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Hawaiian Ripples

by Patricia D. White

Bacchus Imports, Ltd. and Eagle Distributors, Inc.

v.

**George Freitas, Director of Taxation of the
State of Hawaii**

(Docket No. 82-1565)

Argued January 11, 1984

ISSUE

The Commerce Clause of the United States Constitution has long been interpreted to prohibit a state from imposing a tax that discriminates against interstate commerce. Simply put, the principal issue in this case is whether that prohibition only applies to taxes which both discriminate on their face against interstate commerce and have a demonstrable discriminatory effect. If the Court holds that a tax which only discriminates on its face is unconstitutional, then it must address a further issue. That is: Is the Twenty-First Amendment, which reserves to the states the power to regulate liquor within their respective borders, sufficient in scope to overcome the Commerce Clause?

FACTS

Since 1939, Hawaii has imposed an excise tax on liquor sold at wholesale within its borders. The tax is based on the actual wholesale price and is collected from the wholesaler. The rate of tax has increased over the years from 6% to the current 20%. Beginning in 1960, Hawaii's legislature has enacted specific exemptions from the tax for certain locally produced liquor products. From 1960 to 1965, and again from 1971 to 1981, okolehao (a brandy made from the root of the ti plant—a shrub indigenous to Hawaii) was exempt from the tax. In addition, wine made from fruit grown in Hawaii (pineapple as it turns out) was exempted from 1976 to 1981. In 1981, while this case was pending before the Hawaii Supreme Court, an exemption was granted to rum manufactured in Hawaii. It is scheduled to run through June, 1986.

Bacchus Imports, Ltd. and Eagle Distributors, Inc. import alcoholic beverages into Hawaii and sell them at

wholesale. Both paid their 1979 liquor tax under protest and each brought suit in the Hawaii Tax Appeal Court seeking a refund on the ground that the tax paid violated the Equal Protection, Commerce and Import-Export Clauses of the Constitution. The two cases were consolidated, along with two similar suits brought by other liquor wholesalers. The Hawaii Tax Appeal Court upheld the tax. The case was appealed to the Hawaii Supreme Court. That court ruled that the tax was constitutional, and this appeal by Bacchus and Eagle followed.

BACKGROUND AND SIGNIFICANCE

Although the liquor wholesaler understandably do not emphasize the fact in their briefs, it appears that neither okolehao nor pineapple wine is manufactured outside of Hawaii. Thus, neither is imported into the state. Any discriminatory effect of the exemptions from the Hawaiian tax on wholesalers must therefore be felt by the wholesalers of other varieties of liquor. Hawaii argues that okolehao and pineapple wine do not compete with other sorts of alcoholic beverages and that their exemption from the tax is not in fact discriminatory. The wholesalers rely on the fact that the exemptions are discriminatory on their face (and would discriminate against any okolehao or pineapple wine that was imported) for their claim of unconstitutionality. If the Court holds that the Commerce Clause requires a showing of actual discriminatory effect to invalidate a state tax, it would suggest that states can tax to protect various local industries so long as the local product can be described with sufficient specificity to make it appear unique to the state. Such a result would seem to apply rather broadly across product classifications.

On the other hand, the Court could decide that the Commerce Clause is violated by a tax which is discriminatory on its face and still hold that the Hawaiian liquor tax is constitutional. The Twenty-First Amendment to the Constitution provides that "[t]he transportation or importation into any state . . . for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is . . . prohibited." If one of "the laws thereof" contravenes the Commerce Clause, is the Twenty-First Amendment broad enough to overcome that apparent unconstitutionality? Such an inquiry requires the Court to balance the state's interest in the exemptions against the Commerce Clause. If the court resolves this conflict in favor

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of Hawaii, the result would clearly be limited to state liquor taxes. The strength of its impact on the interstate flow of liquor could be slight or enormous depending entirely on the breadth of the Court's language.

ARGUMENTS

For Bacchus Imports, Ltd. and Eagle Distributors, Inc.

1. The principal purpose of the Commerce Clause is to keep states from protecting their own goods from interstate competition by discriminating against goods from other states. Accordingly, the Court has held that a state statute that discriminates on its face is invalid unless the state shows both that it has a legitimate purpose and that there is no nondiscriminatory method by which it might achieve that purpose.
2. The purpose of the Hawaii liquor tax was "to encourage and promote" local industry. This is not a legitimate purpose and the statute is therefore invalid.
3. Even if the purpose of the tax is found not to have been protectionist, Hawaii has not identified any legitimate objective that it does serve.
4. Bacchus and Eagle are not required to show that the tax, in its practical operation, discriminates against interstate commerce. The unlawful protectionist purpose is not mitigated by the fact that it applies equally to Hawaiian and non-Hawaiian taxpayers.
5. The tax violates the foreign Commerce Clause by treating foreign liquor differently from locally produced liquor.
6. The Import-Export Clause prohibits states from imposing a duty on imports. The Hawaii tax is an unconstitutional duty on imports.
7. The historical purpose of the Twenty-First Amendment was to provide a constitutional basis for dry states to remain dry. Although the amendment and the Commerce Clause must be considered in the light of one another, Hawaii has articulated no legitimate (nonprotectionist) state interest upon which it may rely.

For George Freitas, Director of Taxation of the State of Hawaii

1. The wholesalers have not borne the economic burden of the Hawaii tax because it is passed on to the liquor retailers. It would therefore be unjust to allow them to receive any refund of the tax.
2. The wholesalers have suffered no damages as a result of the exemptions from the tax. Without a showing of injury or damages they may not challenge the constitutionality of the Hawaii liquor tax. Their appeal should therefore be dismissed for lack of jurisdiction.
3. Even if the challenged exemptions are invalid, the Court should not invalidate the whole tax. Instead, it should sever the exemptions from the rest of the statute.

4. It would be inequitable to apply a decision in favor of the wholesalers retroactively. Moreover, the exemptions are valid under earlier court decisions interpreting the Twenty-First Amendment.
5. Exempting okolehao and pineapple wine from the liquor tax does not deny equal protection to anyone. The tax applies equally to all liquor wholesalers doing business in Hawaii.
6. A state tax is invalid under the Commerce Clause only if it has the actual effect of discriminating against interstate or foreign commerce. The exemptions in question here have no actual discriminatory effect. Okolehao and pineapple wine are produced solely in Hawaii and pose no competitive threat to other liquors consumed in Hawaii.
7. These exemptions do not violate the Import-Export Clause because they do not discriminate against foreign commerce.
8. The Twenty-First Amendment allows states to tax liquor so long as no competing federal interests based on other constitutional provisions outweigh the state's interest in taxation. Here the exemptions have had no impact on either interstate or foreign commerce and they were enacted to promote the legitimate state interest of promoting two struggling local industries.
9. The protectionist *per se* Commerce Clause rule relied on by the wholesalers does not apply to this case. The exemptions were not enacted to discriminate against foreign products—only to promote two local industries—and the exemptions had no actual discriminatory effect.

Additional Party

Rule 10.4 of the Rules of the Supreme Court of the United States provides that all parties to the proceeding in the lower courts are parties in the Supreme Court. Any party which does not file an appeal is called an "appellee" in the Supreme Court proceeding. Foremost McKesson, Inc. is a liquor wholesaler whose case was part of the consolidated suit in the Hawaii Supreme Court. It did not file a timely appeal in the United States Supreme Court and is thus known as an "appellee" in this case. It filed a brief in support of Bacchus Imports and Eagle Distributors.

AMICUS BRIEFS

For Bacchus, et al.

Distilled Spirits Council of the United States, Inc. and the Wine Institute.

For Hawaii

Multistate Tax Commission.