

2017

## Tweaking the Twenty-First Amendment: An Argument Against Durational-Residency Requirements for Alcohol Beverage Wholesalers and Retailers

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### Recommended Citation

Keegan J. Shea, *Tweaking the Twenty-First Amendment: An Argument Against Durational-Residency Requirements for Alcohol Beverage Wholesalers and Retailers*, 62 St. Louis U. L.J. (2017).  
Available at: <https://scholarship.law.slu.edu/lj/vol62/iss1/18>

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## TWEAKING THE TWENTY-FIRST AMENDMENT: AN ARGUMENT AGAINST DURATIONAL-RESIDENCY REQUIREMENTS FOR ALCOHOL BEVERAGE WHOLESALERS AND RETAILERS

### INTRODUCTION

Say you lived in Washington D.C. and owned a successful restaurant, the profitability of which depended in part on its wine, beer, and liquor sales. The restaurant was successful enough to begin looking for a second location. You determine that Bethesda, Maryland is an ideal location because it is only *seven miles* from your D.C. residence, but there is one problem: the Maryland Code of Alcoholic Beverages imposes a two-year durational-residency requirement on restaurant owners seeking a restaurant liquor license.<sup>1</sup> In order to sell alcohol at the new restaurant, you have to establish a second residence in Bethesda, live there for two years, and face the associated costs.

The Commerce Clause gives the U.S. Congress power to “regulate Commerce . . . among the several States.”<sup>2</sup> This affirmative grant of power

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1. See MD. CODE ANN., Alcoholic Beverages § 4-109(a)(4) (West 2016) (requiring an applicant for a liquor license to have been a resident for the “2 years immediately before filing the application”); see also Aaron Kraut, *Liquor License Residency Requirement a Hurdle to Some*, BETHESDA MAG. (Jan. 23, 2014), <http://www.bethesdamagazine.com/Bethesda-Beat/2014/Liquor-License-Residency-Requirement-A-Hurdle-To-Some/> [<https://perma.cc/QBX9-QU53>]. Maryland is not the only State that imposes durational-residency requirements on alcohol beverage wholesalers and/or retailers. In Tennessee, a retail liquor license may be issued only if you have been a “bona fide resident of [the] state during the two-year period immediately preceding the date upon which application is made.” TENN. CODE ANN. § 57-3-204(b)(2)(A) (West 2016). This statute was ruled unconstitutional by the U.S. District Court for the Middle District of Tennessee in *Byrd v. Tennessee Wine & Spirits Retailers Ass’n*, 259 F. Supp. 3d 785 (M.D. Tenn. 2017). The case has been appealed to the Sixth Circuit, but no decision had been issued at the time this Comment was due for publication. In Wisconsin, you must have resided continuously in the state for at least ninety days prior to the application date to qualify for any license related to alcohol beverages. WIS. STAT. ANN. § 125.04(5)(a)(2) (West 2016). In Missouri, a corporation must be a “resident corporation” to obtain a wholesaler license. MO. REV. STAT. § 311.060.2(3) (2016). To be a “resident corporation,” the corporation must be incorporated under the laws of Missouri, and all of its officers and directors must be “bona fide residents” of Missouri for at least three years. *Id.* § 311.060.3. In Indiana, a corporation cannot obtain an “alcoholic beverage retailer’s permit of any type unless sixty percent (60%) of the outstanding common stock is owned by persons who have been continuous and bona fide residents of Indiana for five (5) years.” IND. CODE § 7.1-3-21-5(a) (2017); see also Greg Trotter, *Binny’s Expansion to Indiana Thwarted by State Liquor Law Changes*, CHI. TRIB. (Apr. 15, 2016, 2:00 PM), <http://www.chicagotribune.com/business/ct-binnys-indiana-expansion-0417-biz-20160415-story.html> [<https://perma.cc/V6K4-537Q?type=image>].

2. U.S. CONST. art. I, § 8, cl. 3.

implies a negative converse known as the dormant Commerce Clause, which prohibits the States from passing legislation that improperly burdens or discriminates against interstate commerce.<sup>3</sup> Normally, when a state statute discriminates on its face, in its purpose, or in its effect against interstate commerce, a strict scrutiny test is applied, and the State must advance “a legitimate local purpose that cannot be adequately served by reasonable nondiscriminatory alternatives” in order to validate the statute.<sup>4</sup> At a minimum, imposing a durational-residency requirement on alcohol beverage wholesalers and retailers discriminates in its effect against interstate commerce because it denies out-of-state residents access to the alcohol market on equal terms as in-state residents.<sup>5</sup> However, Section 2 of the Twenty-first Amendment can save state alcohol regulations, such as durational-residency requirements, from Commerce Clause scrutiny.<sup>6</sup> Section 2 of the Amendment provides: “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.”<sup>7</sup>

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3. See *City of Philadelphia v. New Jersey*, 437 U.S. 617, 626–28 (1978) (holding a state law unconstitutional because it discriminated against articles of interstate commerce); *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142, 145 (1970) (holding a state law unconstitutional because it improperly burdened interstate commerce); see also *New Energy Co. of Ind. v. Limbach*, 486 U.S. 269, 273 (1988) (“It has long been accepted that the Commerce Clause not only grants Congress the authority to regulate commerce among the States, but also directly limits the powers of the States to discriminate against interstate commerce.”).

4. *New Energy Co. of Ind.*, 486 U.S. at 278; see also *Philadelphia*, 437 U.S. at 628. A state statute that discriminates against interstate commerce faces a “virtually *per se* rule of invalidity.” *Id.* at 624.

5. See *Or. Waste Sys., Inc. v. Dept. of Env'tl. Quality of Or.*, 511 U.S. 93, 99 (1994) (“‘Discrimination’ simply means differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter.”). A durational-residency requirement burdens out-of-state residents. An in-state resident either already meets the durational-residency requirement or it at least has more “in-state days” to put toward the requirement than an out-of-state resident.

6. “Commerce Clause scrutiny” refers to both a strict scrutiny test and a *Pike* balancing test. If the statute regulates evenhandedly (i.e., it does not discriminate on its face, purpose, or effect) to advance the health, safety, or welfare of its citizens, but it still has some inadvertent or incidental impact on interstate commerce, then a *Pike* balancing test is applied. See *Pike*, 397 U.S. at 142. Under the *Pike* balancing test, the statute does not face a “virtually *per se* rule of invalidity.” *Philadelphia*, 437 U.S. at 624. Rather, the statute is valid unless the burden on commerce is “clearly excessive” when measured against the state interest. *Pike*, 397 U.S. at 142.

7. U.S. CONST. amend. XXI, § 2. In an effort to end Prohibition, Congress proposed the Twenty-first Amendment to the States, and on December 5, 1933, the requisite 3/4 of States ratified it through state ratifying conventions. Robert P. George, *The Twenty-First Amendment*, CONST. CTR., <https://constitutioncenter.org/interactive-constitution/amendments/amendment-xxi> [<https://perma.cc/3K9Y-D2Z9>]. The Twenty-first Amendment is the only Amendment to have been ratified by state ratifying conventions. *Id.*

Early Supreme Court cases interpreting Section 2 held that it gave the States authorization to discriminate against alcohol.<sup>8</sup> This view slowly changed, and the Supreme Court has more recently held that the Twenty-first Amendment does not entirely remove state alcohol regulations from Commerce Clause scrutiny.

To draw a conclusion . . . that the Twenty-first Amendment has somehow operated to “repeal” the Commerce Clause wherever regulation of intoxicating liquors is concerned would, however, be an absurd oversimplification. If the Commerce Clause had been *pro tanto* “repealed,” then Congress would be left with no regulatory power over interstate or foreign commerce in intoxicating liquor. Such a conclusion would be patently bizarre and is demonstrably incorrect.<sup>9</sup>

Although the Twenty-first Amendment does not save all state alcohol regulations from Commerce Clause scrutiny, it has and continues to give the States significant power in how they design their alcohol distribution systems. Once the Amendment passed, many States developed a three-tier system of alcohol distribution, and now virtually every State has adopted it.<sup>10</sup> The three tiers are: (1) the producer or supplier, (2) the distributor or wholesaler, and (3) the retailer.<sup>11</sup> Typically, producers sell to in-state wholesalers, and the wholesalers pay excise taxes.<sup>12</sup> In-state wholesalers sell to in-state retailers, such as the local liquor store, bar, or restaurant that sells alcohol.<sup>13</sup> The retailers then sell to consumers and collect state sales tax.<sup>14</sup> The “main purpose” of the three-tiered system was to eliminate “the existence of a ‘tied’ system between producers and retailers, a system generally believed to enable organized crime

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8. *See* State Bd. of Equalization of Cal. v. Young’s Mkt. Co., 299 U.S. 59, 62 (1936) (“The words used [in Section 2] are apt to confer upon the State the power to forbid all importations which do not comply with the conditions which it prescribes. The plaintiffs ask us to limit this broad command. They request us to construe the Amendment as saying, in effect: The State may prohibit the importation of intoxicating liquors provided it prohibits the manufacture and sale within its borders; but if it permits such manufacture and sale, it must let imported liquors compete with the domestic on equal terms. To say that, would involve not a construction of the Amendment, but a rewriting of it.” (emphasis added)); *see also* Indianapolis Brewing Co. v. Liquor Control Comm’n of Mich., 305 U.S. 391, 394 (1939) (holding that “the right of a state to prohibit or regulate the importation of intoxicating liquor is not limited by the commerce clause”); *Mahoney v. Joseph Triner Corp.*, 304 U.S. 401, 403–04 (1938) (upholding a statute that “clearly discriminates in favor of liquor processed within the State as against liquor completely processed elsewhere”).

9. *Hostetter v. Idlewild Bon Voyage Liquor Corp.*, 377 U.S. 324, 331–32 (1964).

10. Andrew Tamayo, *What’s Brewing in the Old North State: An Analysis of the Beer Distribution Laws Regulating North Carolina’s Craft Breweries*, 88 N.C. L. REV. 2198, 2204 (2010).

11. *Arnold’s Wines, Inc. v. Boyle*, 571 F.3d 185, 187 (2d Cir. 2009); *see also* Tamayo, *supra* note 10, at 2204.

12. *Arnold’s Wines*, 571 F.3d at 187; *see also* Tamayo, *supra* note 10, at 2200–01, 2204.

13. Tamayo, *supra* note 10, at 2201, 2204.

14. *Arnold’s Wines*, 571 F.3d at 187; *see also* Tamayo, *supra* note 10, at 2204.

to dominate the industry.”<sup>15</sup> Curbing alcohol consumption was another goal of the three-tier system.<sup>16</sup> However, some States use their regulatory power under the three-tier system to impose durational-residency requirements on alcohol beverage wholesalers and retailers.<sup>17</sup>

This Comment will argue that the Twenty-first Amendment does not save these durational-residency requirements from Commerce Clause scrutiny. Part I of this Comment examines the Supreme Court’s decision in *Granholm v. Heald*, which struck down state statutes that effectively required out-of-state wineries to operate in state before they could compete on equal terms with in-state wineries. Although the statutes did not impose durational-residency requirements, *Granholm* is the leading case on the interplay between the Twenty-first Amendment and the Commerce Clause. Part II examines a current circuit split between the Eighth Circuit and Fifth Circuit. In 2013, the Eighth Circuit held that the Twenty-first Amendment saves durational-residency requirements for wholesalers from Commerce Clause scrutiny. In 2016, the Fifth Circuit held that the Amendment does not authorize durational-residency requirements for wholesalers and retailers, and thus the requirements are subject to Commerce Clause scrutiny. Part III argues that the Eighth Circuit’s holding should be reversed because durational-residency requirements directly regulate citizens, and the Twenty-first Amendment only gives States the power to directly regulate alcohol products.

#### I. GRANHOLM V. HEALD

In *Granholm*, the Supreme Court struck down both Michigan and New York statutes that permitted in-state wineries to ship their products directly to in-state consumers, but prohibited out-of-state wineries from doing so.<sup>18</sup> To obtain this preferential treatment and bypass the three-tier system, an out-of-state winery needed to set-up an in-state operation. The statutes did not impose durational-residency requirements.<sup>19</sup> Rather, they effectively imposed “physical presence”

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15. *Arnold’s Wines*, 571 F.3d at 187.

16. Professor Marcia Yablon argues that the Twenty-first Amendment was “created to effectuate . . . temperance goals.” Marcia Yablon, *The Prohibition Hangover: Why We Are Still Feeling the Effects of Prohibition*, VA. J. SOC. POL’Y & LAW 552, 554 (2006). To effectuate those goals, the three-tier system sought to curb consumption by subjecting alcoholic beverages to two layers of tax, *see, e.g., id.*, which inevitably leads to higher prices.

17. *See supra* note 1 and accompanying text. When this Comment refers to wholesalers and retailers, it is specifically referring to alcohol beverage wholesalers and retailers.

18. *Granholm v. Heald*, 544 U.S. 460, 465–66 (2005).

19. Although *Granholm* did not deal with durational-residency requirements, it is the leading case on the interplay between the Twenty-first Amendment and the Commerce Clause. The Eighth Circuit relied heavily on the principles and reasoning established in *Granholm* when it held that the Twenty-first Amendment authorized durational-residency requirement for wholesalers.

requirements.<sup>20</sup> Ultimately, the Court, in a 6–3 decision, held that the statutes were not authorized by the Twenty-first Amendment and violated the Commerce Clause.<sup>21</sup>

A. *Michigan and New York Statutes*

In Michigan, most alcoholic beverages must pass through a three-tier system.<sup>22</sup> Under this system, both in-state and out-of-state producers may sell only to licensed in-state wholesalers.<sup>23</sup> The wholesalers may sell only to in-state retailers, and then in-state retailers sell the alcohol to consumers.<sup>24</sup> Thus, producers cannot bypass the three-tier system and sell directly to consumers. However, the Michigan statute created an exception for in-state wineries, which allowed them to bypass the system and sell directly to in-state consumers.<sup>25</sup> Out-of-state wineries did not receive this preferential treatment. Rather, they had to first distribute their products through the state’s three-tier system and face the inherent disadvantages.<sup>26</sup>

In New York, alcohol is also distributed through a three-tier system.<sup>27</sup> However, wineries that produce wine only from New York grapes (i.e., in-state wineries)<sup>28</sup> qualify for a license allowing them to bypass the three-tier system and ship directly to in-state consumers.<sup>29</sup> A winery that does not produce wine from New York grapes (i.e., an out-of-state winery) can bypass the three-tier system only if it becomes a “licensed New York winery.”<sup>30</sup> This requires the establishment of “a branch factory, office or storeroom within the state of New York.”<sup>31</sup> Both the New York and Michigan statutes effectively required out-of-

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20. *Granholm*, 544 U.S. at 474.

21. *Id.* at 466. In other words, the statutes did not survive Commerce Clause scrutiny.

22. *Id.* at 468–69.

23. *Id.* at 469.

24. *Id.*

25. *Granholm*, 544 U.S. at 469. The statute made *only* in-state wineries eligible for a license to ship directly to in-state consumers. *Id.*

26. *See id.* at 466. The Court recognized that the statutes at issue put out-of-state wineries at a disadvantage from an “economic standpoint.” *Id.* For example, assume there is one in-state producer and one out-of-state producer, and each makes the exact same product. If the product has to pass through an in-state wholesaler and an in-state retailer before reaching the consumer, then the price of the product is naturally going to rise. But if the in-state producer can skip these steps, then it can sell its product cheaper and gain a “competitive advantage” over the out-of-state producer. *See id.*

27. *Id.* at 470.

28. The effect of the statute was to benefit in-state wineries because a winery residing in New York will most likely use grapes grown in New York. “[T]he result is to allow local wineries to make direct sales to consumers in New York on terms not available to out-of-state wineries.” *Id.*

29. *Id.*

30. *Granholm*, 544 U.S. at 470.

31. *Id.* (quoting N.Y. ALCO. BEV. CONT. LAW ANN. § 3(37) (West. Supp. 2005)) (internal quotation marks omitted).

state wineries to have a “physical presence” in the state before their wine received the same treatment as in-state wine.<sup>32</sup>

*B. Strict Scrutiny Test Triggered*

The Court had “no difficulty” in determining that these statutes discriminated against interstate commerce because they gave preferential treatment to in-state producers.<sup>33</sup> As a result, the statutes “deprive[d] citizens of their right to have access to the markets of other States on equal terms.”<sup>34</sup>

If a state statute discriminates on its face, in its purpose, or in its effect against an out-of-state interest or interstate commerce, then the statute faces a “virtually *per se* rule of invalidity” and a strict scrutiny test is applied.<sup>35</sup> In order to validate the statute, the State must show that the discriminatory regulation “advances a legitimate local purpose that cannot be adequately served by reasonable nondiscriminatory alternatives.”<sup>36</sup> These statutes are routinely struck down unless “the discrimination [they impose] is demonstrably justified by a valid factor unrelated to economic protectionism.”<sup>37</sup> Here, if the challenged statutes were not alcohol regulations, the Court would immediately apply a strict scrutiny test.

*C. Does the Twenty-First Amendment Save the Statutes from Commerce Clause Scrutiny?*

The Court recognized that the statutes faced “a virtually *per se* rule of invalidity.”<sup>38</sup> But before applying a strict scrutiny test, the Court considered whether Section 2 of the Twenty-first Amendment saved the statutes.<sup>39</sup> The Court noted that this section

“grants the States virtually complete control over whether to permit importation or sale of liquor and how to structure the liquor distribution system.” A State which chooses to ban the sale and consumption of alcohol altogether could bar its importation; and, as our history shows, it would have to do so to make its laws effective. States may also . . . funnel [alcohol] sales through the three-tier

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32. *Id.* at 474. “Out-of-state wineries . . . face[d] a complete ban on direct shipment.” *Id.*

33. *Id.* at 476.

34. *Id.* at 473.

35. *City of Philadelphia v. New Jersey*, 437 U.S. 617, 624 (1978); *see also Granholm*, 544 U.S. at 476.

36. *Or. Waste Sys., Inc. v. Dep’t. of Env’tl. Quality of Or.*, 511 U.S. 93, 100–01 (1994) (quoting *New Energy Co. of Ind. v. Limbach*, 486 U.S. 269, 278 (1988)) (internal quotation marks omitted).

37. *New Energy Co. of Ind.*, 486 U.S. at 274.

38. *Granholm*, 544 U.S. at 476 (quoting *Philadelphia*, 437 U.S. at 624) (internal quotation marks omitted).

39. *Id.*

system. We have previously recognized that the three-tier system itself is “unquestionably legitimate.”<sup>40</sup>

Thus, Section 2 is in tension with the Commerce Clause because it gives the States significant power in a particular field of interstate commerce. Resolving this tension, the Court held that even though Section 2 gives States power to regulate alcohol, it “does not displace the rule that States may not give a discriminatory preference to their own producers.”<sup>41</sup> The nondiscrimination principle of the Commerce Clause still applies to state alcohol regulations.<sup>42</sup> Here, the statutes were a “straightforward” attempt to discriminate against out-of-state producers, and thus the Twenty-first Amendment did not save them from Commerce Clause scrutiny.<sup>43</sup>

#### D. *Returning to a Strict Scrutiny Test*

The Court returned to a strict scrutiny test to determine whether the statutes “advance[] a legitimate local purpose that cannot be adequately served by reasonable nondiscriminatory alternatives.”<sup>44</sup> First, the States proposed that the statutes served legitimate state interests by keeping alcohol out of the hands of minors because minors have easy access to credit cards and the Internet.<sup>45</sup> But the States offered no “concrete evidence” that out-of-state wineries shipping to in-state consumers will increase alcohol consumption by minors.<sup>46</sup> And the Court requires the “clearest showing” to justify a discriminatory state statute.<sup>47</sup>

Second, New York argued that its statute facilitated tax collection to protect against potential lost tax revenue.<sup>48</sup> Although the Court recognized that New

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40. *Id.* at 488–89 (first quoting *Cal. Retail Liquor Dealers Ass’n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 110 (1980); and then quoting *North Dakota v. United States*, 495 U.S. 423, 432 (1982) (Scalia, J., concurring)).

41. *Id.* at 486.

42. *Id.* at 487.

43. *Granholm*, 544 U.S. at 489.

44. *Id.* at 489 (quoting *New Energy Co. of Ind. v. Limbach*, 486 U.S. 269, 278 (1988)) (internal quotation marks omitted).

45. *Id.* at 489–90. The States argued that minors “are likely to take advantage of direct wine shipments as a means of obtaining alcohol illegally.” *Id.* at 489.

46. *Id.* at 490.

47. *Id.* (quoting *C & A Carbone, Inc. v. Town of Clarkstown*, 511 U.S. 383, 393 (1994)) (internal quotation marks omitted).

48. *Granholm*, 544 U.S. at 491. Michigan advanced a similar argument, but the Court quickly recognized it as a “diversion.” *Id.* Most States rely on wholesalers to collect taxes. *Id.* The wholesalers pay excise tax, and the retailers pay sales tax. *See, e.g., Frequently Asked Questions Regarding Alcoholic Beverages Excise Tax*, N.C. DEP’T REV., <https://files.nc.gov/ncdor/documents/faq/alcoholfaq.pdf?YE1DwnS2aR5v7t4ffOo.oom37XBuIOEh> [<https://perma.cc/U3V7-TZ74>]. Michigan does not rely on wholesalers to collect taxes. *Granholm*, 544 U.S. at 491. Instead it “collects taxes directly from out-of-state wineries on all wine shipped to in-state wholesalers.” *Id.* It requires out-of-state wineries to submit to the state a tax report of all wine sold. *Id.* The Court

York's tax collection concern was not "wholly illusory," this objective could be achieved without discriminating against interstate commerce.<sup>49</sup> The Court found that something as simple as requiring producers to submit regular sales reports and pay state taxes based on the reports could achieve New York's end goal.<sup>50</sup> Other rationales New York and Michigan offered were: "facilitating orderly market conditions, protecting public health and safety, and ensuring regulatory accountability."<sup>51</sup> Yet, the Court found that these objectives could be achieved with a nondiscriminatory alternative (i.e., an "evenhanded licensing requirement").<sup>52</sup> Thus, although States have broad power to regulate alcohol under Section 2, they must do so on evenhanded terms unless they can demonstrate the need for discrimination.<sup>53</sup>

#### E. Granholm Test

The test, set forth in *Granholm*, for determining the constitutionality of state alcohol regulations can be summarized as follows: the Twenty-first Amendment saves state alcohol regulations "when they treat [alcohol] produced out of state the same as its domestic equivalent."<sup>54</sup> A regulation requiring out-of-state wineries to have an in-state presence if their wine is to receive the same treatment as wine from an in-state winery fails this test, and it must survive Commerce Clause scrutiny to be deemed constitutional. Although the Court made clear that "straightforward attempts" to discriminate, like the New York and Michigan statutes, are not saved,<sup>55</sup> it provided no examples of non-straightforward attempts.<sup>56</sup>

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found "[i]f licensing and self-reporting provide adequate safeguards for wine distributed through the three-tier system, there is no reason to believe they will not suffice for direct shipments." *Id.*

49. *Granholm*, 544 U.S. at 491.

50. *Id.*

51. *Id.* at 492.

52. *Id.*

53. *Id.* at 493.

54. *Granholm*, 544 U.S. at 489.

55. *Id.*

56. What would qualify as a non-straightforward attempt, and therefore would be saved by the Twenty-first Amendment? The New York and Michigan statutes discriminated, at a minimum, in their effect, against interstate commerce because they denied out-of-state residents access to the alcohol market on equal terms as in-state residents. The statutes also likely discriminated in their purpose—the Court referred to them as "straightforward attempts" to discriminate. *Id.* Either way, the discrimination triggers a strict scrutiny test, and ultimately the Court applied a strict scrutiny test. *Id.* If the Twenty-first Amendment cannot save a state alcohol regulation that triggers strict scrutiny, from an application of the strict scrutiny test, what regulations can it save? One clear answer is the three-tier system. As *Granholm* shows, States can require all alcohol products to pass through a three-tier distribution system. *Id.* A statute enforcing the three-tier system without any exceptions regulates evenhandedly between in-state and out-of-state producers, but it still arguably has some inadvertent or incidental impact on interstate commerce. See *Pike*, 397 U.S. at 142. For example, in a three-tier system the producer sells to the wholesalers. Marc Sorini, *Understanding*

## II. CIRCUIT SPLIT: EIGHTH CIRCUIT VS. FIFTH CIRCUIT

### A. *The Applicability of the Granholm Test Outside the Producer Tier*

The *Granholm* test focused on the physical product—alcohol; yet, the statutes at issue regulated the producers.<sup>57</sup> When considering a regulation of the producer tier, a test that focuses on the treatment of the product makes sense because the producer tier *produces* the alcohol products. Producers and products are so intertwined that a statute regulating one has a direct impact on the other.<sup>58</sup> The test created by *Granholm* is specifically tied to the producer tier, and it is important to recognize that the *Granholm* test is limited to discrimination benefitting alcohol on the basis of its in-state production status.

*Granholm's* test and its focus on the physical product should not extend to the wholesaler and retailer tiers because these tiers are inherently different from the producer tier.<sup>59</sup> A State cannot require all alcohol sold in the state to be produced in the state.<sup>60</sup> For example, Anheuser-Busch has production operations in eleven states, but consumers can buy its products in all fifty states.<sup>61</sup> Thus, *Granholm* recognized that producers do not have to be in state, but their products may have to pass through the in-state alcohol distribution system before reaching

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*the Three-Tier System: Its Impact on U.S. Craft Beer and You*, CRAFTBEER.COM (Mar. 6, 2017), <https://www.craftbeer.com/craft-beer-muses/three-tier-system-impacts-craft-beer> [https://perma.cc/X7YQ-TMQQ]. And a State can require all alcohol to go through licensed in-state wholesalers. See *North Dakota v. United States*, 495 U.S. 423, 432 (1982) (Scalia, J., concurring). The requirement that all alcohol pass through an in-state wholesaler is likely to have an incidental impact on out-of-state producers: an out-of-state producer may face greater transportation costs to get its product to the wholesaler; an in-state producer may have a better business relationship with the in-state wholesaler; or an out-of-state producer may not be able to find an in-state wholesaler to do business with. If an out-of-state producer brought an action against the State, the Twenty-first Amendment would save the requirement from application of the *Pike* balancing test.

57. The New York statute required out-of-state wineries to create a physical establishment in New York in order for their wine to receive the same treatment as wine from in-state wineries. See *Granholm*, 544 U.S. at 470. In Michigan, the winery had to be “in-state” before its products could be shipped directly to consumers. See *id.* at 469.

58. For example in *Granholm*, an out-of-state *producer* had to set-up an in-state operation before its *products* received equal treatment. *Id.* at 466.

59. For example, imagine there is a state regulation requiring all alcohol sold in the state to be produced in the state (I say “imagine” because this regulation would surely not be saved by the Twenty-first Amendment). This would be a regulation of products, and it would directly affect producers by requiring them to be in state. However, this statute would not have the same impact on wholesalers and retailers because they do not *produce* the product. Wholesalers and retailers could still do business in the state, but the pool of producers they could buy alcohol from would be greatly reduced.

60. See *Granholm*, 544 U.S. at 472 (“The mere fact of nonresidence should not foreclose a producer in one State from access to markets in other States.”).

61. See *Anheuser-Busch InBev: Other Locations*, BREWERYDB, <http://www.brewerydb.com/brewery/BznahA/locations> [https://perma.cc/6JW5-2XMG] (showing that Anheuser-Busch has twelve production operations throughout eleven states).

consumers. So if a State cannot require producers to be in state, but it can subject the producer's products to its distribution laws, then a test focusing on the treatment of the products makes sense. The *Granholtm* analysis, and its application of the nondiscrimination principle, is still relevant when examining a regulation of the wholesaler or producer tier, but it is important to realize why the Court's test focused on the product and not the physical entity producing the product.

Despite the special nature of the producer tier, the Eighth Circuit borrowed from the test set forth in *Granholtm* and concluded that a State may condition access to the wholesaler tier of its three-tier system on durational-residency. In 2016, the Fifth Circuit expressly declined to follow the Eighth Circuit and held that the Twenty-first Amendment does not authorize durational-residency requirements for wholesalers and retailers.

*B. Eighth Circuit: The Twenty-First Amendment Saves Durational-Residency Requirements from Commerce Clause Scrutiny*

In *Southern Wine & Spirits of America, Inc. v. Division of Alcohol and Tobacco Control*, the Eighth Circuit upheld a Missouri statute that imposed a durational-residency requirement on alcohol wholesalers.<sup>62</sup> The statute in question provides: "No wholesaler license shall be issued to a corporation for the sale of intoxicating liquor containing alcohol in excess of five percent by weight, *except to a resident corporation* as defined in this section."<sup>63</sup> In order to qualify as a resident corporation, the corporation must be incorporated under Missouri law, and *all* of its officers and directors must have been "bona fide residents" of Missouri *for at least three years*.<sup>64</sup>

The Division of Alcohol and Tobacco Control of the Missouri Department of Public Safety (the "Division") denied Southern Wine & Spirits of Missouri, Inc. ("Southern Missouri") a wholesaler liquor license because the company was not a "resident corporation" under Missouri law.<sup>65</sup> Southern Missouri's parent company and sole shareholder, Southern Wine & Spirits of America, Inc.

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62. 731 F.3d 799, 812–13 (8th Cir. 2013).

Missouri funnels liquor sales through a tier system, separating the distribution market into discrete levels: the first tier consists of producers, such as brewers, distillers, and winemakers; the second tier is comprised of solicitors, who acquire alcohol from producers and sell it "to, by or through" wholesalers; the third tier is made up of wholesalers, who purchase alcohol from producers or solicitors and sell it to retailers; and the fourth tier consists of retailers, who sell alcohol to consumers.

*Id.* at 802 (citing MO. REV. STAT. §§ 311.180(1), 311.200 (2013)).

63. MO. REV. STAT. § 311.060.2(3) (emphasis added); *see also S. Wine*, 731 F.3d at 802.

64. *S. Wine*, 731 F.3d at 802; *see also* MO. REV. STAT. § 311.060.3.

65. *S. Wine*, 731 F.3d at 803; *see also* MO. REV. STAT. § 311.060.2(3).

(“SWSA”),<sup>66</sup> operates its wholesale alcohol business in thirty-two other states and the District of Columbia.<sup>67</sup> Even though Southern Missouri is incorporated in Missouri, it was not free to do business in Missouri simply because its officers and directors were Florida residents.<sup>68</sup>

#### 1. Did the Statute Have a Discriminatory Purpose?

SWSA pointed to a news report quoting one of the legislation’s sponsors back in 1947, which said the law “was intended to prevent a few big national distillers from monopolizing the wholesale liquor business in Missouri.”<sup>69</sup> Thus, SWSA argued that the purpose of the statute was “mere economic protectionism,”<sup>70</sup> and relied on *Bacchus Imports, Ltd. v. Dias* to argue that alcohol regulations motivated by protectionist intent are unconstitutional.<sup>71</sup> However, the Eighth Circuit rejected the “mere economic protectionism” argument for several reasons.<sup>72</sup>

In dismissing this argument, the Eighth Circuit relied heavily on a “purpose clause” that was added to the statute in 2007, sixty years after the residency requirement was adopted.<sup>73</sup> It provides that the purpose of this chapter is “to promote responsible consumption, combat illegal underage drinking, and achieve other important state policy goals such as maintaining an orderly marketplace composed of state-licensed alcohol producers, importers, distributors, and retailers.”<sup>74</sup> The Eighth Circuit treated this “purpose clause” as controlling because SWSA offered no support for the proposition that a later legislature “cannot supplant an earlier legislature’s intended purpose by enacting an express statutory purpose provision.”<sup>75</sup>

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66. SWSA, Southern Missouri, and four Florida residents who are officers or directors of SWSA and Southern Missouri and shareholders of SWSA (collectively “SWSA”) brought this action. *S. Wine*, 731 F.3d at 803.

67. *Id.*

68. *Id.*

69. *Id.* at 807 (internal quotation marks omitted).

70. *Id.* (quoting *Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263, 276 (1984)) (internal quotation marks omitted).

71. *S. Wine*, 731 F.3d at 809. In *Bacchus*, the Supreme Court ruled that a protectionist tax exemption was unconstitutional because it violated a central tenet of the Commerce Clause, and “mere economic protectionism” is not a clear concern of the Twenty-first Amendment. *Bacchus*, 468 U.S. at 276. SWSA attempted to “sail under the *Bacchus* flag” and win the day solely under a “mere economic protectionism” argument. *S. Wine*, 731 F.3d at 807, 809.

72. First, SWSA did not raise this argument at the trial level. *S. Wine*, 731 F.3d at 807. Second, newspaper articles are “rank hearsay.” *Id.* at 807–08. Third, this statement represents only a single legislator’s views about the purpose of the residency requirement. *Id.* at 808. Fourth, the statement does not establish the sort of protectionist intent that was conceded by the State in *Bacchus*. *Id.*

73. *Id.* at 808.

74. MO. REV. STAT. § 311.015 (2013); *see also S. Wine*, 731 F.3d at 808.

75. *S. Wine*, 731 F.3d at 809.

## 2. Eighth Circuit's Test Helps Twenty-First Amendment Save the Statute from Commerce Clause Scrutiny

After concluding that the statute was not motivated by “mere economic protectionism,” the Eighth Circuit’s analysis shifted to whether the Twenty-first Amendment gives States the power to require a wholesaler to be an in-state resident without running afoul of the Commerce Clause.<sup>76</sup> The Eighth Circuit combined two *Granholm* principles and created a test to analyze the residency requirement’s constitutionality: “[S]tate policies that define the structure of the liquor distribution system while giving equal treatment to in-state and out-of-state liquor products and producers” are protected from “constitutional challenges based on the Commerce Clause.”<sup>77</sup> If a state alcohol regulation meets this test, then, according to the Eighth Circuit, the Twenty-first Amendment saves it.

The first part of this test, “state policies that define the structure of the liquor distribution system,”<sup>78</sup> comes from *Granholm*’s recognition that the three-tier system is “unquestionably legitimate.”<sup>79</sup> Right after this recognition, *Granholm* quoted Justice Scalia’s concurring opinion from *North Dakota v. United States*: “The Twenty-first Amendment . . . empowers North Dakota to require that all liquor sold for use in the State be purchased from a licensed in-state wholesaler.”<sup>80</sup> Thus, state policies that require wholesalers to be in-state do not “run[] afoul of the Commerce Clause.”<sup>81</sup> And, according to the Eighth Circuit, if States can require wholesalers to be in-state, then they can also define the degree of “in-state” presence.<sup>82</sup>

The second part of the test, “while giving equal treatment to in-state and out-of-state liquor product and producers,”<sup>83</sup> comes from *Granholm*’s test: “State policies are protected under the Twenty-first Amendment when they treat liquor produced out of state the same as its domestic equivalent.”<sup>84</sup> Here, the Eighth Circuit held that the Missouri statute “does not discriminate against out-

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76. *Id.* at 810.

77. *Id.* at 809 (emphasis added).

78. *Id.* (emphasis added).

79. *Granholm v. Heald*, 544 U.S. 460, 489 (2005) (quoting *North Dakota v. United States*, 495 U.S. 423, 432 (1982) (Scalia, J., concurring)).

80. *North Dakota*, 495 U.S. at 432; *see also Granholm*, 544 U.S. at 489.

81. *S. Wine*, 731 F.3d at 810.

82. *Id.*

83. *Id.* at 809 (emphasis added).

84. *Granholm*, 544 U.S. at 489. The Eighth Circuit also borrowed the holding from the Second Circuit in *Arnold’s Wines, Inc. v. Boyle*. “Because New York’s three-tier system treats in-state and out-of-state liquor the same, and does not discriminate against out-of-state products or producers, we need not analyze the regulation further under Commerce Clause principles.” *Arnold’s Wines, Inc. v. Boyle*, 571 F.3d 185, 191 (2d Cir. 2009).

of-state liquor products or producers.”<sup>85</sup> Ironically, the statute does not regulate products or producers—it regulates wholesalers. Thus, because Missouri’s durational-residency requirement meets the Eighth Circuit’s two-part test, the Twenty-first Amendment protects it from Commerce Clause scrutiny.

SWSA attacked the first part of this test and contended that the durational-residency requirement is not “protected” because it is not an “inherent” or “integral” part of the alcohol distribution system.<sup>86</sup> But according to the Eighth Circuit, “[t]here is no archetypal three-tier system from which the ‘integral’ or ‘inherent’ elements of that system may be gleaned.”<sup>87</sup> Even if there was, the Supreme Court in *Granholm* cited “in-state wholesaler” in the first sentence after it declared the three-tier system “unquestionably legitimate.”<sup>88</sup> Thus, according to the Eighth Circuit, it follows that in-state wholesalers must be an “inherent” or “integral” part of the three-tier system.<sup>89</sup> The Eighth Circuit seems to argue that there are no “inherent” or “integral” parts to the three-tier system, and any regulation defining the structure of the three-tier system is eligible to be saved from Commerce Clause scrutiny.

### 3. Rational Basis Test

For cautionary purposes, the Eighth Circuit proceeded as if the residency requirement did not have a protected status.<sup>90</sup> Rather than applying a strict scrutiny or balancing test, it applied a rational basis test and held that the law “passes muster.”<sup>91</sup>

The legislature legitimately could believe that a wholesaler governed . . . by Missouri residents is more apt to be socially responsible and to promote temperance, because the officers, directors, and owners are residents of the

85. *S. Wine*, 731 F.3d at 810. But the Eighth Circuit does not explain how this statute does not discriminate against out-of-state liquor products. It likely reached this conclusion because the statute regulates people and not products.

86. *Id.* *Granholm* insulated from Commerce Clause scrutiny only discrimination that is “inherent in the three-tier system itself.” *Wine Country Gift Baskets.com v. Steen*, 612 F.3d 809, 818 (5th Cir. 2010).

87. *S. Wine*, 731 F.3d at 810.

88. *Id.*; see also *Granholm*, 544 U.S. at 489 (quoting *North Dakota v. United States*, 495 U.S. 423, 432 (1982) (Scalia, J., concurring)) (internal quotation marks omitted).

89. *S. Wine*, 731 F.3d at 810.

90. *Id.* at 810–11.

91. *Id.* at 811. The court said the policy is subject to “deferential scrutiny.” *Id.* Deferential scrutiny typically refers to rational basis review. See Jennie S. Stinebaugh, Comment, *Constitutional Law—Heller v. Doe: The Rational Basis Review Guessing Game*, 25 U. MEM. L. REV. 329, 331 (1994) (“The rational basis standard is quite deferential, and statutes scrutinized under it are presumed to be constitutional and are almost always upheld.”); see also Raphael Holoszyc-Pimentel, Note, *Reconciling Rational-Basis Review: When Does Rational Basis Bite?*, 90 N.Y.U. L. REV. 2070, 2074 (2015) (“Traditionally, rational-basis review is extremely deferential to legislatures’ enactments.”).

community and thus subject to negative externalities—drunk driving, domestic abuse, underage drinking—that liquor distribution may produce. . . . The legislature logically could conclude that in-state residency facilitates law enforcement against wholesalers, because it is easier to pursue in-state owners, directors, and officers than to enforce against their out-of-state counterparts.<sup>92</sup>

Yet, there was doubt as to whether the residency requirement was even rationally related to these interests. The deputy state supervisor for the Division, who testified on *behalf* of the Division, could not “‘think of any’ relationship between the residency requirement and the safety of Missouri citizens.”<sup>93</sup> Additionally, Missouri already had one nonresident wholesaler who was grandfathered in.<sup>94</sup>

C. *Fifth Circuit: The Twenty-First Amendment Does Not Authorize Durational-Residency Requirements for Wholesalers and Retailers*

In *Cooper v. Texas Alcoholic Beverage Commission*, the Fifth Circuit expressly declined to follow *Southern Wine* and held that the Twenty-first Amendment does not authorize durational-residency requirements for wholesalers and retailers.<sup>95</sup> There, plaintiffs could not purchase a nightclub in Texas without endangering the club’s alcohol permit because they were out-of-state residents.<sup>96</sup> The Texas Alcoholic Beverage Code (the “Code”) gives the Texas Alcoholic Beverage Commission (the “Commission”) power to refuse an alcohol permit “to any applicant who has not been a *citizen of Texas for at least one year* before filing the application.”<sup>97</sup> The Texas Package Stores Association (“TPSA”) intervened as defendants.<sup>98</sup>

TPSA relied on *Southern Wine* and argued that the durational-residency requirement was constitutional because “[a]ll that the Commerce Clause requires . . . is that a [S]tate treat liquor produced out-of-state the same as liquor produced in-state.”<sup>99</sup> TPSA, like the Eighth Circuit in *Southern Wine*, drew this conclusion from the test set forth in *Granholm*: “State policies are protected under the Twenty-first Amendment when they treat liquor produced out of state

92. *S. Wine*, 731 F.3d at 811.

93. *Id.* Further, the supervisor noted, “wholesalers have ‘little impact upon’ the ‘direct sale’ of alcohol to minors.” *Id.*

94. *Id.* at 811–12. The existence of a nonresident wholesaler operating in Missouri would seem to undercut Missouri’s rationale for imposing the durational-residency requirement. Yet, the Eighth Circuit determined that “[e]xceptions like grandfather clauses do not, in and of themselves, demonstrate the invalidity of rules from which they are carved.” *Id.* at 812.

95. 820 F.3d 730, 743 (5th Cir. 2016).

96. *Id.* at 734.

97. *Id.* (emphasis added).

98. *Id.* at 735. TPSA moved for relief from a permanent injunction entered more than twenty years ago that prevented the Commission from enforcing the Code’s residency requirement. *Id.* at 730. The question before this court was whether it should continue the injunction in light of *Granholm*. *Id.* at 740.

99. *Id.* at 743.

the same as its domestic equivalent.”<sup>100</sup> This conclusion works perfectly for TPSA. Here, it was the *owners* of a nightclub seeking a license.<sup>101</sup> The statute does not regulate alcohol as an article of commerce. As a result, it automatically treats out-of-state and in-state alcohol the same because it all has to pass through Texas’ alcohol distribution system before reaching the consumer.

The Fifth Circuit did not find TPSA’s interpretation persuasive and expressly declined to follow *Southern Wine*.<sup>102</sup> It added an important modifier to the TPSA’s assertion that “[a]ll . . . the Commerce Clause requires . . . is that a [S]tate treat liquor produced out-of-state the same as liquor produced in-state.”<sup>103</sup> The Fifth Circuit held that all the Commerce Clause requires for a *state regulation of the producer tier* is that a State treat alcohol produced out-of-state the same as alcohol produced in-state.<sup>104</sup> Unlike the producer tier, “state regulations of the retailer and wholesaler tiers are not immune from Commerce Clause scrutiny just because they do not discriminate against out-of-state liquor.”<sup>105</sup> The court found that the Twenty-first Amendment does not allow States to impose a durational-residency requirement on the *owners* of alcohol retailers and wholesalers because a durational-residency requirement is not an “inherent” aspect of the three-tier system.<sup>106</sup>

#### D. Defining the States’ Power Under the Three-Tier System

The Eighth Circuit provided no limitations on a State’s power to distinguish between in-state and out-of-state citizens under the three-tier system.<sup>107</sup> Not only can Missouri require wholesalers to be in state, it can define the degree of “in-state” presence.<sup>108</sup> However, the Fifth Circuit did provide a limitation: the distinction has to be an “inherent aspect” of the three-tier system in order for the Twenty-first Amendment to authorize it.<sup>109</sup> In *Cooper*, it held that durational-residency requirements *are not* an “inherent aspect.”<sup>110</sup> But in *Wine Country Gift*

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100. *Granholtm v. Heald*, 544 U.S. 460, 488–89 (2005); *Cooper*, 820 F.3d at 743.

101. *See Cooper*, 820 F.3d at 734, 743.

102. *Id.* at 743.

103. *Id.*

104. *Id.*

105. *Id.*

106. *Cooper*, 820 F.3d at 743 (“Distinctions between in-state and out-of-state retailers and wholesalers are permissible only if they are an inherent aspect of the three-tier system.”).

107. The Eighth Circuit believed there were no “inherent” or “integral” aspects of the three-tier system. *See S. Wine & Spirits of Am., Inc. v. Div. of Alcohol & Tobacco Control*, 731 F.3d 799, 810 (8th Cir. 2013). Also, the Second Circuit provides no limitations. Any challenge to the three-tier system is a “frontal attack on the constitutionality of the three-tier system itself.” *Arnold’s Wines, Inc. v. Boyle*, 571 F.3d 185, 190 (2d Cir. 2009).

108. *S. Wine*, 731 F.3d at 810.

109. *Cooper*, 820 F.3d at 743.

110. *Id.*

*Baskets.com v. Steen*, the Fifth Circuit held that physical-presence requirements for wholesalers and retailers are an “inherent aspect.”<sup>111</sup>

### 1. Fifth Circuit: The Twenty-First Amendment Authorizes Physical-Presence Requirements for Retailers

The purpose of this Comment is to analyze whether the Twenty-first Amendment saves durational-residency requirements from Commerce Clause scrutiny. However, the reasons why the Fifth Circuit upheld a physical-presence requirement help draw some boundaries around the States’ power under the three-tier system.

In *Wine Country*, the Fifth Circuit was presented with a challenge to a state statute, which “allow[s] in-state retailers to deliver alcoholic beverages to their customers within designated local areas, but forbid[s] out-of-state retailers from delivering or shipping alcoholic beverages to customers anywhere in Texas.”<sup>112</sup> Thus, an out-of-state retailer needs an in-state operation to make local deliveries. The reason the Fifth Circuit upheld the statute was because the “physical location of businesses” is an inherent aspect of the three-tier system.<sup>113</sup> The “legal residence of owners,” however, is *not* an inherent aspect.<sup>114</sup> This distinction is important because it allows the owner of an alcohol retail chain to operate in several states.

The court noted that this statute did not discriminate against out-of-state retailers.<sup>115</sup> Assuming that the statute still had an inadvertent or incidental impact on interstate commerce, the court should have applied a *Pike* balancing test. Thus, the Twenty-first Amendment saved this statute from a *Pike* balancing test.

## III. WHY THE TWENTY-FIRST AMENDMENT SHOULD NOT SAVE DURATIONAL-RESIDENCY REQUIREMENTS FROM COMMERCE CLAUSE SCRUTINY

### A. Preventing the Practical Effect of the Eighth Circuit’s Holding

In *Granholm*, the Supreme Court expressed concern over States enacting laws that burden out-of-state citizens.<sup>116</sup> It recognized that “States should not be

111. 612 F.3d 809, 821 (5th Cir. 2010).

112. *Id.* at 812.

113. *Id.* at 821.

114. *Id.*

115. *Id.* at 820. “*Granholm* prohibited discrimination against out-of-state products or producers. Texas has not tripped over that bar by allowing in-state *retailer* deliveries. Yet it also has not discriminated among retailers.” *Id.* The remedy sought was allowing in-state retailers to ship anywhere in Texas because local retailers can deliver within their counties. *Id.* This would give out-of-state retailers “dramatically greater rights than Texas ones.” *Id.*

116. *Granholm v. Heald*, 544 U.S. 460, 472 (2005). (“States may not enact laws that burden out-of-state producers or shippers simply to give a competitive advantage to in-state businesses.”).

compelled to negotiate with each other regarding favored or disfavored status for their own citizens.”<sup>117</sup> That is why we have a rule prohibiting improper state discrimination against interstate commerce—it is “essential to the foundations of the Union.”<sup>118</sup> It was a central concern of the Framers because “economic Balkanization . . . had plagued relations among the Colonies and later among the States under the Articles of Confederation.”<sup>119</sup> The nondiscrimination principle of the Commerce Clause prevents rivalries among the States and the “proliferation of trade zones.”<sup>120</sup> Other Supreme Court cases examining state alcohol regulations have expressed this concern:

[T]he practical effect of the statute must be evaluated not only by considering the consequences of the statute itself, but also by considering how the challenged statute may interact with the legitimate regulatory regimes of other States and what effect would arise if not one, but many or every, State adopted similar legislation.<sup>121</sup>

The practical effect of allowing Missouri to require all officers and directors of a wholesale company to be Missouri residents for at least three years is that it allows other States to pass similar laws. Hypothetically, if every State passed similar laws, alcohol wholesalers could never gain a license to operate in more than one state.

Unfortunately, the Supreme Court missed an opportunity to prevent this result from happening in the future. After the Fifth Circuit held that the Twenty-first Amendment does not authorize durational-residency requirements, TPSA filed a petition for writ of certiorari with the Supreme Court.<sup>122</sup> On November 28, 2016, the Supreme Court denied the petition.<sup>123</sup>

Future courts should follow the Fifth Circuit and hold that the Twenty-first Amendment does not authorize durational-residency requirements for wholesalers and retailers. As the Court of Appeals for the Fifth Circuit recognized, the Twenty-first Amendment should not save laws that directly regulate the *owners* of alcohol retailer and wholesaler companies<sup>124</sup> simply because the laws treat in-state and out-of-state *alcohol* the same. Durational-

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117. *Id.*

118. *Id.*

119. *Id.* (quoting *Hughes v. Oklahoma*, 441 U.S. 322, 325–26 (1979)).

120. *Id.*

121. *Healy v. Beer Inst., Inc.*, 491 U.S. 324, 336 (1989).

122. *Texas Package Stores Assoc., Inc. v. Fine Wine and Spirits of North Texas, LLC*, SCOTUSBLOG, <http://www.scotusblog.com/case-files/cases/texas-package-stores-assoc-inc-v-fine-wine-and-spirits-of-north-texas-llc/> [<https://perma.cc/T8BQ-MCT8>].

123. *Tex. Package Stores Ass’n, Inc. v. Fine Wine & Spirits of N. Tex., LLC*, 820 F.3d 730 (5th Cir. 2016), *cert. denied*, 85 U.S.L.W. 3255 (U.S. Nov. 28, 2016) (No. 16-242); *see also* SCOTUSBLOG, *supra* note 122.

124. For the remainder of this Comment, when “citizens” is used it refers to the owners of alcohol retailer and wholesaler companies.

residency requirements should not be able to evade Commerce Clause scrutiny so easily. The Fifth Circuit's ruling was correct because it distinguished between products and citizens.<sup>125</sup>

The Missouri statute in *Southern Wine* should be, at a minimum, subjected to strict scrutiny because the Twenty-first Amendment intended to provide a shield only for state laws regulating alcohol products, not citizens. And, even if it did intend to cover citizens, the Eighth Circuit's reasoning for why the nondiscrimination principle does not apply takes the *Granholm* reasoning one step too far.

### 1. The Twenty-First Amendment Only Gives States the Power to Regulate Products, Not Citizens

The Twenty-first Amendment only gives States the power to regulate the "transportation or importation" of "intoxicating liquors"<sup>126</sup> because the Amendment only intended to give "dry" States the power to be dry. The Commerce Clause prevented States from subjecting out-of-state alcohol to the same laws as in-state alcohol. So a "dry" State could not truly be "dry" because alcohol crossing state lines had interstate immunity. As a result, Congress proposed to remove the interstate "immunity" from alcohol products, not citizens involved in the alcohol market.

#### a. Legislative Intent

Before Prohibition, the States' "police powers" allowed them to ban the production of domestic alcohol.<sup>127</sup> But a State that wished to be "dry" had no power to prevent liquor from entering its borders because the dormant Commerce Clause prevented the States from improperly burdening interstate commerce.<sup>128</sup> So in 1890, Congress passed the Wilson Act, which empowered States to regulate imported liquor "to the same extent and in the same manner as though such liquids or liquors had been produced in such State or Territory."<sup>129</sup> It did not allow States to discriminate against out-of-state liquor.<sup>130</sup> However,

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125. "The Twenty-first Amendment does not, however, authorize states to impose a durational-residency requirement on the *owners* of alcoholic beverage retailers and wholesalers." *Cooper v. Tex. Alcoholic Beverage Comm'n*, 820 F.3d 730, 743 (5th Cir. 2016).

126. U.S. Const. amend. XXI, § 2.

127. *See* *Mugler v. Kansas*, 123 U.S. 623, 671 (1887) ("The state [has the] authority to prohibit the manufacture and sale of intoxicating liquors . . .").

128. Ethan P. Davis, *Liquor Laws and Constitutional Conventions: A Legal History of the Twenty-first Amendment* 7 (Apr. 1, 2008) (unpublished Yale Law School paper) (available at [http://digitalcommons.law.yale.edu/cgi/viewcontent.cgi?article=1065&context=student\\_papers](http://digitalcommons.law.yale.edu/cgi/viewcontent.cgi?article=1065&context=student_papers) [<https://perma.cc/SUA7-PAD8>]) ("Because of the dormant Commerce Clause . . . dry states were powerless to erect legal barriers to the importation of alcohol from out-of-state.").

129. Wilson Act, 26 Stat. 313, 27 U.S.C. § 121 (1890); *see also* *Granholm v. Heald*, 544 U.S. 460, 478 (2005).

130. *Granholm*, 544 U.S. at 478.

the Supreme Court gave the Wilson Act a restricted construction and held that the Act authorized States to regulate only the resale of imported liquor.<sup>131</sup> Thus, States had no power to regulate alcohol that entered its border in its “original package.”<sup>132</sup> This loophole prevented States from imposing their laws on alcohol products involved in interstate commerce.

In order to close this loophole, Congress passed the Webb-Kenyon Act in 1913. The Act prohibited “[t]he shipment or transportation” of alcohol into a state that 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 . . . .”<sup>133</sup> One of the law’s principal sponsors, Senator William S. Kenyon, said that the bill’s “only purpose” was “to remove the impediment existing as to the States in the exercise of their police powers regarding the traffic or control of intoxicating liquors within their borders.”<sup>134</sup> Like the Wilson Act, it did not allow discrimination against articles of interstate commerce.<sup>135</sup> Rather, it simply removed “all immunities of *liquor* in interstate commerce.”<sup>136</sup> Thus, a “dry” State could prevent alcohol from entering its borders as long as it banned the manufacture and sale of alcohol within its borders.

At the time Congress was discussing proposals to repeal the Eighteenth Amendment, States that wished to be “dry” worried that the Webb-Kenyon Act

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131. *See Rhodes v. Iowa*, 170 U.S. 412, 423 (1898) (“[T]he provisions of the act were intended by congress to cause the legislative authority of the respective states to attach to intoxicating liquors coming into the states by an interstate shipment, only after the consummation of the shipment, but before the sale of the merchandise; that is, that the one receiving merchandise of the character named should, while retaining the full right to use the same, no longer enjoy the right to sell free from the restrictions as to sale created by state legislation . . . .”).

In other words, the court held that the interstate-commerce clause—that is, the power of Congress to regulate interstate commerce—attached to that commodity not only before it entered the State but after it entered the State . . . until the commodity or intoxicating liquor was in fact delivered to the consignee.

76 CONG. REC. 4140 (1933) (statement of Sen. Blaine).

132. *See Rhodes*, 170 U.S. at 423–24.

133. Webb-Kenyon Act, 49 Stat. 877, 27 U.S.C. § 122 (1935) (originally enacted as Act of Mar. 1, 1913, ch. 90, § 1, 37 Stat. 699).

134. 49 CONG. REC. 707 (1912) (statement of Sen. Kenyon).

135. The Webb-Kenyon Act did not repeal the Wilson Act, which expressly proscribed discrimination. If Congress, through the Webb-Kenyon Act, wanted to authorize States to discriminate against out-of-state goods, then it would have repealed the Wilson Act.

136. 76 CONG. REC. 4140 (1933) (statement of Sen. Wagner) (emphasis added).

Mr. WAGNER: I do not want to enter into a controversy, because it really is not very important, but I do not think the Senator meant to say that by this act Congress delegated to the States the power to regulate interstate commerce; Congress itself regulated interstate commerce to the point of removing all immunities of liquor in interstate commerce.

Mr. BLAINE: I thank the Senator. I think he has given the correct statement of the doctrine.  
76 CONG. REC. 4140 (1933) (statement of Sen. Wagner) (statement of Sen. Blaine).

would not provide sufficient protection.<sup>137</sup> There was nothing to prevent the Supreme Court from narrowly interpreting this Act to make the States' power meaningless. Senator John J. Blaine represented the Joint Resolution Committee when proposing the Twenty-first Amendment to Congress.<sup>138</sup> He recognized that the Webb-Kenyon Act was sustained by a divided court and wanted "to assure the so-called dry States against the importation of intoxicating liquor into those States."<sup>139</sup> To provide this assurance, Congress intended to write the Webb-Kenyon Act into the Constitution.<sup>140</sup> Its vehicle was Section 2 of the Twenty-first Amendment.

When our Government was organized and the Constitution of the United States adopted, the States surrendered control over and regulation of interstate commerce. [Section 2] is restoring to the States, in effect, *the right to regulate commerce respecting a single commodity—namely, intoxicating liquor*. In other words, the State is not surrendering any power that it possesses, but rather, by reason of this provision, in effect acquires powers that it has not at this time.<sup>141</sup>

Thus, Congress only intended to give States the power "to regulate commerce respecting a single commodity."<sup>142</sup> Section 2 "restored to the States the power they had under the Wilson and Webb-Kenyon Acts,"<sup>143</sup> namely the power to prevent the importation of alcohol, not citizens of other states. Notably, because the Acts did not authorize discrimination, the power to prevent imports was only effective if the State also banned the manufacture and sale of alcohol within its borders.

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137. The constitutionality of the Act was in doubt. In fact, President Taft vetoed it because he believed it was an unlawful delegation of Congress' Commerce Clause powers. Davis, *supra* note 128, at 12. However, Congress overrode the veto. *Id.* The Act survived a constitutional challenge in *Clark Distilling Co. v. Western Maryland Railway Co.* 242 U.S. 311, 330, 332 (1917). But it was only a 2-2 vote. *Id.* at 332.

138. See 76 CONG. REC. 4141 (1933) (statement of Sen. Blaine) ("Now, Mr. President, I think I have set forth . . . the view of the committee as expressed in this joint resolution."); see also S.J. Res. 211, 72nd Cong. (1932).

139. 76 CONG. REC. 4141 (1933) (statement of Sen. Blaine).

140. *Id.*

The committee felt that since the Congress had acted and had definitely legislated upon this question, while that legislation had been sustained by the Supreme Court, yet it was sustained by a divided court, and that we could well afford to guarantee to the so-call dry States the protection designed by section 2.

*Id.*; see also Davis, *supra* note 128, at 4, 12 (confirming that the Twenty-first Amendment was intended to constitutionalize the Webb-Kenyon Act).

141. 76 CONG. REC. 4141 (1933) (statement of Sen. Blaine) (emphasis added).

142. *Id.*

143. *Granholt v. Heald*, 544 U.S. 460, 484 (2005).

b. Textual Analysis

Congress' intent to constitutionalize the Webb-Kenyon Act is further evidenced by the language of Section 2, which resembles that of the Webb-Kenyon Act. The Webb-Kenyon Act regulated the "shipment or transportation" of alcohol "to be received, possessed, sold, or in any manner used . . . in violation of any law of such State."<sup>144</sup> Section 2 regulates the "transportation or importation into any State . . . for delivery or use therein of intoxicating liquors, in violation of the laws thereof."<sup>145</sup> This resemblance is evidence of "the framers' clear intention of constitutionalizing the Commerce Clause framework established under those statutes."<sup>146</sup>

The language "shipment or transportation" and "transportation or importation" indicates that Congress wanted to give States the power to prevent alcohol *products* from entering their borders. This intention is further shown by Congress' desire to protect "dry" States.<sup>147</sup> However, once a State opens its alcohol market, it may not open it only to in-state interests.<sup>148</sup>

If anything, Section 2 reaches more narrowly than the Webb-Kenyon Act. The Webb-Kenyon Act refers to alcohol that is "to be received, possessed, sold, or in any manner used."<sup>149</sup> Section 2 only refers to "delivery or use."<sup>150</sup> And the Webb-Kenyon Act was not even a grant of interstate commerce power to the States.<sup>151</sup> It only removed the interstate immunity from alcohol.<sup>152</sup> If Congress only intended to remove the interstate character from alcohol, and nothing else, then it does not follow that Congress intended to give States power to impose durational-residency requirements on alcohol wholesalers and retailers.

144. Webb-Kenyon Act, 49 Stat. 877, 27 U.S.C. § 122 (1935) (originally enacted as Act of Mar. 1, 1913, ch. 90, § 1, 37 Stat. 699).

145. U.S. CONST. amend XXI, § 2.

146. *Granholm*, 544 U.S. at 484 (quoting *Craig v. Boren*, 429 U.S. 190, 206 (1976)) (internal quotation marks omitted).

147. See 76 CONG. REC. 4170 (1933) (statement of Sen. Borah) ("[A]s I understand, this is the question of striking out section 2, which provides for the protection of the so-called dry States."); 76 CONG. REC. 4171 (1933) (statement of Sen. Wagner) ("[I]f the dry States want additional assurance that they will be protected I shall have no objection."); 76 CONG. REC. 4518 (1933) (statement of Rep. Robinson) ("Section 2 attempts to protect dry States."); 76 CONG. REC. 4519 (1933) (statement of Rep. Garber) ("Section 2 prohibits the transportation or importation of intoxicating liquors for delivery or use into any of the several States where the laws of the State prohibit such. This section, it is claimed, will protect dry States."); 76 CONG. REC. 4526 (1933) (statement of Rep. Tierney) ("[Section 2] will aid and protect the so-called dry States in permitting them to exclude, if their citizens so wish, all liquor traffic in their domains.").

148. *Peoples Super Liquor Stores, Inc. v. Jenkins*, 432 F. Supp. 2d 200, 221 (D. Mass. 2006) ("*Granholm* cannot be held to sanction protectionist policies at any of the tiers.").

149. 27 U.S.C. § 122.

150. U.S. CONST. amend XXI, § 2.

151. See *Granholm*, 544 U.S. at 481–82.

152. *Id.* at 482.

c. The Indirect Effect of Regulating Products

Naturally, the Twenty-first Amendment gives the States power to indirectly regulate citizens by subjecting their products to state laws. In *Granholm*, if New York and Michigan required *all* alcohol to pass through the three-tier system, then the statutes would indirectly regulate producers by requiring their products to pass through the three-tier system. The Twenty-first Amendment authorizes this.<sup>153</sup>

Unlike the producer tier, the wholesaler and retailer tiers do not produce alcohol. However, they are responsible for the “transportation or importation” of alcohol into a state for the “delivery or use therein.”<sup>154</sup> If a State requires all retail sales of alcohol to be over-the-counter, for example, then the indirect effect is that the retailer needs a physical location in the state. That is why the “physical locations of businesses” is an inherent aspect of the three-tier system.<sup>155</sup> It is an extension of the States’ power to regulate products. Thus, “[w]hen analyzing whether a State’s alcoholic beverage regulation discriminates under the dormant Commerce Clause, a beginning premise is that wholesalers may be required to be within the State.”<sup>156</sup> Imposing durational-residency requirements, however, is not a natural extension of the States’ power to directly regulate alcohol products.

2. The Eighth Circuit Misapplied the Reasoning in *Granholm* in Two Key Ways

Even if it is conceded that the Twenty-first Amendment gave the States power to directly regulate citizens, the Eighth Circuit took *Granholm* one step too far when it gave Missouri’s durational-residency requirement a “protected” status.<sup>157</sup> The statute achieved this “protected” status because it met the Eighth Circuit’s two-pronged test.

a. The Statute Did Not Discriminate Against Out-of-State Alcohol Products

Missouri’s statute directly regulated the officers and directors of alcohol wholesaler companies. Yet, the Eighth Circuit gave the statute a “protected” status because it gave equal treatment to out-of-state products and producers.<sup>158</sup> A statute that only targets the officers and directors of a wholesale company and

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153. For a discussion on the impact the three-tier system has on out-of-state producers, see *supra* note 56 and accompanying text.

154. U.S. CONST. amend XXI, § 2.

155. See *Wine Country Gift Baskets.com v. Steen*, 612 F.3d 809, 821 (5th Cir. 2010).

156. *Id.* at 820.

157. *S. Wine & Spirits of Am., Inc. v. Div. of Alcohol & Tobacco Control*, 731 F.3d 799, 809, 810 (8th Cir. 2013).

158. *Id.*

does not even mention products and producers, is not going to discriminate against out-of-state products and producers. The Eighth Circuit took a protection that *Granholm* established for the producer tier,<sup>159</sup> and then applied it to the wholesaler tier without providing a rationale. This jump cannot be made because the statutes in *Granholm* regulated producers, who *produce* the product.<sup>160</sup> Hence, the holding: “State policies are protected under the Twenty-first Amendment when they treat *liquor* produced out of state the same as its domestic equivalent.”<sup>161</sup> The Missouri statute in *Southern Wine* regulated *citizens*. So the holding, “state policies are protected . . . when they treat *liquor* produced out of state the same as its domestic equivalent,”<sup>162</sup> does not logically follow.

The Fifth Circuit recognized the Eighth Circuit’s error when it held that “state regulations of the retailer and wholesaler tiers are not immune from Commerce Clause scrutiny just because they do not discriminate against out-of-state liquor.”<sup>163</sup> The Eighth Circuit even interpreted *Granholm* as drawing “a bright line between the producer tier and the rest of the system.”<sup>164</sup> But it still took a protection for the producer tier and applied it to the wholesaler tier. Further, *Granholm* never examined state alcohol regulations at the wholesaler or retailer tiers. Thus, if it wished to establish this precedent, it would have stated that this protection applies to the wholesaler and retailer tier.

#### b. The Statute Hid Behind Missouri’s Distribution System

The Eighth Circuit recognized that the nondiscrimination principle applies to products and producers, but it did not apply the nondiscrimination principle to wholesalers. It should have examined whether the statute discriminated against out-of-state wholesalers. The Eighth Circuit likely chose not to apply an important Commerce Clause principle because of the citation right after the Supreme Court declared that the three-tier system is “unquestionably legitimate.”<sup>165</sup> It cited to one of its previous cases, *North Dakota v. United States*, and included a quote from Justice Scalia’s concurrence: “The Twenty-

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159. *Id.* *Granholm* held that “[s]tate policies are protected under the Twenty-first Amendment when they treat liquor produced out of state the same as its domestic equivalent.” *Granholm v. Heald*, 544 U.S. 460, 489 (2005).

160. *Id.* at 469. The statutes at issue in *Granholm* required out-of-state wine to pass through the state’s three-tier system before reaching consumers. *Id.* at 468. The effect of this was that out-of-state wineries could only sell their products directly to consumers if they became an in-state winery. *Id.* at 469.

161. *Id.* at 489.

162. *See id.*

163. *Cooper v. Tex. Alcoholic Beverage Comm’n*, 820 F.3d 730, 43 (5th Cir. 2016).

164. *S. Wine*, 731 F.3d at 810.

165. *Granholm*, 544 U.S. at 489 (quoting *North Dakota v. United States*, 495 U.S. 423, 432 (1982) (Scalia, J., concurring)).

first Amendment . . . empowers North Dakota to require that all liquor sold for use in the State be purchased from a licensed in-state wholesaler.”<sup>166</sup> Based on this, the Eighth Circuit asserted: “If it is beyond question that States may require wholesalers to be ‘in-state’ without running afoul of the Commerce Clause, then we think States have flexibility to define the requisite degree of ‘in-state’ presence . . . .”<sup>167</sup> However, *North Dakota v. United States* was a plurality opinion.<sup>168</sup> And the quote cited by the Supreme Court was from a concurring opinion in which no other Justice joined. This is too weak of a foundation on which to rest such a strong assertion as the Eighth Circuit advanced.

Further, the Eighth Circuit believes that there are no “inherent” or “integral” parts of the three-tier system, and any regulation defining the structure of the system is saved.<sup>169</sup> But there has to be some limitation on these regulations. The States have some room to burden out-of-state interests.<sup>170</sup> But it is not an unlimited power. For cautionary purposes, the Eighth Circuit held that an in-state wholesaler is an “inherent” part of the three-tier system.<sup>171</sup> However, the Eighth Circuit never argued that an in-state wholesaler *who has been a resident for at least three years* is an “inherent” aspect.

The Eighth Circuit took a protection that *Granholm* created for the producer tier and then applied it to the wholesaler tier. It then decided not to apply the nondiscrimination principle. The Eighth Circuit should not be able to pick and choose.

#### B. *Subjecting Missouri’s Statute to Strict Scrutiny*

As argued in Section III.A, the Twenty-first Amendment should not save Missouri’s durational-residency requirement. Thus, because the statute, at a minimum, discriminates in its effect, the next step is to determine whether the statute advances “a legitimate local purpose that cannot be adequately served by reasonable nondiscriminatory alternatives.”<sup>172</sup> Like New York and Michigan in *Granholm*, the burden is on Missouri to make the “clearest showing” that the discrimination is necessary by offering “concrete evidence.”<sup>173</sup> Missouri would argue that:

[A] wholesaler governed . . . by Missouri residents is more apt to be socially responsible and to promote temperance, because the officers, directors, and owners are residents of the community and thus subject to negative

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166. *Id.* (quoting *North Dakota v. United States*, 495 U.S. 423, 432 (1982) (Scalia, J., concurring)).

167. *S. Wine*, 731 F.3d at 810.

168. *See North Dakota*, 495 U.S. 423.

169. *See S. Wine*, 731 F.3d at 810.

170. *See* discussion of *Wine Country*, *supra* Section II.D.1.

171. *S. Wine*, 731 F.3d at 810.

172. *New Energy Co. of Ind. v. Limbach*, 486 U.S. 269, 278 (1988).

173. *Granholm v. Heald*, 544 U.S. 460, 490 (2005).

externalities—drunk driving, domestic abuse, underage drinking—that liquor distribution may produce. Missouri residents . . . are more likely to respond to concerns of the community, as expressed by their friends and neighbors whom they encounter day-to-day . . . . [I]n-state residency facilitates law enforcement against wholesalers, because it is easier to pursue in-state owners, directors, and officers than to enforce against their out-of-state counterparts.<sup>174</sup>

However, the deputy state supervisor for the Division, who testified *on behalf of* the Division, said that “wholesalers have little impact upon the direct sale of alcohol to minors, and that he could not think of any relationship between the residency requirement and the safety of Missouri citizens.”<sup>175</sup> But even if Missouri can provide “concrete evidence” that the durational-residency requirement actually serves the above purposes, it still would not survive strict scrutiny. *Granholm* held that “rationales, such as facilitating orderly market conditions, protecting public health and safety, and ensuring regulatory accountability” can be achieved through non-discriminatory alternatives.<sup>176</sup> Being subject to the negative externalities that liquor distribution may produce is not necessary for someone to be socially responsible. There are less discriminatory ways to require wholesalers to be socially responsible. Additionally, in this modern era, “conducting an interstate investigation would seem just as easy as conducting an intrastate one,”<sup>177</sup> and “improvements in technology have eased the burden of monitoring out-of-state [citizens].”<sup>178</sup> Thus, the legitimate local purposes proposed by Missouri can be achieved through less discriminatory alternatives.

### C. *Privileges and Immunities Clause*

The Privileges and Immunities Clause of the Fourteenth Amendment provides an alternative basis for challenging durational-residency requirements.

All persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the State wherein they reside. No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States . . . .<sup>179</sup>

One privilege and immunity for U.S. citizens is the right to travel. The Supreme Court has defined this as “the right of the newly arrived citizen to the same privileges and immunities enjoyed by other citizens of the same State.”<sup>180</sup> In

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174. *S. Wine*, 731 F.3d at 811.

175. *Id.* (internal quotation marks omitted).

176. *Granholm*, 544 U.S. at 492.

177. *Glazer’s Wholesale Drug Co., Inc., v. Kansas*, 145 F. Supp. 2d 1234, 1243 (D. Kan. 2001).

178. *Granholm*, 544 U.S. at 492.

179. U.S. CONST. amend. XIV, § 1.

180. *Saenz v. Roe*, 526 U.S. 489, 502 (1999) (“Permissible justifications for discrimination between residents and nonresidents are simply inapplicable to a nonresident’s exercise of the right to move into another State and become a resident of that State.”).

other words, the citizen of State A, who elects to become a permanent resident of State B, has the right to be treated like other citizens of State B. The citizen of State A should not have to wait three years to be treated like other citizens of State B. “Neither mere rationality nor some intermediate standard of review should be used to judge the constitutionality of a state rule that discriminates against some of its citizens because they have been domiciled in the State for less than a year.”<sup>181</sup> Thus, the Privileges and Immunities Clause is an alternative path that alcohol beverage wholesalers and retailers can use to subject durational-residency requirements to strict scrutiny.

#### CONCLUSION

Justice Stevens’ dissent in *Granholm* recognized that today, alcohol is viewed as “an ordinary article of commerce, subject to substantially the same market and legal controls as other consumer products.”<sup>182</sup> But back when the Twenty-first was passed, alcohol was known as “demon rum” and millions of Americans condemned its use.<sup>183</sup> The circumstances that justified the passage of the Twenty-first Amendment are not as evident today. There is no longer a legitimate state interest in the alcohol market. Even if there was, durational-residency requirements do not advance it. This Comment does not propose that the Twenty-first Amendment serves no purpose in our day and age. Further, it does not propose a rewriting of the Amendment to expressly narrow the States’ power. Rather, this Comment urges courts to follow the holding of the Fifth Circuit when analyzing the constitutionality of durational-residency requirements for alcohol wholesalers and retailers. From *Young’s Market Co.*<sup>184</sup> to *Granholm*, the States’ reach under the Twenty-first Amendment has been narrowed. It is time for future courts to finish the job and subject durational-residency requirements to Commerce Clause scrutiny.

KEEGAN J. SHEA\*

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181. *Id.* at 504.

182. *Granholm*, 544 U.S. at 494 (Stevens, J., dissenting).

183. *Id.* at 496.

184. *See supra* note 8 and accompanying text.

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