MERCATUS REPORTS

The Bush Administration Regulatory Record

By Susan E. Dudley

Every year, over 60 federal departments, agencies, and commissions employ a combined staff of over 240,000 full-time employees to write and enforce federal regulations. Combined, the agencies issue thousands of new rules annually and the on-budget costs for their regulatory operations in fiscal year 2004 will exceed $39 billion. The social costs of complying with those regulations are likely to be 30 or more times larger.

Recognizing the impact regulations have on our daily lives, every president since Richard Nixon has established regulatory oversight and review procedures within the Executive Office of the President. When he took office in 2000, President George W. Bush chose to operate under procedures established in 1993 by President Bill Clinton's Executive Order 12866. The Clinton order articulated a sound approach to regulatory development and, by leaving it in place, Bush made the point that the principles of good regulation are nonpartisan — they only need to be observed and enforced.

By many measures, the Bush administration has observed and enforced those principles. The Office of Information and Regulatory Affairs (OIRA), headed by John D. Graham, has reinvigorated the review process, sending back to the agencies more rules during the first year of the Bush administration than were returned during the entire eight years of the Clinton administration. Graham has also emphasized transparency in the review process, making available on OIRA's Web site the activities of the office (including meetings). He sends public letters to agencies explaining his reasons for returning draft rules, "prompt letters" to publicly encourage agency action, and "post-review letters" to describe remaining problems in some rules OIRA clears for publication.

This level of activity contrasts sharply with the previous administration, in which OIRA rarely challenged an agency initiative on any grounds. However, OIRA's paradigm seems to be that smarter regulators can devise solutions to perceived problems. The office emphasizes benefit-cost and cost-effectiveness analysis, and advancing public health. While this strategy holds the potential for making large improvements in regulatory effectiveness, there is little evidence that OIRA advocates for market solutions, property rights, individual choice and responsibility, or federalism.

A QUICK START

President Clinton's final months in office generated an unprecedented volume of new rules and regulations dictating how American businesses, citizens, and state and local governments must behave. Like Cinderella leaving the ball, many of the more than 7,000 presidential appointees at executive branch departments and agencies hurried to issue last-minute "midnight regulations" before they turned back into ordinary citizens. Using the number of *Federal Register* pages as a proxy, President Clinton's regulatory activity in the post-election quarter (November, December, and January) represented a 52.5 percent increase over the volume of regulation issued during the same three months of his previous seven years (1993–1999).

In a January 20, 2001 memorandum, White House Chief of Staff Andrew Card directed all federal agencies to withdraw regulations not yet published. The agencies were also instructed to postpone for 60 days the effective date of recently issued but not yet effective regulations in order to give new appointees time to review them before they undertook to enforce them.

After that initial rally, however, principle appeared to give way to politics, and the final disposition of many of the Clinton midnight regulations, including the Environmental Protection Agency's controversial arsenic standards, proved little different from the Clinton version. There are some notable exceptions, including the Forest Service's ban on all new roads in national forests, the EPA's Total Maximum Daily Load (TMDL) rule addressing water quality in lakes and streams, the Department of Interior's ban on snowmobiles in national parks, and the Occupational Safety and Health Administration's ergonomics rule.

Susan E. Dudley is the director of the Regulatory Studies Program at the Mercatus Center at George Mason University. She may be contacted by e-mail at sdudley@gmu.edu.

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MIDNIGHT REGULATIONS One prominent Clinton midnight regulation, the "roadless rule," would have imposed a blanket ban on roads in some national forests. While it is true that the incentives inherent in national forest policies encouraged intrusive logging roads and clearcutting that have damaged ecosystems, the proscription on roads failed to consider how to alter the underlying incentives or that temporary, low-impact roads in roadless areas may be needed for forest health or ecosystem restoration. The Bush administration withdrew the roadless rule and proposed in its place an alternative that allows state governors to petition the Forest Service to ban roads in national forests within their state. While this may appear to be a more federalist approach, as long as the underlying incentive structure remains unchanged and national taxpayers are asked to foot the bill for the roads, it is unlikely to solve the problems that plague national forests.

The water quality TMDL regulation would have given the EPA decision-making power over hundreds of thousands of river segments, lakes, and coastal zone regions, complicating and delaying decision-making about matters that are inherently local. The Bush administration has withdrawn the regulations in favor of flexible, state-oriented approaches to regulating pollution from non-point sources.

At the end of the Clinton administration, the National Park Service promulgated new rules to ban snowmobiles in Yellowstone National Park. The Bush administration reversed that decision in favor of limiting the number of snowmobiles entering Yellowstone to 1,100 per day and imposing other restrictions to limit their impact. Then the courts got involved. In December 2003, a D.C. district judge overturned the Bush regulation on the grounds that it did not follow proper administrative procedures. Two months later, a U.S. district court judge set that ruling aside, and in October 2004 he ruled that it was the Clinton ban that did not involve adequate public participation and failed to follow federal law, calling it "the product of a prejudged, political decision to ban snowmobiles from all the national parks." That latest ruling paves the way for what Interior Secretary Gale Norton calls a "common sense solution for snowmobile use that protects resources while also allowing appropriate access for enjoyment by the public."

KEVIN TUMA (5)

OSHA's midnight ergonomics standard would have straitjacketed employers with procedural requirements and a hierarchy of control measures that would have discouraged individual responsibility and hindered development of creative solutions to the complex problem of musculo-skeletal disorders. Using the Congressional Review Act for the first (and only) time, Congress voted to overturn OSHA's controversial ergonomics regulation in 2001. While the Bush administration may not deserve direct credit for its disapproval, Congress would not likely have taken that action if it had expected a veto from the president.

BETTER REGULATION Increased attention to sound regulatory principles is evident in several new and pending regulations:

EPA After consulting with OIRA, the EPA abandoned its proposal to regulate storm water runoff at construction sites (a rule the agency estimated would cost $4 billion per year) in favor of allowing local zoning controls to manage runoff problems. The EPA has also initiated efforts to rationalize its controversial New Source Review policies, which discouraged electric utilities from upgrading their plants lest they be regulated more stringently as a "new source." The agency has also revised water quality guidelines for the metal products and machinery industry and animal feedlots, thereby significantly reducing the estimated social costs of those rules.

Not all regulatory activities are held to the same standards of accountability, however. Regulations that claim to reduce fine particulate matter seem to get a free pass through OIRA. In 2002, Graham sent a prompt letter to the EPA, encouraging it to devote more research to the health effects of fine particles. Later that year, the EPA and OIRA jointly announced that regulating emissions from non-road diesel engines should be a top environmental priority. The EPA has taken advantage of Graham's enthusiasm for reducing particulate matter. Indeed, because the agency's health effect and benefit models yield huge benefits for reducing fine particles, even unrelated air quality regulations (such as the reduction of mercury from power plants) can claim large benefits from incidental reductions in particulates.

FDA Administrator Graham issued one of his first "prompt letters" to the Food and Drug Administration to encourage it to expedite labeling requirements for trans fats in foods. While the prompt letter did not acknowledge that the lack of consumer information on trans fats and their adverse health effects was due to federal prohibitions under health claims rules, the resulting final regulation was superior to the proposal, which would have forced food producers to mislabel trans fats as saturated fats on the belief that that was a more expedient way to inform consumers that they were "bad" fats. Perhaps more significant than the trans fat rule itself is the FDA's apparent openness to reconsidering its approach to regulating commercial speech. Studies suggest that the FDA's long practice of not letting food producers advertise the health benefits of their products has kept valuable information (such as the negative health effects of trans fats) from consumers. Indeed, in several court cases, the FDA's interpretation of its mandate to protect consumers from fraud has run afoul of the First Amendment right to free speech. Through two public notices, the FDA has sought comment on how it can best protect consumers from inaccurate or fraudulent information, without preventing food producers from providing truthful information.

Transportation After initially proposing to extend its regulations governing airline computer reservation systems, the Department of Transportation responded to public comment and allowed the outdated rules to sunset at the end of 2003.

Labor In contrast to President Clinton's Department of Labor, which focused its resources and political capital on one rule (ergonomics), the Bush Labor Department has been quietly pursuing a variety of regulatory strategies. OSHA has removed from its agenda of pending regulations several rules that have been languishing for a decade or more, and instead is focusing on cooperative efforts with companies and increased enforcement of existing rules. Over the objections of labor union officials, the Employment Standards Administration issued a rule requiring unions to disclose financial information to their members. The department successfully defended the rule against a lawsuit brought by the AFL-CIO in federal district court.

GUIDELINES AND REPORTS

During President Bush's term, OIRA has issued several guidelines to agencies for regulatory development and review. Issuing clear analytical guidelines, and holding agencies accountable for complying with them, is an important step toward regulatory reform. If followed and enforced, those guidelines could have a positive influence on regulatory policy.

The 2000 Information Quality Act required the Office of Management and Budget to create guidelines to "provide policy and procedural guidance to Federal agencies for ensuring and maximizing the quality, objectivity, and integrity of information (including statistical information) disseminated by Federal agencies." OIRA responded to that requirement with two sets of guidelines: one on scientific peer review (which is still in draft form) that it developed with the President's Office of Science and Technology Policy, and one addressing data quality. In addition, OIRA worked with the Council of Economic Advisers to issue guidelines for conducting regulatory analysis.

PEER REVIEW The administration has issued two draft versions of peer review guidelines in an attempt to find procedures that will guide agencies to improve the quality of the science underlying regulatory actions. If implemented properly, meaningful peer review would improve the quality of scientific information and reduce the degree to which OIRA questions agencies' scientific judgments. However, OIRA's latest draft guidelines (issued in April 2004) fall short of forcing meaningful changes.

OIRA and the Office of Science and Technology Policy first issued a draft peer review bulletin in August 2003. The draft not only required agencies to comply with broad peer-review principles, but also recognized that financial conflicts-of-interest can arise from ties to an agency as well as to industry, stressed the need for openness in the peer review process, and appropriately limited peer review to scientific and not policy issues.

Bowing to pressure from other agencies, OIRA modified the guidelines in April 2004 to exempt more analyses from peer review. Among the analyses exempted were National Academy of Sciences reports and Regulatory Impact Analyses, arguably the two categories of analysis that are most influential in determining regulatory policy. It also abandoned language that would have limited peer review to scientific matters, and provided significantly more discretion to federal agencies in deciding who to include as peer reviewers and when a peer review was adequate.

Neither draft contains mechanisms for a third party to hold an agency accountable for following the peer review guidelines. That shortcoming, combined with the discretion given to agencies for the peer review process, means the guidelines are unlikely to accomplish the objective of more rigorous and defensible scientific support for proposed regulatory activities.

DATA QUALITY In September 2001, OIRA issued government-wide information quality guidelines for compliance with the Information Quality Act. The guidelines provide broad definitions of important concepts but require the individual agencies to issue their own guidelines tailored to the demands of each agency. OIRA guidelines also require agencies to establish mechanisms to allow affected people to seek and obtain correction of information maintained and disseminated by agencies.

Most agencies have followed suit with their own agency-specific guidelines, and they are mixed. For example, the EPA's guidelines exempt many analyses from data quality scrutiny and refer to pre-existing guidelines the agency has relied upon for years, suggesting that the EPA already meets or exceeds any quality control standards envisioned by the Information Quality Act. Several parties have filed petitions under the legislation, requesting correction to agencies' data that do not meet the act's standards of objectivity, quality, and integrity. The significance of the act ultimately depends on the disposition of those petitions.

CIRCULAR A-4 In September 2003, OIRA issued Circular A-4 to provide guidance to federal agencies for performing regulatory analysis as required by EO 12866. The 48-page document lays out detailed steps for examining regulatory proposals, from identifying a need for federal action to examining alternatives and evaluating costs and benefits. As a circular, it carries more weight than the 1996 "Best Practices" guidance it replaced. Compliance with Circular A-4 is effective for proposed regulations as of January 1, 2004, and for final regulations starting January 1, 2005.

In general, the circular provides solid analytic guidelines that, if followed, should improve regulatory policy. It provides more detailed guidance in several key areas, including the conduct of cost-effectiveness analysis and benefit-cost analysis as well as how to treat uncertainty using formal probabilistic analysis. It is refreshing that the circular encourages agencies to be transparent in their analysis and assumptions so that reviewers can understand and reproduce results. The guidelines should help ensure greater consistency across agency analyses and should facilitate more accurate annual reporting of regulatory costs and benefits as required by Congress.

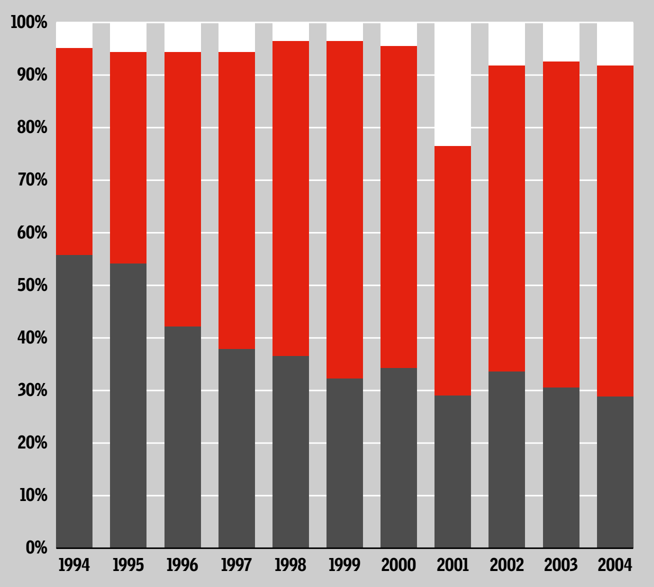
Despite those good qualities, the circular takes some curious turns that seem inconsistent with an administration philosophy that embraces markets and limited government. For example, Circular A-4 is arguably less demanding than either the Reagan or Clinton guidelines in its requirement that, before considering regulatory intervention into private markets, an agency must first identify a significant market failure. The new guidelines cite "other possible justifications" for regulatory action, including "promoting privacy and personal freedom." It provides no example of when regulation (which, almost by definition, restricts personal freedoms) would be necessary to promote personal freedom.

The circular also suggests that "harmonization of U.S. and international rules may require a strong Federal regulatory role." What this means is unclear. Would the new guidelines endorse restrictions on promising new therapeutic or agricultural products so as to "harmonize" with European Union members who prefer not to use biotechnology techniques? U.S. foreign policy ought to stress our objective of exporting freedom, not

FIGURE 1

OIRA's Review of Draft Regulations

■ Withdrawn ■ Approved with Change ■ Approved without Change



importing government regulations — particularly regulations that lack an economic rationale apart from "everybody does it."

Circular A-4, like the Clinton guidelines before it, supports the use of the controversial benefit-valuation technique known as contingent valuation (CV). Noting that CV may be the only method available to estimate "non-use" values, the guidelines attempt to address its problems by enumerating "best practices" for conducting CV. Relying on a technique because it is the only thing available is a weak endorsement, at best. All of the best practices, and all of the care in the world, will not redeem a technique that is fundamentally flawed.

ANNUAL REPORT TO CONGRESS OIRA's annual response to its congressional mandate to report on the costs and benefits of regulation routinely misses an opportunity to highlight problems with agency regulatory analyses and offer a meaningful estimate of the full impacts of regulation. Instead, the reports tally agency estimates of the costs and benefits of economically significant regulations issued over the previous fiscal year, with no independent assessment of the quality or usefulness of agency analyses. The benefits and costs for fiscal year 2003 are based on agency estimates for only six regulations, or one-tenth of one percent of the final rules published in the *Federal Register* during the year.

REGULATORY REVIEW TRENDS

In addition to looking at specific guidelines and regulatory actions, statistics on the disposition of regulations pursuant to review under EO 12866 is informative. As noted above, OIRA is using prompt letters to encourage agencies to take regulatory action and "return letters" to send agencies back to the drawing board for rules OIRA finds inconsistent with administration policy. In the first year of the George W. Bush administration, OIRA issued five prompt letters, 14 return letters, and wrote "post-review letters" publicly explaining the weaknesses of two rules it allowed to go into effect. In 2002, OIRA wrote four prompt letters and two post-review letters, but returned only five regulations. In 2003, the number of prompt and post-review letters remained at four and two, respectively, but only two rules were returned. At the time this article was written, OIRA had issued only one post-review and one prompt letter in 2004.

One possible explanation for the decline in public return letters is that, after the initial rap on the knuckles at the beginning of the new administration, agencies are producing better analysis and writing regulations that are more consistent with EO 12866's principles. A more plausible explanation is that, rather than be exposed to the public reprimand of a return letter, regulatory agencies prefer to negotiate a resolution with OIRA or withdraw regulations that have reached an impasse.

OIRA keeps statistics on the percentage of draft regulations that it approves without change, with change, or that agencies withdraw. Those numbers suggest that President Bush's OIRA required changes to regulations before approving them more frequently than the three previous administrations. The statistics also show that more rules were withdrawn after OIRA reviewed them during this administration than during any other administration. (Note that this comparison may be misleading with respect to the Reagan and George H. W. Bush administrations because, since 1992, OIRA reviews only "significant" rules, which would likely receive more scrutiny.) Figure 1 shows the percentage of rules reviewed by OIRA since 1994 that were approved without change, approved with change, and withdrawn.

REGULATORY BURDEN OIRA claims to have reduced the costs of new regulations during the current Bush administration. According to OIRA statistics, the cost of major new regulations issued during George W. Bush's first three years in office was $1.6 billion per year, compared to an average of $6.2 billion per year during the Clinton administration and $8.4 billion during the first Bush administration. It recognizes that those averages do not include the fourth year of the current administration, which experience suggests will impose more regulations than the previous three years.

Those statistics must be considered with a grain of salt because they reflect agency estimates of the costs of rules and exclude regulations for which agencies have not estimated costs. Indeed, the $2.5 billion annual cost estimate for new rules issued in fiscal year 2003 is, as noted above, based on agency estimates for only one-tenth of one percent of the final rules published in the *Federal Register* during the year.

Other statistics on trends in regulatory activity paint a different picture and suggest that the regulatory state is growing. The annual page count in the *Federal Register*, which is admittedly an imperfect proxy for regulatory activity, averaged 74,610 pages for the first three years of the current Bush administration, compared to 71,578 pages for the eight years of the Clinton administration, 59,519 for the George H. W. Bush administration, and 54,335 for the Reagan administration.

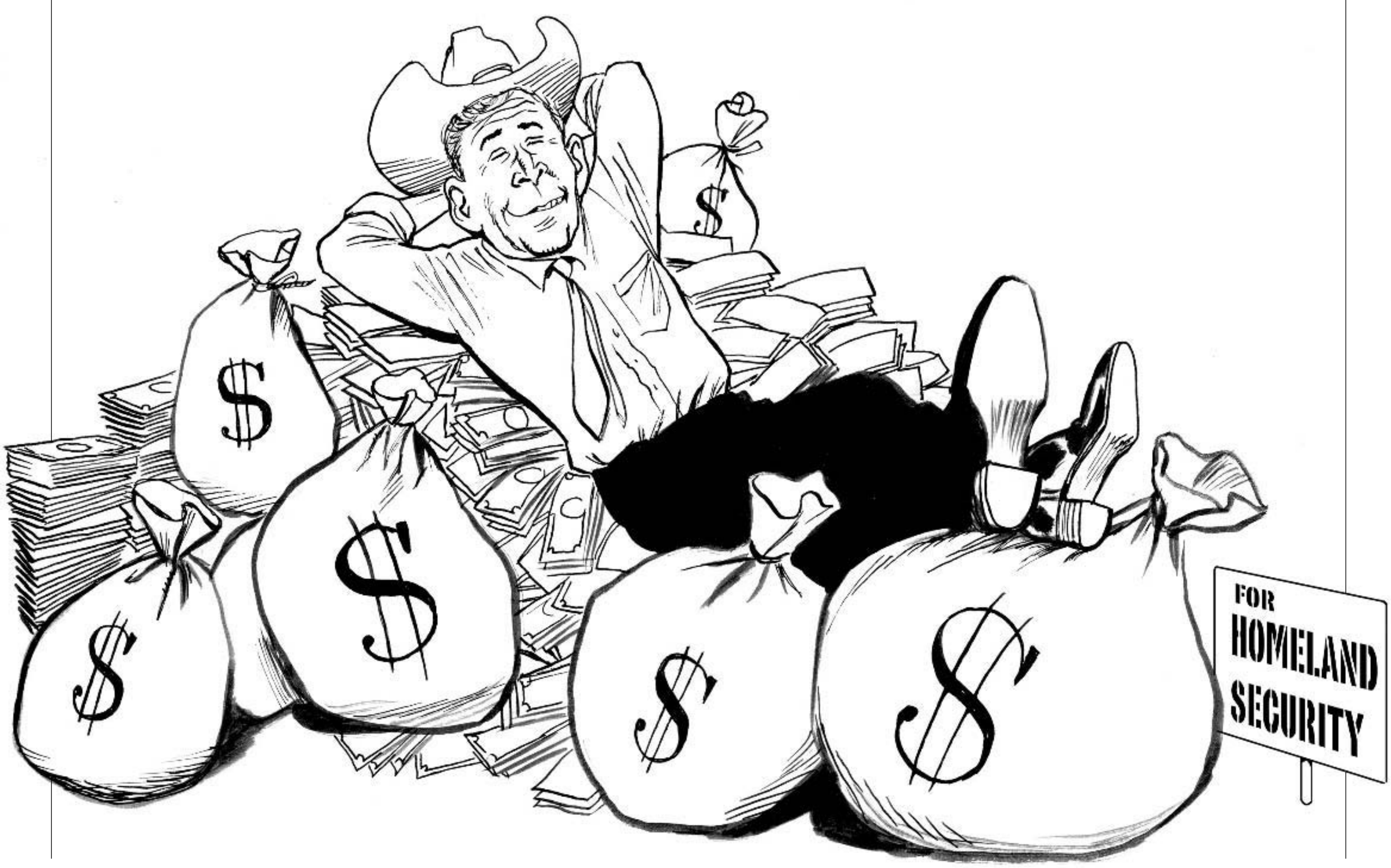
According to a recent report by the Mercatus and Weidenbaum centers, the regulators' budget — the on-budget costs of writing and enforcing regulations — has increased by 47 percent in real terms during President Bush's tenure. Regulatory staff has grown by 40 percent since 2000. Those large increases reflect concerns about corporate governance and homeland security; the FY 2005 budget request for the Securities and Exchange Commission's regulatory activities has increased by 156 percent since FY 2000 and budgets related to homeland security regulatory activities have increased by 98 percent in real terms over the same period.

CONCLUSION

The Bush administration has reasserted control over federal rulemaking in important ways. OIRA has reinvigorated the regulatory review process, exhibiting a willingness to return regulations that do not meet analytical requirements, and has required changes in a larger percentage of the rules it reviewed than previous administrations. It has issued guidelines to agencies on regulatory analysis, peer review, and data quality that, while not entirely consistent with free-market and federalism principles, are generally sound. It has also increased the transparency of its activities, reducing criticism that it operates in secret to advance special interests.

The administration can boast several significant regulatory and deregulatory initiatives that benefited from careful analysis and consideration of tradeoffs. Some of those regulatory activities, notably the TMDL and storm water runoff rules, appropriately defer decisions to state and local governments. Others, such as effluent guidelines covering different sectors, are more cost-effective than they would otherwise have been as a result of regulatory oversight. The sunsets of the Transportation Department's airline computer reservation system rules and the FDA's request for public comment on the impact of its regulations on First Amendment rights reflect a willingness to question the status quo and reevaluate practices that may be outdated or inappropriate.

Overall, however, OIRA's paradigm appears to be that, rather than rely on market processes, property rights, and individual choice, smarter regulators can devise government solutions to perceived problems. Administrator Graham has added scientists and public health specialists to OIRA staff, issued prompt letters to encourage regulatory activity, and emphasized cost-effectiveness analysis to promote public health. OIRA can point to examples of where this model has improved the cost-effectiveness of rules, but this faith in the ability of smarter regulators to analyze problems and achieve socially optimum results overlooks the insights of public choice economics, federalism principles, and free-market environmentalism. It has led, for example, to the present situation with the mercury emissions rule where the EPA need only suggest ancillary reductions in particulate matter to calculate health benefits that dwarf its estimated costs and justify any regulation. R



Wine Wars: Uncorking E-commerce?

By Asheesh Agarwal, Jerry Ellig, and Todd Zywicki

The U.S. Supreme Court's docket this term includes three cases, which will be heard together, concerning the sale of wine directly to consumers. The cases challenge laws in New York and Michigan that permit in-state wineries to sell and ship their products directly to state residents, but prohibit out-of-state wineries from doing the same thing.

The plaintiffs argue that the laws are little more than economic protectionism for Michigan and New York businesses, and thus they violate the so-called "dormant commerce clause." The defendants respond that the laws are permitted under the Twenty-first Amendment, which gives states the right to regulate alcohol. The dispute has generated considerable attention because, though the suits focus specifically on wine, the Court's decision will likely have far-reaching effects on the field of Internet "e-commerce."

DORMANT COMMERCE CLAUSE The commerce clause of the U.S. Constitution provides that Congress has the power to "regulate Commerce with foreign Nations, and among the several States." From that, the courts have developed the dormant commerce clause doctrine, which holds that if Congress has not specifically permitted some form of interstate barrier to trade, that barrier should be considered unconstitutional unless some substantial, non-protectionist state interest is involved. For example, the Court in 1824 invalidated a New York law granting a navigation monopoly in state waters, then in 1875 threw out a discriminatory Missouri license tax on importers of out-of-state products, then in 1935 tossed out a New York price-control law that discriminated against out-of-state milk producers, and in 1989 overturned a Connecticut statute that required vendors to conform in-state beer prices to prices in other states.

In analyzing a potentially problematic state law, the first step is to determine whether it discriminates against interstate commerce or merely has incidental effects on interstate commerce. The Supreme Court has held that state laws discriminating against interstate commerce on their face are "virtually per se invalid."

If a statute discriminates against interstate commerce, the state must show that it "advances a legitimate local purpose that cannot be adequately served by reasonable nondiscriminatory alternatives." It is not sufficient just to show that the regime as a whole is justifiable; the discrimination itself must be shown to be vital to achieving the regulatory objective. Under those strictures, the state's burden is high — the Court has required states to provide substantial empirical and other evidence demonstrating that it has no alternative but to adopt measures that discriminate against out-of-state merchandise. In fact, the Court has only upheld one discriminatory state law, in the 1986 case of *Maine v. Taylor.*

It does not appear that either Michigan or New York can meet that standard. The arguments most often used to defend the laws — that the prohibition is required to discourage underage drinking, excessive drinking, and evasion of alcohol taxes — do not explain why the two states would continue to permit intrastate direct sales. In New York, for instance, 190 in-state wineries can ship directly to consumers' homes. As one judge has observed, it is difficult to believe that temperance concerns justify discrimination, because consumers can become just as "drunk on local wines" as those of out-of-state suppliers.

The underage drinking issue is largely a red herring. When Federal Trade Commission staff surveyed enforcement officials from states that allow interstate direct shipping, few reported any problems with shipping to minors. Sting data from states that ban out-of-state direct shipping suggest that it is at least as easy for minors to buy alcohol in local retail stores as it is online. In a 2002 survey, large percentages of high school students, from 68 to 95 percent, said that it is "fairly easy" or "very easy" to get alcohol. Given those facts, it is doubtful that interstate direct shipping would increase the availability of alcohol to minors.

Moreover, the benefit to consumers from allowing direct shipment of out-of-state wines is significant. Not only does e-commerce increase the variety of wines that consumers can purchase, but it also lets them find lower prices. Recent research by Alan E. Wiseman and Jerry Ellig indicates that Virginia's direct shipment ban, which was lifted in July 2003, prevented consumers from purchasing some premium wines at lower prices. Using a 67-bottle sample of popular wines, Wiseman and Ellig found that, though e-commerce cost savings varied depending on the price per bottle, the quantity ordered, and shipping method, online shopping for the entire sample could save the consumer as much as 3.6 percent. Most savings occurred on the more expensive bottles; online savings of 7 to 13 percent were available on bottles costing at least $20, and savings of 17 to 21 percent were available on bottles costing at least $40. The authors calculated that a comparison shopper who buys each bottle from the cheapest source (on-line or off-line) could save an average of between $2.21 and $4.30 per bottle on the

Asheesh Agarwal is assistant director of the Office of Policy Planning at the Federal Trade Commission.

Jerry Ellig is a senior research fellow at the Mercatus Center at George Mason University.

Todd Zywicki is a professor of law at the George Mason University School of Law and currently a visiting professor of law at the Georgetown University Law Center.

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entire sample, or 1.6 to 9.7 percent, depending on the quantity and shipping method.

E-COMMERCE Though often regarded as unique, the Michigan and New York cases have broad implications for e-commerce. In particular, if the New York law is upheld, states would have significant leeway to impose "physical presence" requirements on firms that currently sell over the Internet.

Under the New York law, out-of-state wineries may ship wine directly to consumers only if those wineries establish a "physical presence" in the state. The Second Circuit held that, because of this option, New York's scheme is "non-discriminatory." New York argues that physical presence requirements do not discriminate against out-of-state wineries because they are subject to far less regulatory control than in-state wineries. Without the physical presence requirement, the states argue they could not exercise appropriate oversight.

It has long been a backbone principle of constitutional law that a state cannot require the firm to have an in-state physical presence in order to sell merchandise in the state. In its 1992 decision for *Kraft Gen. Foods, Inc. v. Iowa Dep't. of Revenue and Finance,* the Supreme Court held that there is "no authority" for the proposition that a discriminatory tax against out-of-state commerce "may be upheld if a taxpayer could avoid that discrimination by changing the domicile of the corporations through which it conducts its business." Upholding physical presence requirements could thus sweep well beyond the alcohol context and could have an especially pernicious impact given the prevalence of mail order and Internet commerce. State physical presence laws deprive online suppliers of one of the main efficiency benefits of e-commerce: the ability to provide goods and services over large distances without the need for a substantial, far-flung physical presence. If extended to industries besides wine — as the Second Circuit seemed to do with tobacco in the 2003 case of *Brown & Williamson Tobacco Corp. v. Pataki* — physical presence requirements could force online companies such as Amazon.com or catalogue retailers such as L.L. Bean to establish offices in all 50 states.

As the Supreme Court recognized in the 1951 case *Dean Milk Co. v. City of Madison,* permitting this type of requirement "would invite multiplication of preferential trade areas destructive of the very purpose of the commerce clause." Indeed, because states enforce a host of consumer protection laws against out-of-state sellers, the argument that states have to require an in-state physical presence to exercise adequate regulatory oversight could apply to every company that ships any product to consumers in another state. If upheld, physical presence requirements would represent a substantial step in the direction of economic balkanization.

In the past, the Supreme Court has expressly held that states may not satisfy their regulatory objectives by requiring out-of-state suppliers to establish an in-state physical presence. The Court "has viewed with particular suspicion state statutes requiring business operations to be performed in the home State that could more efficiently be performed elsewhere. Even where the State is pursuing a clearly legitimate local interest, this particular burden on commerce has been declared to be virtually per se illegal."

CONCLUSION The Supreme Court has two possible roadmaps for affirming Michigan and New York's bans on interstate shipment of wine, both of which could be disastrous. On one hand, the Court could recognize the protectionist intent of the laws and nonetheless hold that they are justified. That would ignore the Court's longstanding commitment to enforcing the Constitution's promise of the internal free flow of goods and the requirement that protectionist bans be justified by a real showing of a compelling need for the discrimination itself. On the other hand, the Court could hold that the "physical presence" exception renders the New York and Michigan laws nondiscriminatory. That result could be even more damaging to consumers and competition, as it could unravel the entire foundation of the Constitution's protection of interstate commerce. That would justify the enactment of similar requirements in any industry where a plausible nexus to consumer protection concerns exists, and could spawn a round of reciprocal trade barriers against out-of-state sellers. R

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