in-state or out-of-state winery).

82. See *Brooks v. Vassar*, 462 F.3d 341, 352–54 (4th Cir. 2006) (upholding Virginia's personal importation restriction against plaintiffs' argument that the laws discriminated against out-of-state retailers); Ethan Davis, *Uncorking a Seventy-Four-Year-Old Bottle: A Toast to the Free Flow of Liquor Across State Borders*, 117 YALE L.J. POCKET PART 133, 137 (2007) (arguing that personal import limits are unconstitutional).

83. Mike Figge, Case Note, *Granholtm v. Heald*, 544 U.S. 460 (2005), 8 WYO. L. REV. 231, 240 & n.79 (2008) (noting challenges to state laws with production capacity caps).

84. See *supra* Part II.D.1 (detailing the Court's analysis of the challenged statutes).

85. See *supra* notes 59–61 and accompanying text (describing the “core concerns” balancing test).

Commerce Clause that applies to discriminatory state regulations in other contexts applies to state alcohol regulations.<sup>86</sup>

In any event, it is clear that *Granholm* signals the Court's willingness to strike down laws that discriminate against out-of-state wine manufacturers as impermissible burdens on interstate commerce. With this background in mind, the focus of the Note shifts to the analysis of Iowa's particular statutes.

### III. IOWA'S WINE-DISTRIBUTION LAWS

The *Granholm* decision makes two Iowa wine statutes potential litigation targets: Iowa's reciprocal-shipment statute, which governs the ability of out-of-state wine manufacturers to ship their wine directly to Iowa consumers, and Iowa's native-wine statute, which grants certain privileges to Iowa wine manufacturers that are not available to non-native-wine manufacturers.<sup>87</sup> A court would likely find that the entire reciprocal-shipment statute, as well as certain provisions of the native-wine statute, place unconstitutional burdens on interstate commerce and cannot be justified by the state's authority to regulate alcohol under the Twenty-first Amendment. This Part begins with an overview of Iowa wine regulation before analyzing the two statutes.

#### A. OVERVIEW OF WINE REGULATION IN IOWA

Following the repeal of Prohibition, Iowa was one of the original "control" jurisdictions that asserted direct control over the wholesale and retail distribution of all alcoholic beverages, excluding beer.<sup>88</sup> The state privatized the wholesale and retail distribution of wine in the mid-1980s.<sup>89</sup> Presently, the Iowa Alcoholic Beverages Division ("ABD") regulates the sale and distribution of all alcoholic beverages within the state under the Iowa Alcoholic Beverage Control Act.<sup>90</sup>

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86. *Brooks*, 462 F.3d at 351 (interpreting the post-*Granholm* analytical framework for determining the validity of state alcohol regulations). That is, a different standard does not apply in the Twenty-first Amendment context for determining whether a state law's discriminatory effects are permissible. Jonathan M. Rotter & Joshua S. Stambaugh, *What's Left of the Twenty-First Amendment?*, 6 CARDOZO PUB. L. POL'Y & ETHICS J. 601, 613 (2008).

87. For a summary of the current status of native-wine regulation in Iowa, see Memorandum from John Lundquist, Assistant Attorney Gen., State of Iowa, to Lynn Walding, Iowa Alcoholic Beverages Div. Adm'r (Apr. 13, 2007) (on file with the Iowa Law Review).

88. Iowa Dep't of Alcoholic Beverages, ABD Historical Highlights, [http://www.iowaabd.com/about\\_office/historical\\_highlights/historical\\_highlights.jsp](http://www.iowaabd.com/about_office/historical_highlights/historical_highlights.jsp) (last visited Aug. 29, 2008) [hereinafter ABD Historical Highlights]. Iowa policymakers viewed direct control as furthering three objectives: first, the prevention of crime like that during the Prohibition era; second, the limitation of liquor consumption that would otherwise be greater in a profit-driven market; and third, the use of revenue for substance-abuse treatment and the promotion of moderation. STATE OF IOWA ALCOHOLIC BEVERAGES DIV., A STUDY OF IOWA'S LIQUOR WHOLESAL SYSTEM 8 (2002), available at [http://www.iowaabd.com/doc/warehouse\\_study.pdf](http://www.iowaabd.com/doc/warehouse_study.pdf).

89. ABD Historical Highlights, *supra* note 88.

90. IOWA CODE §§ 123.1, .4 (2007).

Iowa law prohibits any person from manufacturing, importing, or selling wine in Iowa unless that person obtains a wine permit, certificate, or liquor-control license from the ABD.<sup>91</sup> The ABD has statutory authority to issue four classes of wine permits: “A,” “B,” “B” native, and “C” native.<sup>92</sup> All persons who manufacture wine for resale in Iowa must obtain a class “A” wine permit; class “A” wine permittees may only sell wine at wholesale.<sup>93</sup> Class “A” permittees must pay a \$1.75 wine gallonage tax on each gallon of wine manufactured for sale and sold at wholesale, and for all wine imported for sale at wholesale and sold at wholesale.<sup>94</sup> Class “B” wine permittees may sell wine at retail for off-premises consumption and may purchase wine for resale only from class “A” wine permittees.<sup>95</sup> Class “B” native-wine permittees may sell native wine only at retail for off-premise consumption and may purchase wine for resale only from a native winery holding a class “A” wine permit.<sup>96</sup> Class “C” native-wine permittees may sell native wine only at retail for on- or off-premise consumption, and may purchase wine for resale only from a native winery holding a class “A” wine permit.<sup>97</sup> All manufacturers, vintners, bottlers, importers, and vendors of wine must obtain a vintner’s certificate of compliance in order to ship, sell, or have wine brought into Iowa for resale.<sup>98</sup>

*B. IOWA’S RECIPROCAL-SHIPMENT STATUTE*

Iowa regulates the direct shipment of wine to consumers under a reciprocity model.<sup>99</sup> While thirteen states used the reciprocity model when the Court decided *Granholm* in 2005, all but Iowa and New Mexico have abandoned their reciprocal-shipment statutes.<sup>100</sup> Not only does this shift make Iowa’s current model impractical, but *Granholm*’s mandate that states treat out-of-state and in-state wineries on equal terms casts considerable doubt on the constitutionality of a reciprocity system for wine direct shipment.

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91. *Id.* § 123.171.

92. *Id.* § 123.173(1). The Act classifies “B,” “B” native, and “C” native as retail wine permits. *Id.* § 123.3(30).

93. *Id.* §§ 123.173(2), .177. Class “A” permittees may only sell to persons holding a class “A” or “B” wine permit and to persons holding a retail liquor-control license. *Id.* § 123.177(1).

94. *Id.* § 123.183(1). The wine gallonage tax rate is not collected on wine sold between class “A” wine permittees. *Id.*

95. IOWA CODE §§ 123.173(2), .178 (2007).

96. *Id.* §§ 123.173, .178A.

97. *Id.* §§ 123.173, .178B.

98. *Id.* § 123.180.

99. *Id.* § 123.187.

100. See *supra* notes 21–24 and accompanying text (describing the use of the reciprocity system).

### 1. Statutory Interpretation

Under Iowa's reciprocal-shipment statute, out-of-state wineries that are licensed in states affording Iowa an "equal reciprocal shipping privilege" may ship a maximum of eighteen liters of wine per month to Iowans of legal drinking age for their personal consumption or use.<sup>101</sup> An "equal reciprocal shipping privilege" means allowing wineries located in [Iowa] to ship into another state, wine, not for resale, but for consumption or use by a person twenty-one years of age or older.<sup>102</sup> Iowa's class "A" and "B" wine permittees may ship a maximum of eighteen liters of wine per month to out-of-state consumers for personal consumption or use.<sup>103</sup> The reciprocal-shipment statute does not address the ability of in-state wineries to ship directly to Iowa consumers.

The statute is ambiguous, and the relevant administrative rules are silent, regarding exactly what constitutes an "equal reciprocal shipping privilege." As a result, it is unclear which states even qualify to ship wine directly to Iowa consumers. To illustrate this ambiguity, there are at least three approaches to defining the states that provide Iowa with an "equal reciprocal shipping privilege": (1) states that use an explicit reciprocity statute; (2) states that allow direct shipment to consumers without the imposition of sales, use, or wine gallonage taxes; and (3) any states that generally allow direct shipping to consumers.

The first interpretation would require that other states have an explicit reciprocal-shipment statute. While this interpretation may appear to flow most naturally from the basic idea of reciprocity, it is problematic because it effectively nullifies the statute's use of the term "equal." That is, simply because another state uses the phrase "reciprocal shipping" indicates little about the equities of that state's shipping privileges.

The second interpretation would define reciprocal states as states that allow direct shipment without the imposition of certain taxes, fees, or charges. The statute itself provides the basis for this interpretation: shipments made pursuant to Iowa's reciprocal-shipment privilege are not subject to sales tax, use tax, or wine gallonage tax.<sup>104</sup> Thus, an "equal reciprocal" privilege could require that similar provisions exist in another state. Even though this interpretation does open up shipping from states that do not have explicit reciprocity statutes, it would pose practical problems for the ABD and wineries in keeping up-to-date on the minutiae of other states' tax and fee requirements.

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101. IOWA CODE § 123.187(2) (2007).

102. *Id.* § 123.187(1). Wine brought into Iowa under the privilege is not subject to sales tax, use tax, or the wine gallonage tax. *Id.* § 123.187(2).

103. *Id.* § 123.187(3).

104. *Id.* § 123.187(2).

The third interpretation would encompass any state that allows the direct shipment of wine to consumers. This approach to Iowa's statute presents the broadest access to Iowa consumers by only excluding shipments from states that ban direct shipment outright.<sup>105</sup> However, just like under the first interpretation, it is unclear whether other state laws would satisfy the "equal" language in the Iowa statute. If the Iowa legislature intended that this approach result under the statute, this Note proposes that it is best accomplished through the institution of a direct-shipment permit system, not by keeping the reciprocal-shipment statute and merely clarifying its terms through administrative rules.<sup>106</sup> As these interpretations indicate, the ambiguity in the reciprocal-shipping statute makes it difficult to determine whether an out-of-state winery may ship wine directly to Iowa consumers. Further, since a system of reciprocity is only as effective as its constituents, the decisive move away from the reciprocity model on the national level could very well leave Iowa as the only state holding on to a statute with little practical effect.

## 2. Constitutional Analysis

The constitutionality of the reciprocity model for wine shipment was not directly before the Court in *Granholm*.<sup>107</sup> Nevertheless, the Court briefly addressed reciprocity systems in less-than-favorable language. Emphasizing that "States do not need, and may not attempt, to negotiate with other States regarding their mutual economic interests," the *Granholm* Court noted that "[t]he perceived necessity for reciprocal sale privileges risks generating the trade rivalries and animosities, the alliances and exclusivity, that the Constitution and, in particular, the Commerce Clause were designed to avoid."<sup>108</sup> In the context of wine direct shipments, reciprocity arrangements are problematic because they require out-of-state entities that are not in a qualifying reciprocal state to use the state's three-tier system. At the same time, out-of-state wineries in qualifying reciprocal states do not have to go through the three-tier system because they can ship directly to consumers. In *Granholm*, the Court struck down the laws at issue because they mandated that out-of-state wine, but not in-state wine, travel through the three-tier system.<sup>109</sup>

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105. See *supra* note 15 (listing states that ban direct shipments to their consumers).

106. See *infra* Part IV (recommending that the Iowa legislature adopt a direct-shipment permit system).

107. See *Granholm v. Heald*, 544 U.S. 460, 473 (2005) ("State laws that *protect* local wineries have led to the enactment of statutes under which some States condition the right of out-of-state wineries to make direct wine sales to in-state consumers on a reciprocal right in the shipping State." (emphasis added)).

108. *Id.* at 472-73.

109. *Id.* at 474.

In cases outside the alcohol context, the Court has found that reciprocity arrangements are facially discriminatory and thus unconstitutional where they allow out-of-state entities access to in-state markets only if the other state provides similar benefits.<sup>110</sup> Since *Granholm* seems to foreclose the idea that alcohol regulations receive special treatment under the Commerce Clause,<sup>111</sup> a court could easily conclude that reciprocity arrangements for direct shipment are invalid in the same way. Even if reciprocity arrangements as a whole are not unconstitutional after *Granholm*, the intersection of Iowa's reciprocal-shipment statute with the direct-shipment privileges in the native-wine statute leads to the conclusion that Iowa does not regulate the direct shipment of wine to consumers on evenhanded terms.

### C. IOWA'S NATIVE-WINE STATUTE

Iowa law has included special provisions for native-wine manufacturers since the State's first post-Prohibition alcohol statutes.<sup>112</sup> Iowa's current native-wine statute has clearly aided the expansion of Iowa's wine industry since its enactment in 2003.<sup>113</sup> However, *Granholm* requires a reevaluation of the statute—with regard not only to direct shipment, but also to the other privileges that increase native-wine manufacturers' access to Iowa consumers in ways unavailable to non-native manufacturers.

#### 1. Iowa's Wine Industry

The recent growth in Iowa's wine industry is more appropriately termed a resurgence, as Iowa was one of the nation's top grape-growing states at the beginning of the twentieth century. European homesteaders established Iowa's earliest vineyards on their farms, growing grapes and making juice, wine, and jams for their families.<sup>114</sup> By 1899, Iowa ranked eleventh in national grape production; by 1919, the state ranked sixth.<sup>115</sup> Iowa's grape

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110. CHEMERINSKY, *supra* note 30, at 432 & n.56 (citing *Great Atl. & Pac. Tea Co. v. Cottrell*, 424 U.S. 366 (1976), where the Court unanimously invalidated a Mississippi law that only allowed the shipment of out-of-state milk to in-state consumers if the other state accepted Mississippi's milk on reciprocal terms).

111. See *supra* Part II.D.1 (describing the *Granholm* Court's analytical framework).

112. Act of Mar. 6, 1934, ch. 24, § 49, 1934 Iowa Acts 54. Although the State had exclusive wholesale and retail control over wine distribution under the Iowa Liquor Control Act of 1934, native-wine manufacturers were authorized to sell and deliver their native wine to the public for off-premises consumption. *Id.*

113. See Iowa Alcoholic Beverages Comm'n, Commission Meeting Minutes 3 (Feb. 23, 2007), [http://www.iowaabd.com/about\\_office/commission\\_minutes/02232007.pdf](http://www.iowaabd.com/about_office/commission_minutes/02232007.pdf) (recognizing provisions in the native-wine statute that have boosted Iowa's wine industry).

114. RICH PIROG, GRAPE EXPECTATIONS: A FOOD SYSTEM PERSPECTIVE ON REDEVELOPING THE IOWA GRAPE INDUSTRY 4 (2000), available at <http://www.leopold.iastate.edu/pubs/staff/grapes/Grape.pdf>.

115. *Id.* at 1.

yields peaked in 1929 at 15.8 million pounds before declining severely in subsequent decades.<sup>116</sup>

Initiatives to reestablish Iowa's grape industry began in the 1980s, fueled by the growing Iowa wine industry and farmers' need to diversify in order to remain profitable.<sup>117</sup> A recent survey showed that Iowa wineries were optimistic about the future of Iowa's grape and wine industries: the wineries projected that their wine production in 2009 would be six times greater than that in 2002, and they planned to use Iowa-grown grapes in at least two-thirds of their production by 2009, compared to one-third in 2002.<sup>118</sup> Analysts expect the Iowa grape and wine industry to remain "very viable" and grow at a "strong pace."<sup>119</sup>

## 2. Statutory Interpretation

The provisions of Iowa's native-wine statute apply only to "manufacturers of native wines."<sup>120</sup> The native-wine statute defines "manufacturer" as "only those persons who process in Iowa the fruit, vegetables, dandelions, clover, honey, or any combination of these ingredients, by *fermentation* into wines."<sup>121</sup> It is important to note that "native wine" is also defined under the Iowa Alcoholic Beverages Control Act, meaning "wine manufactured in this state."<sup>122</sup> This definition does not explain the term "manufactured" and must be read in conjunction with the definition of "manufacturer" in the actual native-wine statute to determine who receives the statute's benefits.<sup>123</sup> Accordingly, fermentation occurring in Iowa is the key element for qualification as a native-wine manufacturer.<sup>124</sup>

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116. *Id.* at 5–6. By 1966, Iowa grape production was only 480,000 pounds, a decline primarily attributable to corn-herbicide drift that damaged vineyards. *Id.*

117. *Id.* at 6, 15; Susan Saulny, *Iowa Finds Itself Deep in Heart of Wine Country*, N.Y. TIMES, Nov. 19, 2006, at 1 (profiling an Iowa farmer who netted \$40 per acre with corn and soybeans, compared to upwards of \$1500 per acre with grapes).

118. Press Release, U.S. Dep't of Agric., 2006 Winery Survey, *available at* [http://www.iowaagriculture.gov/Horticulture\\_and\\_FarmersMarkets/pdfs/2006WinerySurvey.pdf](http://www.iowaagriculture.gov/Horticulture_and_FarmersMarkets/pdfs/2006WinerySurvey.pdf). Iowa's wine production increased from 51,500 gallons in 2002 to more than 246,000 gallons in 2006, with an annualized market value of more than \$12.3 million. OVRM, *supra* note 1, at 14.

119. OVRM, *supra* note 1, at 14. The average monthly wine sales for all wines produced in Iowa measured in at 9800 gallons in December 2006, up from 5000 gallons in 2004. *Id.*

120. IOWA CODE § 123.56 (2007).

121. *Id.* § 123.56(6) (emphasis added); IOWA ADMIN. CODE r. 185-5.1(1) (2008) ("A manufacturer of native wine is a person in Iowa who processes grapes, cherries, other fruits or other fruit juices, vegetables, vegetable juices, dandelions, clover, honey, or any combination of these ingredients, by fermentation into wine.").

122. IOWA CODE § 123.3(22A) (2007).

123. *See id.* § 123.56(6) (defining "manufacturer"). The ABD's administrative rules also place residency requirements on native-wine manufacturers. IOWA ADMIN. CODE r. 185-5.1(2) (2008).

124. "Native winery" is not a defined term under Iowa law, and what should constitute a native Iowa winery is still open for debate. The possibilities range, for example, from the Iowa winery that makes wine exclusively from grapes that the winery grows, to the winery that uses a

Native-wine manufacturers, like non-native-wine manufacturers, must obtain a class “A” wine permit to manufacture and sell their wine in Iowa.<sup>125</sup> Without obtaining any additional permits, native-wine manufacturers automatically receive the benefits of the native-wine statute. The benefits include the following:

- Native-wine manufacturers may “ship wine in closed containers to individual purchasers inside and outside this state.”<sup>126</sup> There are no volume limitations on the amount of wine that native-wine manufacturers may ship. In contrast, non-native manufacturers may only ship directly to Iowa residents per the ambiguous terms of the reciprocal-shipment statute, which includes an eighteen-liter-per-month shipping limit for each customer.<sup>127</sup>
- Native-wine manufacturers with class “A” wine permits may sell their own native wine at retail for off-premises consumption.<sup>128</sup> Non-native-wine manufacturers with class “A” wine permits may only sell their wine at wholesale.<sup>129</sup>
- Native-wine manufacturers do not pay the \$1.75 wine gallonage tax on native-wine retail sales made at the manufacturer’s winery or retail establishments.<sup>130</sup> Non-native-wine manufacturers with class “A” wine permits pay the wine gallonage tax on all wine manufactured for sale and sold at wholesale in Iowa.<sup>131</sup>
- Native-wine manufacturers can procure the required class “A” wine permit for \$25.<sup>132</sup> The normal fee for non-native-wine manufacturers is \$750.<sup>133</sup>

These privileges effectively exempt native-wine manufacturers from operating within Iowa’s three-tier alcohol distribution system: despite being manufacturers, they are allowed to make retail sales, ship wine directly to

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percentage of Iowa grapes blended with out-of-state juice. Iowa Alcoholic Beverages Comm’n, *supra* note 113, at 6–7.

125. IOWA CODE § 123.56(1) (2007) (“[M]anufacturers of native wines . . . holding a class ‘A’ wine permit as required by this chapter, may sell, keep, or offer for sale and deliver the wine.”). The ABD’s administrative rules misleadingly refer to a “Class ‘A’ native wine permit.” IOWA ADMIN. CODE r. 185-5.1(3)(a) (2008). The Iowa Code only authorizes a general Class “A” permit with no distinction between native and non-native manufacturers. IOWA CODE § 123.173(1) (2007).

126. IOWA CODE § 123.56(3) (2007).

127. *See supra* Part III.B (analyzing Iowa’s reciprocal-shipment statute).

128. IOWA CODE § 123.56(1) (2007).

129. *See supra* Part III.A (describing the privileges under Iowa’s wine permits).

130. IOWA ADMIN. CODE r. 185-5.1(11) (2008). Native-wine manufacturers must pay the tax on native wine sold at wholesale to retail liquor licensees, retail beer permittees, retail wine permittees, and the ABD. *Id.*

131. IOWA CODE § 123.183(1) (2007). Iowa does not collect the wine gallonage tax on sales between class “A” wine permittees. *Id.*

132. *Id.* § 123.56(4).

133. *Id.* § 123.179(1).

Iowa consumers, and avoid certain taxes.<sup>134</sup> Since these privileges are not available to non-native-wine manufacturers, Iowa's native-wine statute is a prime target for post-*Granholm* litigation because it does not regulate out-of-state wine on evenhanded terms with in-state wine.

### 3. Constitutional Analysis

The most significant problem with Iowa's native-wine statute is that it gives native-wine manufacturers direct-shipment access to Iowa consumers on terms that are unavailable to non-native-wine manufacturers. As the Court stated in *Granholm*, Section 2 of the Twenty-first Amendment "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>135</sup> No other provision of Iowa law provides out-of-state wineries with comparable express direct-shipment access to Iowa consumers without volume limits. Non-native wine manufacturers who hold the exact same class "A" wine permit as the native-wine manufacturer do not have that explicit direct-shipment access to Iowa consumers.<sup>136</sup>

As explored above, Iowa's reciprocal-shipment statute governs the ability of non-native manufacturers to ship wine directly to Iowa consumers.<sup>137</sup> The reciprocal-shipping statute only allows direct shipping if the manufacturers are licensed in a state that provides Iowa with an ambiguous "equal reciprocal shipping privilege."<sup>138</sup> Even if a non-native manufacturer qualifies under this statute, it is limited to shipping no more than eighteen liters of wine per month to any resident.<sup>139</sup> Not only is the reciprocity model itself likely unconstitutional after *Granholm*, but a court could interpret the ambiguous provisions of Iowa's reciprocal-shipment statute as severely limiting the ability of out-of-state wineries to ship directly to in-state consumers.<sup>140</sup> On its face, Iowa's reciprocal-shipping statute seems to ban the direct shipment of wine from any non-reciprocal state. A court could plausibly interpret the statute as only allowing direct shipping from states with explicit reciprocity statutes—which would ban shipments from all states except New Mexico.<sup>141</sup>

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134. See *supra* Part II.A (describing the three-tier alcohol distribution system).

135. *Granholm v. Heald*, 544 U.S. 460, 493 (2005).

136. IOWA CODE § 123.173 (2007). Non-native manufacturers can obtain all possible wine permits under Iowa law and not have the explicit direct-shipment access to Iowa residents that native-wine manufacturers receive from simply being native-wine manufacturers.

137. See *supra* Part III.B.1 (exploring the various ways in which a court could interpret the statute's language).

138. IOWA CODE § 123.187 (2007).

139. *Id.* § 123.187(2).

140. See *supra* Part III.B.2 (discussing *Granholm* and how it briefly addressed the constitutionality of the reciprocity model).

141. See *supra* note 23 (reviewing the New Mexico statute that leveled the playing field for small wineries).

In addition to the direct-shipment access, other provisions of the native-wine statute are vulnerable to constitutional challenge. In particular, litigants could argue that the wine gallonage tax exemption and retail-sales authority given to native-wine manufacturers disproportionately burden interstate commerce. Non-native class “A” wine permittees can only sell wine at wholesale and must pay the wine gallonage tax on those sales. In contrast, native-wine manufacturers with class “A” permits can sell their wine at retail and do not have to pay the wine gallonage tax on these sales. Litigants could argue that this differential treatment discriminates against interstate commerce in that it allows in-state wineries access to Iowa consumers in ways that are unavailable to out-of-state wineries.

The justifications that Iowa would put forward in defense of these laws would likely be similar to Michigan’s and New York’s justifications in *Granholm*.<sup>142</sup> With regard to the direct-shipment issue, Iowa could argue that the native-wine statute is necessary to collect taxes, as the State could keep better track of native-wine manufacturers than non-native. However, a court would likely find that Iowa could achieve this purpose through less discriminatory means, such as a direct-shipment permit system. The State probably cannot use concerns about underage drinking to justify disparate treatment between native and non-native manufacturers; if this was a serious concern, the State would not authorize direct shipment by native-wine manufacturers.

*Granholm* held that these justifications are unlikely to persuade a court. It is thus likely that a court would find that Iowa’s reciprocal-shipment statute and the provisions of the native-wine statute analyzed above are unconstitutional and unjustifiable under the State’s authority to regulate alcohol under the Twenty-first Amendment.

#### IV. RECOMMENDATIONS FOR STATUTORY CHANGE

In light of the foregoing analysis, the Iowa legislature should change the current regulatory framework for wine distribution by eliminating Iowa’s reciprocal-shipment system and the direct-shipment privilege for native-wine manufacturers. In place of these provisions, the State should enact a direct-shipment permit system to allow the direct shipment of wine to Iowa consumers on terms that treat out-of-state and in-state wineries equally. Further, the legislature should reconsider the inclusion of the benefits granted to native-wine manufacturers under the native-wine statute. These changes would be a proactive step against lawsuits challenging the constitutionality of Iowa’s wine statutes in light of *Granholm* and a signal to the nation that Iowa is serious about keeping its laws on par with national shifts in wine regulation.

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142. See *supra* Part II.D.1 (outlining Michigan’s and New York’s arguments concerning tax collection and underage drinking).

A direct-shipment permit system would allow qualifying out-of-state and in-state wineries to ship wine directly to Iowa consumers by obtaining the requisite permit from the ABD. The permit system would not only treat in-state and out-of-state wineries on equal regulatory terms in compliance with *Granholm*, but it would also allow the ABD to have more regulatory oversight of the out-of-state entities that ship wine into the state—an enforcement mechanism that is currently lacking under the reciprocal-shipment statute.

In considering the shift to the direct-shipment permit system, the legislature should avoid a hasty outright prohibition of all direct shipment. Some states have responded to the *Granholm* decision in this way.<sup>143</sup> Prohibiting all direct shipment involves less administrative effort than instituting a new permit system. However, such a move would come at the expense of both Iowa native-wine manufacturers and Iowa wine consumers. Native-wine manufacturers would lose a method for generating sales and interest in Iowa consumers to the detriment of the state's wine industry. Without direct shipment, Iowa residents would find it more difficult to obtain out-of-state wines that are unavailable at Iowa retailers.<sup>144</sup> Continuing to allow direct shipments to Iowa consumers through a direct-shipment permit system is a sounder policy approach to promote Iowa's wine industry, to enhance consumer choice, and to protect the state against litigation.

The Model Direct Wine Shipment Bill, which the Court cited in *Granholm*, presents an appropriate template from which the Iowa legislature can craft the state's new direct-shipment permit system.<sup>145</sup> The Model Bill is comprehensive enough that the State could adopt it without substantive changes. Applying the Model Bill to Iowa, the main provision in Iowa's direct-shipment permit statute could provide as follows:

[A]ny person currently licensed in this or any other state as a wine producer, supplier, importer, wholesaler, distributor or retailer who obtains a Wine Direct Shipper License . . . may ship up to twenty four (24) 9-liter cases of wine annually directly to a resident of Iowa who is at least 21 years of age for such resident's personal use and not for resale.<sup>146</sup>

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143. See Matthew Dickson, Note, *All or Nothing: State Reaction in the Wake of Granholm v. Heald*, 28 WHITTIER L. REV. 491, 507 (2006) (tracking the changes in state regulations since 2005).

144. See generally FTC WINE REPORT, *supra* note 8 (discussing anti-competitive barriers in wine e-commerce).

145. *Granholm v. Heald*, 544 U.S. 460, 491 (2005); Model Direct Shipment Bill [hereinafter Model Bill], available at <http://www.wineinstitute.org/files/ModelDirectShipmentBill.pdf>. The National Conference of State Legislatures' Task Force on the Wine Industry adopted the Model Bill in November 1997. See Free the Grapes, Model Direct Shipping Bill, <http://www.freethethegrapes.org/model.html> (last visited Jan. 4, 2009).

146. Model Bill, *supra* note 145.

The direct-shipment statute should delineate the process that direct-shipment permittees must follow in order to ship directly wine to Iowans. The permittee would have to file an application with the ABD, pay a registration fee, provide a copy of its current alcoholic-beverage-license (either issued in Iowa or in another state), and obtain a Wine Direct Shipper Permit from the ABD.<sup>147</sup> The new direct-shipment statute should also explain the various restrictions placed on permittees. These restrictions could include the following: volume limits on shipment;<sup>148</sup> prominent notices declaring the presence of alcohol inside shipping containers;<sup>149</sup> procedures for reporting sales and shipment quantities; and procedures for sales- and excise-tax payment.<sup>150</sup>

The move to a direct-shipment permit system would not be without resistance. Alcohol wholesalers have a financial stake in the continuing viability of the three-tier system (i.e., not allowing consumers to purchase directly from manufacturers).<sup>151</sup> The wholesaling lobby would likely argue that direct shipment promotes underage drinking because minors could obtain alcohol over the Internet.<sup>152</sup> However, the facts do not necessarily support these arguments; indeed, some studies have disproven the lobby's arguments.<sup>153</sup> Additionally, the direct-shipment statute may be met with resistance from local wineries that have reaped benefits from the native-wine statute and consequently may not support an entirely new system that gives out-of-state wineries equal shipping access to Iowa residents.

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147. *Id.*

148. The Model Bill suggests that licensees should be restricted to shipping no more than twenty-four nine-liter cases of wine annually to any one person for personal use, and not for resale. *Id.*

149. The Model Bill suggests that all containers that ship directly to residents include a "conspicuous disclaimer" reading "CONTAINS ALCOHOL: SIGNATURE OF PERSON AGE 21 OR OLDER REQUIRED FOR DELIVERY." *Id.*

150. In fashioning these restrictions, the legislature should be aware of some of the statutory provisions that litigants have challenged following *Granholtm*. See *supra* notes 79–83 (noting challenges to retailer restrictions, personal import limits, and volume-caps).

151. See Press Release, Wine & Spirits Wholesalers of Am., Supreme Court Rejection of Carrier Age Verification Calls into Question State Direct Shipping Laws (Feb. 21, 2008), <http://www.wsaw.org/content.cfm?sectionid=20&detail=41&FromSearchResult=direct%20ship> (noting that the Wine and Spirits Wholesalers of America, an organization that represents the interests of alcohol wholesalers, "has long opposed unregulated shipments of alcohol to residences because they dodge the system of state controls which are crucial to preventing abuse"). The organization lists as the "dangers" of direct shipping the "potential introduction of counterfeit or tainted product in the marketplace; ineffective and unverifiable tax collection; and loss of the face-to-face transaction at purchase, highly valued by states in addressing a range of regulatory goals, including preventing sales to minors." *Id.*

152. *Id.*

153. See Donna Leinwand, *Teens Not Rushing Online to Buy Wine, Survey Shows*, USA TODAY, Oct. 9, 2006, at 3A, available at [http://www.usatoday.com/tech/news/2006-08-09-survey-online-alcohol\\_x.htm](http://www.usatoday.com/tech/news/2006-08-09-survey-online-alcohol_x.htm) (noting that a survey from Teenage Research Unlimited found that two percent of youths ages fourteen to twenty had bought alcohol online).

The ABD should take the lead in persuading the legislature to change to the direct-shipment permit system, while informing Iowa wineries about the need for the change. While there are indications that the Iowa ABD supports the movement to a direct-shipment system, the legislature has yet to take action on this issue.<sup>154</sup> Pressure from the ABD would likely be the most successful method for instituting change, as out-of-state wineries are more likely to lobby in states where changes in shipping laws could provide access to more consumers than in Iowa.<sup>155</sup>

Further, the legislature should consider repealing the wine gallonage tax exemption and retail-sale authority privileges provided to Iowa's native-wine manufacturers under the native-wine statute. As described above, these privileges are vulnerable to litigation challenging their constitutionality in light of *Granholm*.<sup>156</sup> This reconsideration, and the move to the direct-shipment permit system, would ensure that Iowa regulates in-state and out-of-state wineries' access to Iowa consumers on equal terms as *Granholm* mandated.

#### V. CONCLUSION

"[T]here are two ways, and two ways only, in which an ordinary private citizen, acting under her own steam and color of no law, can violate the United States Constitution," writes Laurence Tribe. "One is to enslave somebody, a suitably hellish act. The other is to bring a bottle of beer, wine, or bourbon into a State in violation of its beverage control laws . . ."<sup>157</sup> The historically controversial role of state alcohol regulation continues to play out in the nation's courts to this day. At the same time, the growth of Iowa's wine industry makes Iowa's wine laws even more relevant than they have been at any other time. In light of the Supreme Court's decision in *Granholm v. Heald*, Iowa should adopt a direct-shipment permit system to replace both the native-wine and reciprocal-shipping statutes, and should reconsider the privileges granted to native-wine manufacturers under the native-wine statute. Taking this proactive step would help the state avoid potential constitutional challenges, signal to the nation that Iowa is serious about keeping its laws on par with national shifts in wine regulation, and demonstrate that Iowa intends to participate seriously in the national wine market.

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154. Posting of Jeff Carroll to ShipCompliant: Wine Shipping Blog, Free The Grapes! Legislative Update, <http://shipcompliantblog.com/blog/2007/03/19/free-the-grapes-legislative-update/> (Mar. 19, 2007, 5:05).

155. Iowa's per capita wine consumption lags behind other states. TORDSEN ET AL., IOWA STATE UNIV., VALUE-ADDED AGRIC. EXTENSION, GENERAL WINE BACKGROUND 5-6 (2004), available at [http://www.agmrc.org/media/cms/winebackground\\_30609D9EC2BBD.pdf](http://www.agmrc.org/media/cms/winebackground_30609D9EC2BBD.pdf).

156. See *supra* Part III.C (analyzing Iowa's native-wine statute).

157. Laurence H. Tribe, *How to Violate the Constitution Without Really Trying: Lessons from the Repeal of Prohibition to the Balanced Budget Amendment*, 12 CONST. COMMENT. 217, 220 (1995).