Dormant Commerce Clause Issues Are Evolving In Cannabis

By **Tommy Tobin and Andrew Kline** (March 27, 2023)

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Can states restrict ownership of licensed businesses to state residents only? The answer to this question would generally be a straightforward no — states cannot attempt to provide undue, preferential treatment to their own citizens over those from other states.

But federal courts have reached different conclusions when it comes to state-legal marijuana operations.

For instance, in the U.S. Court of Appeals for the First Circuit,[1] the appellate panel concluded last year in Northeast Patients Group v. United Cannabis Patients and Caregivers of Maine that the U.S. Constitution precluded states from implementing residency requirements for dispensary ownership in Maine.

By contrast, on Feb. 7, the U.S. District Court for the Western District of Washington concluded in Brinkmeyer v. Washington State Liquor and Cannabis Board that similar residency requirements in Washington state would be upheld.[2]

Both federal courts wrestled with the state regulation of marijuana in the context of the dormant commerce clause.

This article explores what legal and policy advisers in the cannabis space need to look out for as this issue evolves across the country. We also look at the related interstate compacts issue looming in the background.

What Is the Dormant Commerce Clause?

A foundational constitutional principle is that Congress has exclusive authority to legislate issues involving commerce between the states.[3]

As a corollary to this authority, courts have recognized the dormant commerce clause — also known as the negative commerce clause — to protect against states imposing undue burdens upon interstate commerce.[4]

The U.S. Supreme Court explained in its 2019 Tennessee Wine and Spirits Retailers Association v. Thomas decision that the dormant commerce clause is intended to prevent states "from adopting protectionist measures and thus preserves a national market for goods and services."[5]

The court also noted that the dormant commerce clause is "the primary safeguard against state protectionism."[6]

Even when a state regulation does not discriminate against out-of-state residents on its face, the court has struck down state mandates when the burden on interstate commerce "is clearly excessive in relation to the putative local benefits," as articulated in its 1970 Pike v. Bruce Church decision.[7]

As the Supreme Court explained in its 1988 New Energy Co. v. Limbach decision, the dormant commerce clause means that

> state statutes that clearly discriminate against interstate commerce are routinely struck down ... unless the discrimination is demonstrably justified by a valid factor unrelated to economic protectionism.[8]

For example, the court invoked the dormant commerce clause to strike down a state requirement mandating the use of a certain shape of mudguards on trucks passing through the state when surrounding states mandated a different shape.[9]

Why the Controversy Over Cannabis?

Cannabis is illegal at the federal level. But more than two-thirds of states have legalized cannabis for medical use, and more than 20 states have created adult-use marketplaces.[10] Meanwhile, the dormant commerce clause aims to preserve a national market.

So, the inscrutable law school exam question that we face is this: Can cannabis be the subject of the dormant commerce clause when a national market for cannabis is illegal at the federal level?

Majority View: Courts Using Dormant Commerce Clause to Strike Down Residency Requirements

A majority of federal courts that have taken up the dormant commerce clause issue have struck down residency requirements on the basis that such mandates violate the dormant commerce clause.

These cases include, but are not limited to:

- NPG LLC v. City of Portland, Maine, in which the U.S. District Court for the District of Maine in 2020 granted the plaintiff's preliminary injunction and reasoned that the plaintiff was likely to succeed on its argument that Maine's cannabis licensing residency requirements violated the dormant commerce clause;[11]

- Variscite NY One Inc. v. New York, in which the U.S. District Court for the Northern District of New York last November found similarly as applied to New York's residency requirements;[12]

- Toigo v. Department of Health and Senior Services, in which the U.S. District Court for the Western District of Missouri in 2021 held similarly in relation to Missouri's cannabis licensing residency requirements;[13]

- Lowe v. City of Detroit, in which the U.S. District Court for the Eastern District of Michigan in 2021 found that Detroit's cannabis licensing requirements violated the dormant commerce clause;[14] and

- Finch v. Treto,[15] in which the U.S. District Court for the Northern District of Illinois concluded last June that Illinois's cannabis licensing residency requirements likely violated the dormant commerce clause but denied preliminary injunctive relief on other grounds.

Abstaining from Ruling

Other courts have abstained from ruling on the issue.

In Original Investments LLC v. Oklahoma,[16] the U.S. District Court for the Western District of Oklahoma in 2021 concluded that the federal illegality of cannabis meant that the court should refuse to rule as to avoid granting relief that would violate federal law.

The Western District of Washington similarly ruled last August in Shelton v. Liquor and Cannabis Board Washington that it could not grant declaratory relief that would effectively mean that the court was ordering activity that remains federally illegal.[17]

Elsewhere, in Peridot Tree Inc. v. City of Sacramento,[18] the U.S. District Court for the Eastern District of California refused last October to issue a ruling on the dormant commerce clause as to avoid "disrupting California's efforts to 'establish a coherent policy with respect to a matter of substantial public concern'" because the state courts "are well-equipped to do" so. This case is currently on appeal to the U.S. Court of Appeals for the Ninth Circuit.[19]

Minority View: Dormant Commerce Clause Does Not Apply to Cannabis

Most recently, the Western District of Washington declined to apply the dormant commerce clause when evaluating Washington state's residency requirements, reasoning that there is not a national market for cannabis given its federal illegality.

In Brinkmeyer, the Seattle federal court ruled that the dormant commerce clause "does not apply to federally illegal markets, including Washington's cannabis market and, thus, it does not apply to Washington's residency requirements."

The Washington court specifically disagreed with the U.S. Court of Appeals for the First Circuit that the federal government had substantially legalized cannabis through the exercise of prosecutorial discretion, writing that "prosecutorial discretion is not equivalent to legalization."

In addition, the Washington court further disagreed with the First Circuit's approach that the Rohrabacher-Farr Amendment was persuasive as to Congress' intent to exercise its commerce clause powers. The Rohrabacher-Farr Amendment has prohibited the U.S. Department of Justice from using appropriated funds to interfere with the implementation of state-legal medical marijuana since 2014.

The appropriations amendment does not legalize cannabis and must be renewed each fiscal year.

In the words of the First Circuit, the Rohrabacher-Farr Amendment "plainly reflect[s] an effort by Congress to free the market in medical marijuana from being subject to the full degree of federal criminal enforcement to which that market otherwise would be subject."[20]

What Does This Mean?

The cannabis industry has much to watch regarding the dormant commerce clause and related issues like interstate compacts.

First, the cannabis industry should look to the coming dormant commerce clause debates in the appellate courts.

To date, the First Circuit — the only appellate panel to evaluate whether the dormant commerce clause applies to state-legal cannabis marketplaces — arrived at two important conclusions: (1) It concluded that the dormant commerce clause does apply to state-legal cannabis markets, and (2) the appellate panel determined that a state's residency requirements regarding cannabis-licensed businesses must be struck down under the dormant commerce clause.

Moving forward, the Ninth Circuit will see appeals in cases challenging the dormant commerce clause. As noted above, the Peridot Tree case is currently on appeal, and an appeal has been filed in the Brinkmeyer case, so expect to see further argument about the effect of the Rohrabacher-Farr Amendment.

Second, the cannabis industry should continue to watch district courts. Currently, the majority view has seen state residency requirements struck down on dormant commerce clause grounds.

Given this majority view, additional cases might see courts adopting similar views, but the recent Brinkmeyer decision suggests that courts could take a different view.

The Brinkmeyer court's reasoning was similar to that of the dissent in the First Circuit's case; namely, that there cannot be a national market for goods that are federally illegal.

District courts could find this reasoning persuasive in challenging the emerging majority view. Such challenges would prompt additional litigation at the appellate level, and further uncertainty for state regulators and regulated businesses.

Third, cannabis legalization is increasingly becoming a question of not if, but when.[21] While multiple legislative and administrative proposals would deschedule or legalize cannabis, these proposals should recognize the existing state-legal marketplaces and incorporate regulatory provisions to avoid dormant commerce clause challenges in advance.[22]

The worst-case scenario would be to legalize the plant only to find that existing and necessary state regulations violate the U.S. Constitution.

While residency requirements have been the focus of many dormant commerce clause cannabis cases to date, future controversies may be looming regarding lab testing

requirements, track and trace mandates, or packaging and labeling standards, particularly when some state standards are stricter than others.

For instance, states with medical cannabis programs all have potency and/or contaminant testing requirements. However, the testing standards and methodologies vary from state to state.

Some require testing for several fungal and bacterial microorganisms — e.g., Colorado, Connecticut, Hawaii, Illinois, Oklahoma and Massachusetts — with wide variations about the extent of such testing.

Some states require testing for 13 pesticides — e.g., Colorado — and other states require testing for 66 pesticides, e.g., California.[23]

Conflicts among state requirements present concerns that could raise headaches for regulated businesses, prompt litigation and put pressure on regulators to harmonize rules across jurisdictions.

Fourth, the cannabis industry should watch state houses. Not only have states lead the charge regarding cannabis legalization and regulation, but many states are also now considering interstate compacts, which would permit interstate trade of cannabis among states.

Oregon and California have passed such laws, and Washington state is considering a similar approach.[24]

Washington's proposal, for example, would take effect after (1) a change in federal law to allow interstate transfers of cannabis, or (2) a DOJ opinion allowing or tolerating cannabis across state lines.

One item to watch closely is that California's top cannabis regulator has asked the state's attorney general to issue an advisory opinion regarding whether the import and export of cannabis would result in significant legal risk to California under the Controlled Substances Act.[25]

While this opinion may fulfill state statutory requirements for California to trigger its interstate compact statute, this request was crafted to focus on the risks to the state arising from the CSA regarding interstate transfers of cannabis.

Moreover, California's trigger for its interstate commerce compact differs from that passed in Oregon or contemplated in Washington.

Oregon's interstate compact law, passed in 2019, allows interstate agreements for cannabis only upon (1) changes to federal law, or (2) a DOJ opinion or memorandum allowing or tolerating the interstate transfer of cannabis.[26]

The Washington Legislature is considering S.B. 5069, which contains the same triggers.[27]

As such, California's interstate cannabis compact might see the state allowing imports or exports to or from the state, but may find no other jurisdiction with which to trade, at least until other states' triggers for interstate agreements come into effect.

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[1] Ne. Patients Grp. v. United Cannabis Patients & Caregivers of Me., 45 F.4th 542 (1st Cir. 2022).

[2] Brinkmeyer v. Wash. State Liquor & Cannabis Bd., No. 3:20-cv-05661 (W.D. Wash.).

[3] U.S. Const. art. I, § 8, cl. 3.

[4] See Tommy Tobin & Andrew Kline, A Sleeping Giant: How the Dormant Commerce Clause Looms Over the Cannabis Marketplace, Yale L. & Pol'y Rev. Inter Alia (Jan. 3, 2022), https://ylpr.yale.edu/inter_alia/sleeping-giant-how-dormant-commerce-clause-looms-over-cannabis-marketplace.

[5] Tenn. Wine & Spirits Retailers Ass'n v. Thomas, 139 S. Ct. 2449, 2459 (2019).

[6] Id. at 2461.

[7] Pike v. Bruce Church, Inc., 397 U.S. 137, 142 (1970).

[8] New Energy Co. of Ind. v. Limbach, 486 U.S. 269, 274 (1988).

[9] Bibb v. Navajo Freight Lines, Inc., 359 U.S. 520, 529 (1959) (invalidating state mandate regarding certain types of mudflaps).

[10] National Conference of State Legislatures, State Medical Cannabis Laws (Sept. 12, 2022), https://www.ncsl.org/health/state-medical-cannabis-laws.

[11] No. 2:20-cv-00208-NT, 2020 WL 4741913, at *8–12 (D. Me. Aug. 14, 2020), aff'd sub nom. Ne. Patients Grp. v. United Cannabis Patients & Caregivers of Me., 45 F.4th 542 (1st Cir. 2022).

[12] No. 1:22-cv-1013 (GLS/DJS), 2022 WL 17257900, at *5–9 (N.D.N.Y. Nov. 10, 2022).

[13] 549 F. Supp. 3d 985, 990–96 (W.D. Mo. 2021).

[14] 544 F. Supp. 3d 804, 812–16 (E.D. Mich. 2021).

[15] No. 22 C 1508, 2022 WL 2073572, at *12–20 (N.D. Ill. June 9, 2022).

[16] 542 F. Supp. 3d 1230, 1235 (W.D. Okla. 2021).

[17] Shelton v. Liquor & Cannabis Bd. of the State of Wash., No. 21-5135, 2022 WL 2651617, at *5 (W.D. Wash. Aug. 16, 2022).

[18] No. 22-cv-00289-KJM-DB, 2022 WL 10629241, at *11 (E.D. Cal. Oct. 18, 2022).

[19] See Sam Reisman, Sacramento Pot Retail Policy Unconstitutional, 9th Circ. Told, Law360 (Feb. 24, 2023), https://www.law360.com/cannabis/articles/1579729?nl_pk=5502c6a3-d705-410c-a0cc-051c2c4e3b36.

[20] 45 F.4th at 553.

[21] Tobin & Kline, A Sleeping Giant, at 5-6.

[22] Id.

[23] See National Cannabis Laboratory Council, Standardizing Cannabis Lab Testing Nationally (2022) https://www.perkinscoie.com/images/content/2/5/253590/Standardizing-Cannabis-Lab-Testing-Nationally-FINAL-7-1-1.pdf.

[24] Ben Adlin, New Washington Bill Would Allow Interstate Marijuana Commerce, Marijuana Moment (Dec. 23, 2022), https://www.marijuanamoment.net/new-washington-bill-would-allow-interstate-marijuana-commerce/.

[25] Dep't of Cannabis Control, Ltr. to M. Lee (Jan. 27, 2023), https://www.law360.com/articles/1571232/attachments/0.

[26] SB 582. https://olis.oregonlegislature.gov/liz/2019R1/Downloads/MeasureDocument/SB0582/Enrolled.

[27] SB 5089, https://app.leg.wa.gov/billsummary/?BillNumber=5069&Year=2023&Initiative=false.