No. _____

In The Supreme Court of the United States

SAM FRANCIS FOUNDATION, ESTATE OF ROBERT GRAHAM, CHUCK CLOSE, and LADDIE JOHN DILL,

Petitioners,

v.

CHRISTIE'S, INC., SOTHEBY'S, INC., and EBAY, INC.,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

In *Healy v. Beer Institute*, 491 U.S. 324 (1989), the Court wrote that "the 'Commerce Clause . . . precludes the application of a state statute to commerce that takes place wholly outside of the State's borders, whether or not the commerce has effects within the State[.]'" 491 U.S. at 336 (quoting *Edgar v. MITE Corp.*, 457 U.S. 624, 642-43 (1982) (plurality opinion)). But the Court has long and consistently held that the purpose of its "dormant" or "negative" Commerce Clause jurisprudence is to "prohibit[ ] States from discriminating against or imposing excessive burdens on interstate commerce[.]" *Comptroller of Treasury of Md. v. Wynne*, 135 S. Ct. 1787, 1794 (2015). As a result, the lower courts are divided over whether a state statute violates the dormant Commerce Clause simply because it applies to commerce "wholly outside" of the state that enacted it – as the en banc Ninth Circuit held in this case – or whether the dormant Commerce Clause is violated only if a state statute discriminates against or excessively burdens interstate commerce. The question presented is:

If a state statute does not in any way discriminate against, or impose an excessive burden on, interstate commerce, does the Commerce Clause of the United States Constitution, art. I, § 8, cl. 3, nevertheless require the statute's invalidation *solely* because it regulates commerce occurring beyond the borders of the state that enacted it?

PARTIES TO THE PROCEEDINGS

Petitioners are the Sam Francis Foundation, the Estate of Robert Graham, Chuck Close, and Laddie John Dill. Respondents are Christie's, Inc.; Sotheby's, Inc.; and eBay, Inc.

RULE 29.6 CORPORATE DISCLOSURE STATEMENT

The Sam Francis Foundation is a nonprofit public benefit corporation. It has no parent company, and no publicly held company owns 10 percent or more of its stock.

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OPINIONS BELOW

The en banc Ninth Circuit's opinion is reported at 784 F.3d 1320 (9th Cir. 2015). App. 1-35. The Ninth Circuit did not issue a panel opinion in the case. The opinion of the United States District Court for the Central District of California is reported at 860 F. Supp. 2d 1117 (C.D. Cal. 2012). App. 42-61.

JURISDICTION

The en banc Ninth Circuit issued its opinion on May 5, 2015. On July 15, 2015, Justice Kennedy granted petitioners' application to extend the time within which to file a petition for a writ of certiorari to September 2, 2015. This Court has jurisdiction under 28 U.S.C. § 1254(1). Pursuant to Supreme Court Rule 29.4(c), petitioners notified the Attorney General of California of these proceedings.

CONSTITUTIONAL AND STATUTORY PROVISIONS AT ISSUE

The courts below concluded that a portion of California's Resale Royalties Act, Cal. Civ. Code § 986, violated the Commerce Clause of the United States Constitution, art. I, § 8, cl. 3. Both the Act, App. 62-66, and the Commerce Clause, App. 67, are reproduced in the appendix to this petition.

STATEMENT OF THE CASE

In the fall of 1973, Sotheby's conducted an unusually lucrative art auction. The taxicab magnate whose collection was on the block, and who had recently purchased – for modest amounts – some of the work to be auctioned, ended up reaping famously large profits. *See* Barbara Rose, *Profit Without Honor*, New York Magazine, Nov. 5, 1973, at 80-81. That auction, and especially those profits, helped galvanize artists to lobby for a *droit de suite*; that is, a right to collect royalties on the subsequent sales of their artwork. In 1976, California's Resale Royalty Act, Cal. Civ. Code § 986, created such a right – but only for certain art sales made in California, or outside of California if made by a California resident or the resident's agent (*e.g.*, an auctioneer).

The Act works as follows: If a work of fine art (as defined by statute) is re-sold (1) at a profit and (2) for over $1,000, either (3) in California, or (4) elsewhere by a Californian or a Californian's agent, then the seller (or agent) is required to withhold 5 percent of the sales price and pay it to the artist. Cal. Civ. Code §§ 986(a), (a)(1), (b)(2); App. 62, 64. If unable to locate the artist within 90 days of the sale, the seller (or agent) is required to remit the 5 percent royalty to California's Arts Council, which in turn takes up the task of searching for and paying the artist. *Id.* §§ 986(a)(2), (a)(5); App. 62, 63. The Act confers an assignable and devisable right of action that allows an artist to recover damages and attorney fees from a

seller or seller's agent who fails to withhold, pay or remit the required royalty. *Id.* § 986(a)(3); App. 62-63.

Petitioners Chuck Close and Laddie John Dill are artists owed royalties under the Act; the Sam Francis Foundation and the Estate of Robert Graham hold rights to royalty payments due their artist namesakes. *See* App. 43. Proceeding as putative representatives of a class of artists, they filed three complaints in the United States District Court for the Central District of California. *Ibid.* Invoking the court's diversity jurisdiction under 28 U.S.C. § 1332(d)(2), they alleged that respondents Sotheby's, Christie's, and eBay – all out-of-state companies with substantial presences in California (California is eBay's principal place of business) – acted as agents for California art sellers, on sales within and outside California. None, however, paid or remitted the required royalties. *See* App. 43.

Sotheby's, Christie's, and eBay moved to dismiss the artists' complaints, contending that the Resale Royalties Act violates the Commerce Clause, art. I, § 8, cl. 3, and the Takings Clause, amend. V, of the United States Constitution, and is preempted by the Copyright Act, 17 U.S.C. §§ 301, et seq. The district court forwent analysis of the auctioneers' preemption and Takings Clause claims, and instead dismissed the artists' complaints in their entirety on the basis that the Resale Royalties Act violates the "dormant"

aspect of the United States Constitution's Commerce Clause, art. I, § 8, cl. 3.[1] *See* App. 43-44.

Relying on this Court's opinion in *Healy v. Beer Institute*, 491 U.S. 324 (1989) – and without finding the Act protectionist, discriminatory, or otherwise burdensome of interstate commerce – the district court held that the Act was a per se unconstitutional regulation of extraterritorial activity because it "explicitly regulates applicable sales of fine art occurring wholly outside California." App. 54. And although the Act has a severability clause, Cal. Civ. Code § 986(e); App. 65, the district court held the portions of the Act that apply to sales outside California were not severable. App. 58. The district court therefore invalidated the entire Act. *Ibid.*

The artists appealed. After hearing argument, but before issuing a decision, a panel of the Ninth Circuit ordered the parties to brief "their respective positions on whether th[e] case should be heard en banc." App. 41. The panel directed the parties specifically to address "whether there is a conflict in our case law regarding the applicability of *Healy* . . . ." *Ibid.* In doing so, the panel sought to resolve a conflict between (1) the proposition that *Healy* appears to

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[1] The same district court had, in an unrelated case, previously disapproved the auctioneers' other principal argument, *i.e.*, that the Copyright Act, 17 U.S.C. §§ 301, et seq., preempts the Resale Royalties Act. *See Baby Moose Drawings, Inc. v. Valentine*, No. 2:11-cv-00697-JHN-JCGx, 2011 WL 1258529, at *3 (C.D. Cal. Apr. 1, 2011).

require the automatic invalidation of *any* statute regulating commerce beyond the enacting state's boundaries, *Rocky Mountain Farmers Union v. Corey*, 730 F.3d 1070, 1101 (9th Cir. 2013), *cert. denied*, 143 S. Ct. 2875 (2014), and (2) the view that *Healy*'s reach is limited to the type of laws *Healy* itself addressed, *i.e.*, price-control or price-affirmation statutes, *Ass'n des Eleveurs de Canards et d'Oies du Quebec v. Harris* ("*Canards et d'Oies*"), 729 F.3d 937, 951 (9th Cir. 2013), *cert. denied*, 135 S. Ct. 398 (2014). App. 41. The parties briefed the issue, and the Ninth Circuit granted en banc review without the three-judge panel ever issuing an opinion in the case.

The en banc court affirmed the district court's ruling that a portion of the Resale Royalties Act violates the dormant Commerce Clause, but reversed its ruling on severability. Two judges concurred in part; another filed a partial dissent.

Writing for the majority, Judge Graber "easily" applied what she called "the simple, well established constitutional rule summarized in *Healy*," *i.e.*, that a state law necessarily violates the Commerce Clause if it applies "'to commerce that takes place wholly outside of the State's borders, whether or not the commerce has effects within the State.'" App. 8, 12 (quoting *Healy*, 491 U.S. at 336). Since the Act applies to "sales outside the state of California," the majority held per se unconstitutional the portions of the law applying to *any* out-of-state sales, whether made by a Californian or an agent. App. 4.

Rather than invalidate the entire Act, however, the majority severed and invalidated only the portions reaching out-of-state sales, and remanded the case to the panel to consider the auctioneers' remaining arguments. App. 15. The panel subsequently remanded the case to the district court to undertake the inquiry in the first instance. App. 37.

Judge Berzon, joined by Judge Pregerson, concurred with the majority in part. Because "none of the parties before us are California sellers," and the record does not "contain any evidence pertaining to out-of-state sales by California residents," neither Judge Berzon nor Judge Pregerson would have opined on the Act's constitutionality as to out-of-state sales by Californians themselves. App. 34. Instead, they would have invalidated the Act only as to sales made out-of-state by agents. App. 33.

Concurring and dissenting, Judge Reinhardt wrote that he agreed the Act violated the dormant Commerce Clause when applied to out-of-state sales by the auctioneers, but that he would have held the Act explicitly *constitutional* as to Californian art sellers themselves. App. 18-19, 29. He noted that in all of this Court's dormant Commerce Clause cases invalidating a state law because of its extraterritorial reach, "the laws at issue have had a direct effect on out-of-state commercial transactions by regulating the price or terms of such transactions," or "by otherwise requiring 'an out-of-state merchant to seek regulatory approval in one State before undertaking a transaction in another[.]'" App. 27 (citation omitted).

Here, he observed, as applied to Californians, "the Act is plainly a regulation of . . . in-state obligations," *i.e.*, the obligation that Californians pay a percentage "of the proceeds that Californians have received from the sale of art, regardless of where the sale takes place." *Ibid.*

But while he agreed with the majority that the Act could not be applied constitutionally to the auctioneers' out-of-state sales, Judge Reinhardt joined a growing body of jurists, including Sixth Circuit Judge Sutton, to air "serious doubts that such a *per se* rule" – the *Healy* rule – "is wise as a matter of policy or that it is within the purview of the dormant Commerce Clause as properly framed." App. 30. As did Judge Sutton, Judge Reinhardt noted that the "central concern of the dormant Commerce Clause," curtailing economic protectionism, is not a purpose served by an extraterritoriality doctrine that requires courts blindly to "invalidate all state laws that apply extraterritorially . . . ." *Ibid.* Such a doctrine "'has nothing to do with favoritism. Even state laws that neither discriminate against out-of-state interests nor disproportionately burden interstate commerce may run afoul of extraterritoriality.'" *Ibid.* (quoting *Am. Beverage Ass'n v. Snyder*, 735 F.3d 362, 378 (6th Cir. 2013) (Sutton, J., concurring), *cert. denied*, 134 S. Ct. 89 (2013)).

By applying a rule that compelled the automatic invalidation of a statute solely because of its extraterritorial reach, Judge Reinhardt observed, the Ninth Circuit was invalidating a law that "imposes

obligations on out-of-state entities not to serve any protectionist purpose, but rather to make the law's valid requirement that Californians remit a portion of the proceeds they receive from art sales more effective." App. 30. The Act "does not provide any incentive for auction houses to sell the art of Californians relative to other states' residents, nor does it impose more stringent regulations on out-of-state auction houses than it does on California auction houses." App. 30-31. Thus, although Judge Reinhardt believed this Court's jurisprudence compelled the Act's invalidation as to out-of-state sales by agents, App. 32, he urged that this Court should reconsider the rule, App. 32-33.

REASONS TO GRANT THE PETITION

Judge Reinhardt and Judge Sutton are hardly alone in questioning why the dormant Commerce Clause should require the invalidation of a statute just because it reaches extraterritorial activity. The dormant Commerce Clause is a judge-made doctrine that exists to prevent states from enacting protectionist trade barriers, but a statute's extraterritorial reach alone says nothing about how it will affect trade, and certainly not enough to conclude that the statute is protectionist. Given the disconnect between what *Healy* requires – the per se invalidation of any law that reaches commerce "wholly outside" its enacting state – and the purpose *Healy* is supposed to be serving, it is not surprising that the courts of

appeals are divided over what role extraterritoriality should play in dormant Commerce Clause jurisprudence. It is equally unsurprising that legal scholars have long criticized *Healy*'s prohibition on extraterritorial regulation as a rule adrift of whatever moorings it ever might have had. Those are shaky grounds on which to undertake "[t]he serious duty of condemning state legislation as unconstitutional," *Chadwick v. Kelly*, 187 U.S. 540, 547 (1903), as the Ninth Circuit has done here.

By reading *Healy* to demand the per se invalidation of *any* statute that regulates commerce "wholly outside" its enacting state, the Ninth Circuit adopted a rule in direct opposition to at least the First, Tenth, and Eighth Circuits, all of which have held that a statute's extraterritorial reach alone is *not* reason enough to invalidate it. For its part, the Second Circuit has admitted it is confused about how to treat extraterritoriality in its dormant Commerce Clause jurisprudence. The Third Circuit is also confused, but silently so. Meanwhile, the Seventh Circuit is in the same camp as the Ninth, while the Sixth Circuit, per Judge Sutton, is there reluctantly.

Suffice it to say, and contrary to the declaration of the en banc majority in this case, the law in this area is neither "simple" nor "well established." App. 8, 12. It is instead, as Tenth Circuit Judge Gorsuch called it, "the least understood" area of dormant Commerce Clause jurisprudence. *Energy & Env't Legal Inst. v. Epel*, ___ F.3d ___, 2015 WL 4174876, at *3 (10th Cir. 2015); *see also* Lea Brilmayer, Jack

Goldsmith & Erin O'Hara O'Connor, *Conflict of Laws* 377 (7th ed. 2015) (dormant Commerce Clause extraterritoriality jurisprudence is "unsettled and poorly understood"); Katherine Florey, *State Courts, State Territory, State Power: Reflections on the Extraterritoriality Principle in Choice of Law and Legislation*, 84 Notre Dame L. Rev. 1057, 1134 (2009) (dormant Commerce Clause extraterritoriality jurisprudence is a "famously murky and unsettled area of law"); Jack L. Goldsmith & Alan O. Sykes, *The Internet and the Dormant Commerce Clause*, 110 Yale L.J. 785, 789 (2001) ("The scope of the extraterritoriality principle is unclear.").[2] This degree of confusion over a rule of constitutional scope is enough, by itself, to warrant the Court's intervention.

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[2] The history of *this case* belies the notion that a per se rule of invalidity is well established: At least 14 judges agreed with the three-judge panel that the issue demanded the attention of an en banc court before the panel even issued an opinion. That is not the hallmark of a "well established" doctrine – it's the unmistakable sign of a jurisprudential quagmire. *See United States v. Blajos*, 292 F.3d 1068, 1071-72 (9th Cir. 2002) (initial en banc hearing is necessary to resolve intracircuit conflicts).

And despite having gone en banc to sort the issue out, in the recently-decided *Chinatown Neighborhood Ass'n v. Harris*, ___ F.3d ___, 2015 WL 4509284 (9th Cir. 2015), the Ninth Circuit panel intimated, in the space of two paragraphs, both that *any* state law regulating activity wholly outside the enacting state is per se unconstitutional, *id.* at *6 (citing this case), and that *Healy* applies only to price control regimes, *ibid.* (citing *Canards et d'Oies*, 729 F.3d at 951). *But see* App. 41 (calling for en banc review in this case precisely to decide which of those two distinct rules to apply in an extraterritoriality challenge).

There is more: A rule that demands the reflexive invalidation of a state law solely because it applies to conduct "wholly outside" the state is simply a bad rule. The courts that have adopted a strictly territorial rule of invalidity have done so based on language in *Healy* that "is so sweeping" – and so divorced from the core purpose of the dormant Commerce Clause – "that most commentators have assumed that [it] cannot mean what [it] appear[s] to say." Florey, *supra*, at 1090. Literally applied, because *Healy* invalidates *every* statute reaching commerce "wholly outside" the enacting state, it is "clearly too broad," Goldsmith & Sykes, *supra*, at 790, and "risk[s] serious problems of overinclusion," defenestrating (for example) "state health and safety regulations that require out-of-state manufacturers to alter their designs or labels[,]" *Energy & Env't Legal Inst.*, 2015 WL 4174876, at *5. And states will have a difficult time knowing in advance whether their laws will satisfy the rule, because a doctrine that forces courts to distinguish between (1) conduct "wholly outside," and (2) conduct partially within a state simply lets in the back door the same arbitrary and unworkable territorialism that the Court long ago heaved out the front. *See, e.g.*, *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977) (dispensing with rigid territorialism in taxing interstate commerce); *see also Allstate Ins. Co. v. Hague*, 449 U.S. 302, 312-13 (1981) (plurality opinion) (same, choice-of-law); *Int'l Shoe Co. v. Washington*, 326 U.S. 310, 316 (1945) (same, personal jurisdiction).

In light of all this, it is no surprise that several parties have, in recent years, asked the Court to revisit its dormant Commerce Clause extraterritoriality jurisprudence. But many of those cases also presented issues that fell indisputably within the scope of the dormant Commerce Clause – *i.e.*, they involved statutes that created trade barriers – and therefore made poor vehicles for the Court to address extraterritoriality. *Compare* Pet. for a Writ of Certiorari at i, *Snyder v. Am. Beverage Ass'n*, No. 12-1221 (Apr. 8, 2013) (seeking review of a dormant Commerce Clause ruling on the basis of extraterritoriality) *with* Conditional Cross-Pet. for a Writ of Certiorari at i, *Am. Beverage Ass'n v. Snyder*, No. 12-1344 (May 10, 2013) (conditionally seeking review of the same ruling on the basis of other dormant Commerce Clause issues).

California's Resale Royalties Act, however, cannot be – and has not been – called protectionist, discriminatory, unduly burdensome on interstate commerce, or any of the other watchwords that *should* raise a dormant Commerce Clause alarm. App. 30-31. The most that can be said of it is that it occasionally requires an entity outside of California – but one that is necessarily doing business with a Californian – to undertake a trivial task, *i.e.*, to withhold 5 percent of the sales price of a Californian's property, and to send that money to someone. But since precisely the same requirements would apply to an entity conducting a sale *within* California, the statute does not place any extra burden on interstate commerce.

By holding unconstitutional a critical portion of a state law on such dubious grounds, the Ninth Circuit managed not to tear down a trade barrier, but instead to punch a hole through a core principle of federalism. It has effectively ended California's experiment with the *droit de suite* – and run roughshod over the state's legislative policy of promoting the arts – for no good reason. *See generally New State Ice Co. v. Liebmann*, 285 U.S. 262, 311 (1932) (Brandeis, J., dissenting) (extolling the virtues, in a federal system, of state-initiated "novel social and economic experiments"). Its judgment, and the rule on which it is based, warrant review. The Court should grant certiorari.

I. THE COURT SHOULD GRANT CERTIORARI TO RESOLVE THE CONFLICT AMONG THE CIRCUITS ON THE ISSUE OF WHETHER THE COMMERCE CLAUSE REQUIRES COURTS TO INVALIDATE A STATE LAW SOLELY BECAUSE IT HAS EXTRATERRITORIAL REACH.

The dormant Commerce Clause exists to prevent states from enacting protectionist measures that benefit their residents at the expense of a national open market. *See Comptroller of Treasury of Md. v. Wynne*, 135 S. Ct. 1787, 1794 (2015); *McBurney v. Young*, 133 S. Ct. 1709, 1719 (2013); *Dep't of Revenue of Ky. v. Davis*, 553 U.S. 328, 337-38 (2008); *Associated Indus. of Mo. v. Lohman*, 511 U.S. 641, 650 (1994); *New Energy Co. of Ind. v. Limbach*, 486 U.S. 269, 273-74 (1988); *Hughes v. Oklahoma*, 441 U.S. 322, 326

(1979). Consequently, there is "a 'virtually *per se* rule of invalidity'" for state laws that discriminate against interstate commerce in favor of intrastate commerce. *United Haulers Ass'n v. Oneida-Herkimer Solid Waste Mgmt. Auth.*, 550 U.S. 330, 338 (2007) (quoting *Philadelphia v. New Jersey*, 437 U.S. 617, 624 (1978)). On the other hand, a non-protectionist state law that only incidentally burdens interstate commerce is presumed constitutional "unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits." *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970).

The question dividing the courts of appeals is whether also to invalidate a state law that is not protectionist – or even excessively burdensome on interstate commerce – just because it applies "to commerce that takes place wholly outside of the State's borders. . . . " *Healy*, 491 U.S. at 336 (internal quotation marks and citations omitted).

A. The First, Tenth, and Eighth Circuits Flatly Reject the Notion That the Extraterritorial Application of a Statute Is Sufficient Reason to Invalidate It.

1. The First Circuit.

The First Circuit recently and explicitly held that a violation of the dormant Commerce Clause requires more than just extraterritoriality. As then-Chief Judge Lynch wrote, in *IMS Health Inc. v. Mills*, 616 F.3d 7, 29 (1st Cir. 2010), *abrogated on other*

grounds sub nom. IMS Health, Inc. v. Schneider, 131 S. Ct. 3091 (2011), "[w]hatever the present scope of the extraterritoriality doctrine, it clearly does not require per se invalidation of *all* extraterritorial applications contained within state statutes regulating commerce."

When Maine empowered its physicians to block data aggregators from selling the physicians' prescribing histories, the aggregators argued, in part, that the Maine law unconstitutionally restricted out-of-state sales of the aggregated data. *IMS Health*, 616 F.3d at 12-14. Upholding Maine's law against that extraterritoriality challenge, the First Circuit observed that this Court has used extraterritoriality only as a basis for invalidating price affirmation laws – and also as a basis for invalidating laws to the extent that they confer a regulatory veto over an out-of-state entity's out-of-state conduct. *Id.* at 30. The First Circuit further observed that, unlike the Maine law, the statutes this Court has invalidated based on extraterritoriality all "raised independent concerns about protectionism under established strands of the dormant Commerce Clause." *Ibid.*; *see also id.* at 43 (Lipez, J., concurring in the judgment) (echoing the point that extraterritoriality alone is insufficient to invalidate a statute).

2. The Tenth Circuit.

In the recently-decided *Energy and Environment Legal Institute v. Epel*, an organization of out-of-state

coal producers claimed that Colorado was unconstitutionally regulating their sales of coal to out-of-state electricity producers, because Colorado – which imports electricity from those producers – requires 20 percent of its electricity to come from renewable sources. 2015 WL 4174876, at *1. The coal producers argued that *Healy* required the Tenth Circuit "to declare 'automatically' unconstitutional any state regulation with the practical effect of 'control[ling] conduct beyond the boundaries of the State.'" *Id.* at *5. The Tenth Circuit rejected that argument, noting that "[w]ithout a regulation more blatantly regulating price and discriminating against out-of-state consumers or producers," it makes no sense to apply a per se rule. *Id.* at *4.

Writing for the panel, Judge Gorsuch analogized dormant Commerce Clause jurisprudence to antitrust law: "As there we find here a kind of 'rule of reason' balancing test" – *Pike* – "providing the background rule of decision with more demanding '*per se*' rules applied to discrete subsets of cases where, over time, the Court has developed confidence that the challenged conduct is almost always likely to prove problematic and a more laborious inquiry isn't worth the cost." *Id.* at *2. Judge Gorsuch then explained that the "discrete subset[ ] of cases" in which a statute's extraterritorial sweep is sufficient to command its per se invalidation is limited to cases like *Healy* itself, *i.e.*, those involving "(1) a price control or price affirmation regulation, (2) linking in-state prices to those charged elsewhere, with (3) the effect of raising costs

for out-of-state consumers or rival businesses." *Id.* at *3. Since the Colorado renewable source rule was none of those things, it survived the coal producers' extraterritoriality challenge.

3. The Eighth Circuit.

In *Southern Union Co. v. Missouri Public Service Commission*, 289 F.3d 503, 508 (8th Cir. 2002), the Eighth Circuit held that the *only* basis for per se invalidity under the dormant Commerce Clause is "discrimination against interstate commerce, or other form of 'economic protectionism'. . . ." Consequently, because it affected in- and out-of-state entities equally, the court upheld a Missouri statute requiring both in- and out-of-state utility companies doing business in Missouri to seek the state's approval before purchasing debt or equity in another utility company (likewise without regard to whether the target company was in- or out-of-state). *Id.* at 505-06, 508.

B. Other Circuits Are Confused About How to Treat Extraterritoriality: The Second Circuit, Admittedly; the Third Circuit, Silently.

1. The Second Circuit.

The Second Circuit has explicitly admitted its confusion about how to treat extraterritoriality under the dormant Commerce Clause: "We have analyzed the extraterritorial effects of state regulations as a form of excessive burden under the *Pike* balancing

test, and also as a basis for per se invalidity. . . . [I]t is not entirely clear from our dormant Commerce Clause precedents which test should apply in this case. . . ." *SPGGC, LLC v. Blumenthal*, 505 F.3d 183, 193 (2d Cir. 2007) (internal citations omitted). *But see Am. Beverage Ass'n*, 735 F.3d at 376 n.7 (noting that a statute's extraterritorial reach – because it isn't a quantifiable burden itself – is not a factor for *Pike* balancing). In the end, rather than deciding how to deal with extraterritoriality under the dormant Commerce Clause, the Second Circuit avoided the issue: It held that a Connecticut statute regulating gift cards did not reach extraterritorially.

2. The Third Circuit.

The Third Circuit hasn't admitted confusion outright, but it has treated extraterritoriality cases inconsistently. For example, in *American Express Travel Related Services, Inc. v. Sidamon-Eristoff*, 669 F.3d 359 (3d Cir. 2012), it began its analysis from the premise that a statute challenged under the dormant Commerce Clause would be subject to heightened scrutiny if protectionist; otherwise it would be subject to *Pike* balancing. That approach left no room at all for a category of per se invalidity based on extraterritorial reach. *Id.* at 372.

Amex's extraterritoriality argument in the case had nothing to do with protectionism: It complained that for uniformity's sake, it would have to charge a fee on traveler's checks nationwide to offset the

effects of a New Jersey law that made it less profitable to sell traveler's checks in New Jersey. *Id.* at 372-73. And if it imposed a fee everywhere, Amex charged, New Jersey would have "dictated commercial activity in other states." *Id.* at 373. Because Amex did not allege protectionism, under the rule it announced, the Third Circuit applied the *Pike* test to an extraterritoriality challenge. *Id.* at 373.

But the Third Circuit had previously used extraterritoriality as a marker of per se invalidity – even as it recognized simultaneously that this Court had only applied such a per se rule in limited categories of cases. *A.S. Goldmen & Co. v. N.J. Bureau of Sec.*, 163 F.3d 780, 785-86 (3d Cir. 1999), *cert. denied*, 528 U.S. 868 (1999). In *A.S. Goldmen*, a New Jersey securities broker argued that New Jersey violated the dormant Commerce Clause by applying its securities law to restrict sales of shares in an out-of-state corporation, made by phone from New Jersey, to an out-of-state buyer – in a state where the sale would not be subject to restriction. *Id.* at 784. But although the Third Circuit announced a per se rule of invalidity in the case, it turned out that the court of appeals had no occasion to apply it: The court determined instead that Goldmen's sale of shares in New York, by phone from New Jersey, was not "wholly outside" New Jersey. *Id.* at 786-87.

C. The Seventh and Sixth Circuits, Like the En Banc Ninth Circuit in This Case, Apply a Rigid Rule of Per Se Invalidity to Any Statute Reaching "Wholly Outside" the Enacting State.

1. The Seventh Circuit.

The Seventh Circuit applies a rule of per se invalidity that turns solely on the extraterritorial reach of a challenged statute. *See Midwest Title Loans, Inc. v. Mills*, 593 F.3d 660, 665 (7th Cir. 2010), *cert. denied*, 562 U.S. 829 (2010) ("[A]nother class of nondiscriminatory local regulations is invalidated without a balancing of local benefit against out-of-state burden, and that is where states actually attempt to regulate activities in other states."); *Dean Foods Co. v. Brancel*, 187 F.3d 609, 616 (7th Cir. 1999) (observing that the Seventh Circuit has "hewed to the per se rule" that "a statute or regulation that violates the extraterritoriality ban is per se invalid").

As a consequence of that rule, the Seventh Circuit held that Indiana could not apply its commercial code to an Illinois car title lender that made loans in Illinois to Hoosiers – even though the lender advertised in Indiana and filed liens in Indiana on collateral located in Indiana. *Midwest Title Loans*, *Inc.*, 593 F.3d at 662-63, 669. And when Indiana argued that the Due Process Clause would allow it to apply its substantive law in a suit between the lender and a Hoosier, the Seventh Circuit held that didn't matter, either: "[I]f the presence of an interest that might support state jurisdiction without violating the due

process clause of the Fourteenth Amendment dissolved the constitutional objection to extraterritorial regulation, there wouldn't be much left of *Healy* and its cognates." *Id.* at 668.

2. The Sixth Circuit.

The Sixth Circuit, after concluding specifically that a challenged Michigan law did *not* "discriminate against interstate commerce," nevertheless held it "'virtually *per se* invalid under the dormant Commerce Clause'" because it "regulates extraterritorial commerce." *Am. Beverage Ass'n*, 735 F.3d at 373 (citation omitted). In the process, like the First and Tenth Circuits, the Sixth Circuit recognized that this Court "has applied the extraterritoriality doctrine only in the limited context of price-affirmation statutes." *Ibid.* Nevertheless, the court held the statute at issue – which required soft-drink manufacturers to mark bottles and cans uniquely for sale in Michigan and subjected the manufacturers to criminal penalties for using the same containers elsewhere – to be extraterritorial in effect and therefore in violation of the dormant Commerce Clause.

Judge Sutton concurred, and while he agreed that the Michigan law ran afoul of a per se rule against extraterritoriality, he wondered: "Is it possible that the extraterritoriality doctrine, at least as a freestanding branch of the dormant Commerce Clause, is a relic of the old world with no useful role to play in the new?" *Id.* at 378 (Sutton, J.,

concurring). After all, the doctrine "has nothing to do with favoritism," as "[e]ven state laws that neither discriminate against out-of-state interests nor disproportionately burden interstate commerce may run afoul of extraterritoriality . . . ." *Ibid.*

Moreover, "[e]liminating extraterritoriality as a freestanding Commerce Clause prohibition also would not eliminate the role of territory in constitutional law." *Id.* at 380. "Territorial limits on lawmaking underlie, indeed animate, many other constitutional imperatives," and "[t]he most powerful of these, due process," already prescribes "limits [on] a State's power to extend its law outside its borders." *Ibid.* Consequently, "[a] law that does not discriminate against interstate commerce, that complies with the traditional requirements of due process and that complies with," *e.g.*, the Full Faith and Credit Clause and the Extradition Clause, "should not be invalidated solely because of an extraterritorial effect." *Ibid.*

* * *

Judge Sutton (and Judge Reinhardt, in this case) recognized that the court of appeals was, pursuant to a doctrine meant to address economic protectionism, invalidating a statute that had nothing to do with protectionism at all. But Judges Reinhardt and Sutton also felt that *Healy* compelled that result. *See id.* at 378 (*Healy* takes extraterritoriality so "seriously" that it can invalidate a statute that "has nothing to do with favoritism"); App. 32. Elsewhere,

however, Judge Gorsuch, Judge Lynch, Judge Lipez, and others, also troubled by the prospect of such an outcome, avoided it by reading *Healy* narrowly. *See, e.g.*, *Energy & Env't Legal Inst.*, 2015 WL 4174876, at *5 (characterizing *Healy*'s broad language as dicta). Still other judges, on other courts – including the en banc majority in this case – have unhesitatingly adopted a broad, per se rule of invalidity. The disarray among the courts in deciding what to do with *Healy* would be reason enough for this Court to issue a writ of certiorari – but it is not the only reason.

II. CERTIORARI IS WARRANTED TO EXTIRPATE A RULE THAT IS DISCONNECTED FROM THE REST OF THE COURT'S COMMERCE CLAUSE JURISPRUDENCE AND CONTRARY TO ITS DUE PROCESS CLAUSE JURISPRUDENCE.

Judge Sutton, Judge Reinhardt, and the others critical of *Healy*'s per se rule are right: Whatever a court is doing when it invalidates a state law solely because of the law's extraterritorial reach, it isn't vindicating any of the concerns that animate the dormant Commerce Clause. *Am. Beverage Ass'n*, 735 F.3d at 378; App. 30.

Judge Sutton is correct also to observe that such an extraterritoriality rule is thus entirely unmoored from any actual constitutional doctrine. It is a rule run amok; nothing but "'a roving license for federal courts to determine what activities are appropriate

for state and local government to undertake.'" *Am. Beverage Ass'n*, 735 F.3d at 380 (quoting *United Haulers Ass'n*, 550 U.S. at 343); *see generally* Donald H. Regan, *Siamese Essays: (I)* CTS Corp. v. Dynamics Corp. of America *and Dormant Commerce Clause Doctrine; (II) Extraterritorial State Legislation*, 85 Mich. L. Rev. 1865, 1887-95 (1987) (attempting to locate a constitutional basis for a strict prohibition on extraterritorial regulation, and not finding one in the Commerce Clause). The courts that have nevertheless followed that rule have had to ignore the scholarly consensus that it is overbroad. *See, e.g.*, Florey, *supra*, at 1090; Goldsmith & Sykes, *supra*, at 789-90, 806. In doing so, those courts, like the Ninth Circuit in this case, purport simply to be following *Healy*. *See* App. 8, 32-33. There is good reason, though, to believe *Healy* does not actually mean what those courts think it means.

First, *Healy* itself provides a clue, in a footnote that must be overlooked by any court reading the case to demand the application of a freestanding, per se prohibition on extraterritoriality: "[T]he critical consideration in determining whether the extraterritorial reach of a statute violates the Commerce Clause" is not simply that the statute has an extraterritorial reach, it "is the overall effect of the statute on both local and interstate commerce." 491 U.S. at 337 n.14. Moreover, the language courts have otherwise taken as *Healy*'s rule was meant only to summarize a series of other dormant Commerce Clause cases, not to announce a new doctrine. *Ibid.*; *see id.* at

336; *see also Brown-Forman Distillers Corp. v. N.Y. State Liquor Auth.*, 476 U.S. 573, 582-83 (1986); *Edgar v. MITE Corp.*, 457 U.S. 624, 642-43 (1982) (plurality opinion); *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511, 521-22 (1935). And as both Judge Gorsuch and Judge Sutton noted, in none of those other cases was a statute's extraterritorial reach the cause of the dormant Commerce Clause problem it presented. *See Energy & Env't Legal Inst.*, 2015 WL 4174876, at *3; *Am. Beverage Ass'n*, 735 F.3d at 380-81 (Sutton, J., concurring). For that matter, an extraterritoriality rule was unnecessary even to decide *Healy* itself, as the Court found simultaneously that the Connecticut statute at issue was discriminatory on its face. *Healy*, 491 U.S. at 340-41; *id.* at 345 (Scalia, J., concurring in part and concurring in the judgment) (observing that the Court's extraterritoriality discussion was "unnecessary to decide the present cases").

Second, in the 16 years since *Healy*, this Court has revisited the issue of dormant Commerce Clause extraterritoriality only once. In that case, *Pharmaceutical Research & Manufacturers of America v. Walsh*, 538 U.S. 644, 669 (2003), the Court had little to say about *Healy* – save to distinguish it from *Walsh* by noting that the latter, unlike the former, had nothing to with price controls. Perhaps *Walsh* was meant to limit the application of any dormant Commerce Clause extraterritoriality rule to cases involving price controls, as some courts, *see, e.g.*, *Energy & Env't Legal Inst.*, 2015 WL 4174876, at *5, and commentators, *see, e.g.*, Brannon P. Denning,

Extraterritoriality and the Dormant Commerce Clause: A Doctrinal Post-Mortem, 73 La. L. Rev. 979, 990-92 (2013), have surmised. If that's true, though, other courts – including the Ninth Circuit in this case – missed the hint.

Third, a broad reading of *Healy* dooms beneficial state laws to per se invalidity after only an assessment – having nothing to do with economic protectionism or commercial interference – of whether the laws apply to conduct occurring "wholly outside" their enacting states. Yet such assessments often prove arbitrary, because it is difficult to fix the locus of an activity that spans multiple states, or even to distinguish "extraterritorial behavior" from "its local effects." *See* Mark P. Gergen, Correspondence, *Territoriality and the Perils of Formalism*, 86 Mich. L. Rev. 1735, 1738 (1988).[3] And arbitrariness, in turn, makes for "bad constitutional law." *Id.* at 1739.

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[3] *See, e.g.*, *Rocky Mountain Farmers Union v. Corey*, 740 F.3d 507, 517-19 (9th Cir. 2014) (M. Smith, J., joined by O'Scannlain, J., Callahan, J., Bea, J., Ikuta, J., and N.R. Smith, J., dissenting from denial of reh'g en banc) (arguing that a California regulation's in-state incentives are functionally the same as out-of-state mandates); *compare Midwest Title Loans, Inc.*, 593 F.3d at 662-63, 669 (Illinoisan's loan to a traveling Hoosier is "wholly outside" Indiana, even though the collateral is in Indiana) *with Quik Payday, Inc. v. Stork*, 549 F.3d 1302, 1308 (10th Cir. 2008), *cert. denied*, 556 U.S. 1209 (2009) (Utahan's loan to Kansan physically located outside of Kansas is nevertheless not "wholly outside" Kansas as long as, *e.g.*, the funds are sent through a Kansas bank); *and A.S. Goldmen & Co.*, 163 F.3d at 786-87 (broker subject to New Jersey securities regulation

(Continued on following page)

Finally, because the Constitution disdains arbitrary rules, *Garfield v. United States ex rel. Goldsby*, 211 U.S. 249, 263 (1908), in a related context, the Court long ago abandoned similarly arbitrary limitations on state power: It has been decades since the Court expunged strict territorialism from its Due Process Clause jurisprudence. *See Allstate Ins. Co.*, 449 U.S. at 312-13 (plurality opinion) (due process allows a state to apply its substantive law in a legal proceeding whenever a party has "a significant contact or [a] significant aggregation of contacts" with the state); *Int'l Shoe Co.*, 326 U.S. at 316 (due process allows a state's courts to assert jurisdiction over a defendant based only on "certain minimum contacts" with the state). Having buried hidebound territorialism in one place, the Court probably did not intend for the concept to reemerge nearby. *See Healy*, 491 U.S. at 336 n.13 (noting that the dormant Commerce Clause's limits on extraterritorial regulation should be "similar" to the Due Process Clause's limits on state court jurisdiction); *cf. Complete Auto Transit, Inc.*, 430 U.S. at 279 (abandoning the formal vestiges of territorialism in favor of a functional method of analyzing taxes levied on interstate commercial activity).

Or, to put it another way: If the Due Process Clause, and the functionalist limitations it places on the states, are already "[t]he most powerful" means

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when brokering, from New Jersey, the sale of shares in a Delaware company to a New Yorker).

of "limit[ing] a State's power to extend its law outside its borders," *Am. Beverage Ass'n*, 735 F.3d at 380 (Sutton, J., concurring), why should the dormant Commerce Clause impose a different, incongruent, and strictly territorial restriction on state laws that otherwise do nothing to contravene the dormant Commerce Clause's purpose?[4] *Cf. Direct Mktg. Ass'n v. Brohl*, 135 S. Ct. 1124, 1134-35 (2015) (Kennedy, J., concurring) (expressing alarm at one particularly expensive result of allowing the dormant Commerce Clause to impose strict territorial limits on states' regulatory authority).

CONCLUSION

Given the strange – the bad – things that can happen when courts apply a rule that broadly prohibits extraterritorial regulation, the circuits are starkly divided as to whether *Healy* actually prescribes such a rule at all. If confusion among and within the circuits over *what* rule to apply were not reason enough for the Court to grant certiorari in this case, there is also the fact that in those circuits that have chosen a

[4] Judge Posner wrote that reading the dormant Commerce Clause coextensively with the Due Process Clause would leave little of *Healy*. *Midwest Title Loans, Inc.*, 593 F.3d at 668. But as this petition explains, perhaps there *should be* little of *Healy*. *See Energy & Env't Legal Inst.*, 2015 WL 4174876, at *3, *5. *See* Regan, *supra*, at 1873 ("In my opinion, extraterritoriality is not a dormant commerce clause problem.").

strict, per se rule, it is anyone's guess *when* the rule will be applied: All turns on the frequently arbitrary determination whether the regulated commerce occurs "wholly outside" the regulating state. Conversely and nonsensically, *nothing* turns on whether the statute at issue actually protects the enacting state's markets – the central concern of the dormant Commerce Clause. As a result, both regulating states and regulated entities are left in the dark about the scope of the states' proper lawmaking authority in our federal system.

This Court should grant certiorari to dispel that confusion and to make clear that *Healy* did not announce a free-standing, per se rule of unconstitutionality based solely on a statute's extraterritorial application.

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FOR PUBLICATION

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

SAM FRANCIS FOUNDATION; ESTATE OF ROBERT GRAHAM; CHUCK CLOSE; LADDIE JOHN DILL, *Plaintiffs-Appellants*, v. CHRISTIES, INC., a New York corporation, *Defendant-Appellee*.	No. 12-56067 D.C. No. 2:11-cv-08605-MWF-FFM

SAM FRANCIS FOUNDATION; ESTATE OF ROBERT GRAHAM; CHUCK CLOSE; LADDIE JOHN DILL, *Plaintiffs-Appellants*, v. EBAY, INC., a Delaware corporation, *Defendant-Appellee*.	No. 12-56068 D.C. No. 2:11-cv-08622-MWF-PLA

ESTATE OF ROBERT GRAHAM; CHUCK CLOSE; LADDIE JOHN DILL, individually and on behalf of all others similarly situated,
Plaintiffs-Appellants,

v.

SOTHEBY'S, INC., a New York corporation,
Defendant-Appellee.

No. 12-56077

D.C. No. 2:11-cv-08604-MWF-FFM

OPINION

Appeals from the United States District Court for the Central District of California, Michael W. Fitzgerald, District Judge, Presiding

Argued and Submitted En Banc December 16, 2014 – Pasadena, California

Filed May 5, 2015

Before: Sidney R. Thomas, Chief Judge, and Harry Pregerson, Stephen Reinhardt, Diarmuid F. O'Scannlain, Barry G. Silverman, Susan P. Graber, M. Margaret McKeown, Marsha S. Berzon, Consuelo M. Callahan, Carlos T. Bea, and Andrew D. Hurwitz, Circuit Judges.

Opinion by Judge Graber; Partial Concurrence and Partial Dissent by Judge Reinhardt; Concurrence by Judge Berzon

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OPINION

GRABER, Circuit Judge:

California's Resale Royalty Act requires the seller of fine art to pay the artist a five percent royalty if "the seller resides in California or the sale takes place in California." Cal. Civ. Code § 986(a). Plaintiffs in these consolidated appeals are artists and the estates of artists. Sitting en banc, we address Plaintiffs' allegation that Defendants – two auction houses and an online retailer – violated the Act by failing to pay mandatory royalties on sales of fine art. Reviewing de novo the district court's order dismissing this action, *Zadrozny v. Bank of N.Y. Mellon*, 720 F.3d 1163, 1167 (9th Cir. 2013), we hold that the Act's clause regulating sales outside the state of California facially violates the "dormant" Commerce Clause but that the offending provision is severable from the remainder of the Act. We return the case to the three-judge panel for its consideration of the additional issues raised by the parties on appeal.

A. *Background*

The Act requires that, "[w]henever a work of fine art is sold and the seller resides in California or the sale takes place in California, the seller or the seller's agent shall pay to the artist of such work of fine art or to such artist's agent 5 percent of the amount of such sale." Cal. Civ. Code § 986(a). The artist's right to the royalty may not be waived or reduced by contract. *Id.* The Act defines "fine art" as "an original painting, sculpture, or drawing, or an original work of art in glass." *Id.* § 986(c)(2). The Act exempts some sales, including those for less than $1,000 and those involving an artist who died before 1983. *Id.* § 986(b).

When art is sold by an agent, "the agent shall withhold 5 percent of the amount of the sale, locate the artist and pay the artist." *Id.* § 986(a)(1). If the seller or the seller's agent cannot locate the artist within 90 days, the seller or agent must transfer the royalty to the California Arts Council. *Id.* § 986(a)(2). In that event, the Arts Council must attempt to locate the artist and deliver the royalty. *Id.* § 986(a)(5). If the artist still has not been located after seven years, the Arts Council may use the funds for "acquiring fine art." *Id.* If the seller or the seller's agent fails to comply with the Act, the artist or the artist's heirs may sue the seller or the seller's agent for the royalty plus reasonable attorney fees. *Id.* § 986(a)(3), (7).

Invoking the royalty provision, Plaintiffs brought three separate class actions against Defendants Sotheby's, Inc., Christie's, Inc., and eBay, Inc., alleging

that Defendants, acting as agents of sellers of fine art, failed to comply with the Act's requirements. Plaintiffs allege that some sales took place in California and that other sales took place outside California but on behalf of a seller who is a resident of California. Defendants moved to dismiss the cases arguing, among other things, that the Act violates the dormant Commerce Clause.

The district court granted Defendants' motions to dismiss. The court held that the Act's regulation of sales outside California is an impermissible regulation of wholly out-of-state conduct, in violation of the dormant Commerce Clause. The court next held that the entire Act must be stricken as unconstitutional, because the invalid portion of the Act could not be severed. The court declined to reach the parties' alternative arguments, such as Defendants' argument that the Act is preempted by federal copyright laws and Defendant eBay's argument that it is neither a seller nor a seller's agent.

Plaintiffs timely appealed, and we consolidated the separate appeals. A three-judge panel heard oral argument last year. But, after argument, the panel directed the parties to file simultaneous briefs setting forth their positions on whether this case should be heard en banc. Thereafter, a majority of nonrecused active judges voted to hear the case en banc.

B. *Dormant Commerce Clause*

The Commerce Clause of the United States Constitution assigns to Congress the authority "[t]o regulate Commerce with foreign Nations, and among the several States." U.S. Const. art. I, § 8, cl. 3. Implicit in this "affirmative grant of regulatory power to Congress" is a "'negative aspect,' referred to as the dormant Commerce Clause." *Conservation Force, Inc. v. Manning*, 301 F.3d 985, 991 (9th Cir. 2002). The dormant Commerce Clause is a "limitation upon the power of the States," *Great Atl. & Pac. Tea Co. v. Cottrell*, 424 U.S. 366, 371 (1976) (internal quotation marks omitted), which "prohibits discrimination against interstate commerce and bars state regulations that unduly burden interstate commerce," *Quill Corp. v. North Dakota*, 504 U.S. 298, 312 (1992) (citation omitted). This principle ensures that state autonomy over "local needs" does not inhibit "the overriding requirement of freedom for the national commerce." *Great Atl. & Pac. Tea Co.*, 424 U.S. at 371 (internal quotation marks omitted).

California's Resale Royalty Act requires the payment of royalties to the artist after a sale of fine art whenever "the seller resides in California *or* the sale takes place in California." Cal. Civ. Code § 986(a) (emphasis added). Defendants challenge the first clause because it regulates sales that take place outside California. Those sales have no necessary connection with the state other than the residency of the seller. For example, if a California resident has a part-time apartment in New York, buys a sculpture in

New York from a North Dakota artist to furnish her apartment, and later sells the sculpture to a friend in New York, the Act requires the payment of a royalty to the North Dakota artist – even if the sculpture, the artist, and the buyer never traveled to, or had any connection with, California. We easily conclude that the royalty requirement, as applied to out-of-state sales by California residents, violates the dormant Commerce Clause.

The Supreme Court has held that "our cases concerning the extraterritorial effects of state economic regulation stand at a minimum for the following proposition[ ]: . . . the Commerce Clause precludes the application of a state statute to commerce that takes place wholly outside of the State's borders, whether or not the commerce has effects within the State." *Healy v. Beer Institt.*, 491 U.S. 324, 336 (1989) (ellipsis and internal quotation marks omitted); *see also id.* (holding that "a statute that directly controls commerce occurring wholly outside the boundaries of a State exceeds the inherent limits of the enacting State's authority and is invalid regardless of whether the statute's extraterritorial reach was intended by the legislature"). Here, the state statute facially regulates a commercial transaction that "takes place wholly outside of the State's borders." *Id.* Accordingly, it violates the dormant Commerce Clause. *See also Valley Bank of Nev. v. Plus Sys., Inc.*, 914 F.2d 1186, 1189-90 (9th Cir. 1990) ("Direct regulation occurs when a state law directly affects transactions that take place . . . entirely outside of the state's borders.

Such a statute is invalid per se. . . .” (citation and internal quotation marks omitted)).

Cases such as *Rocky Mountain Farmers Union v. Corey*, 730 F.3d 1070 (9th Cir. 2013), and *Association des Eleveurs de Canards et d'Oies du Quebec v. Harris*, 729 F.3d 937 (9th Cir. 2013), do not apply here. Unlike this case – which involves regulation of wholly out-of-state conduct – *Corey* and *Harris* concerned state laws that regulated *in-state conduct* with allegedly significant out-of-state practical effects. *See Corey*, 730 F.3d at 1080 (California's imposition of a low-carbon fuel standard, which applied to fuels “consumed *in California*” (emphasis added)); *Harris*, 729 F.3d at 941-43 (California's ban on the *in-state* sale of certain types of foods, including foie gras made by the plaintiffs).

Nor do cases that concerned the validity of state-imposed *taxes*, such as *Quill Corp.*, 504 U.S. 298, and *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977), control here. The rules applied in those cases do not govern because the Act does not impose a tax; it regulates conduct among private parties. The Act requires the seller or the seller's agent to pay a royalty *to the artist*, a private party, not to the government. Cal. Civ. Code § 986(a). The Act even spells out additional procedural requirements for agents of sellers: “the agent shall withhold 5 percent of the amount of the sale, locate the artist and pay the artist.” *Id.* § 986(a)(1). The agent must withhold the royalty, undertake affirmative efforts to locate the artist and, once found, pay the artist. Nothing of the

sort is required by an ordinary tax law, such as those at issue in *Quill Corp.* and *Complete Auto.*[1]

It matters not that, in some circumstances, the royalty amount eventually may wind up, through a form of escheat, in a special fund of the State's coffers. If the seller or the agent withholds the royalty, attempts unsuccessfully to locate the artist, remits the royalty to the Arts Council after 90 days, and if the Arts Council attempts unsuccessfully to locate the artist for seven years, only then does "the right of the artist terminate[ ]," and an amount equal to the royalty may be used by the Arts Council to purchase fine art. *Id.* § 986(a)(5). That contingent consequence seven-and-a-quarter years after the sale does not change the fact that the Act directly regulates the conduct of the seller or the seller's agent for a transaction that occurs wholly outside the State. Accordingly, *Healy* governs. Under *Healy*, the Act's clause regulating out-of-state art sales where "the seller resides in California," Cal. Civ. Code § 986(a), and no other connection to California need exist, violates the

[1] For the same reasons, we reject the partial concurrence's assertion that the Act is "only a minor regulation of the proceeds." Partial concurrence at 17. The Act requires the seller or the seller's agent affirmatively to look for the artist and to pay the artist a royalty. If the seller or the seller's agent fails to locate the artist adequately, the artist may sue for damages plus attorney fees. The Act's regulation of the conduct of the seller and the seller's agent is neither "minor" nor a "regulation of the proceeds" alone.

dormant Commerce Clause as an impermissible regulation of wholly out-of-state conduct.

The partial concurrence urges us to impose an artificial limitation – one never urged by any party – on that straightforward holding by limiting it to agents and not deciding the issue with respect to sellers. We decline for the simple reason that the constitutional doctrine that we apply operates without regard to that distinction. Under *Healy*, "the Commerce Clause precludes the application of a state statute to commerce that takes place wholly outside of the State's borders." 491 U.S. at 336 (ellipsis and internal quotation marks omitted). As we explain above, the Act's regulation of out-of-state sales runs afoul of that constitutional rule; accordingly, we must strike that portion of the Act as an impermissible regulation of wholly out-of-state commerce.

The scope of our holding is neither improper nor inconsistent with the Supreme Court's guidance. It is always possible to narrow a holding. For example, we could limit our holding today to agents from New York and reserve the question with respect to agents from, say, Pennsylvania. Or we could limit our holding to corporate agents and reserve the question with respect to natural persons. But, where the constitutional rule applies without regard to those facts, issuing an artificially constrained opinion serves no purpose; indeed, it would confuse the issue and lead to judicial inefficiency. Contrary to the partial concurrence's assertion, we neither "anticipate a question of constitutional law" nor "formulate a rule of

constitutional law." *United States v. Raines*, 362 U.S. 17, 21 (1960); partial concurrence at 19. We merely apply the simple, well established constitutional rule summarized in *Healy*.

C. *Severability*

We next consider whether we may sever the invalid clause – "the seller resides in California or" – from the remainder of the Act. "Severability is . . . a matter of state law." *Leavitt v. Jane L.*, 518 U.S. 137, 139 (1996) (per curiam). In California, courts "look first to any severability clause." *Cal. Redev. Ass'n v. Matosantos*, 267 P.3d 580, 607 (Cal. 2011). Here, the California legislature enacted the following provision:

> If any provision of this section or the application thereof to any person or circumstance is held invalid for any reason, such invalidity shall not affect any other provisions or applications of this section which can be effected, without the invalid provision or application, and to this end the provisions of this section are severable.

Cal. Civ. Code § 986(e). That broadly worded clause covers the situation here. Accordingly, there is "a presumption in favor of severance." *Cal. Redev. Ass'n*, 267 P.3d at 607; *see also Santa Barbara Sch. Dist. v. Superior Court*, 530 P.2d 605, 618 (Cal. 1975) (holding that "a severability clause normally calls for sustaining the valid part of the enactment" (internal quotation marks omitted)).

We must also look to "three additional criteria: The invalid provision must be grammatically, functionally, and volitionally separable." *Cal. Redev. Ass'n*, 267 P.3d at 607 (internal quotation marks omitted). The first two criteria are met easily. After severance, the revised provision reads: "Whenever a work of fine art is sold and . . . the sale takes place in California, the seller or the seller's agent shall pay to the artist of such work of fine art or to such artist's agent 5 percent of the amount of such sale." Cal. Civ. Code § 986(a) (severed clause replaced with ellipsis). Grammatical separability exists because "the invalid part[ ] can be removed as a whole without affecting the wording or coherence of what remains"; the revised provision above is perfectly coherent.[2] *Cal. Redev. Ass'n*, 267 P.3d at 607 (internal quotation marks omitted). Similarly, there is functional separability because "the remainder of the statute is complete in itself." *Id.* at 608 (internal quotation marks omitted). The revised provision has a reduced scope,

[2] If we adopted the partial concurrence's approach, the grammatical separability test almost certainly would fail, and we would be required to invalidate the Act in its entirety. The partial concurrence refutes that conclusion by citing an earlier California Supreme Court case that purportedly does not require grammatical separability. Partial concurrence at 22-23 n.9 (citing *People v. Kelly*, 222 P.3d 186 (Cal. 2010)). Because the latest California Supreme Court precedent plainly requires grammatical separability, though, we apply that test. *See also Vivid Entm't, LLC v. Fielding*, 774 F.3d 566, 574-75 (9th Cir. 2014) (applying the grammatical separability test from *California Redevelopment Ass'n*).

of course, because it applies only to in-state sales; but it is complete, has coherent functionality, and does not conflict with any of the Act's other provisions.

The volitional separability test, although not facially obvious, also is met. We conclude that "the remainder [of the statute] would have been adopted by the legislative body had [it] foreseen the partial invalidation of the statute." *Id.* (internal quotation marks omitted). Indeed, we think that the legislature *actually* foresaw the partial invalidation of the statute. In detailed letters to the bill's legislative sponsor and to the governor, while deliberations were underway and before the Act's passage, legislative counsel explained that the law's "application to sales which occur outside of the State of California" would violate the Commerce Clause. But, counsel opined, the law "would be valid . . . as to sales which occur in California." Despite those warnings, the enacted version of the law included regulation of both in-state sales and out-of-state sales in easily separable clauses. Perhaps most tellingly, the enacted version also added the severability clause, which expressly states the legislature's intent that "the provisions of this section are severable" if "any provision of this section or the application thereof to any person or circumstance is held invalid for any reason." Cal. Civ. Code § 986(e). We find no reason to deviate from the "presumption in favor of severance." *Cal. Redev. Ass'n*, 267 P.3d at 607.

D. *Conclusion*

California Civil Code section 986 regulates out-of-state and in-state sales of fine art. We hold that the provision regulating out-of-state sales violates the dormant Commerce Clause but that the provision is severable from the remainder of the Act. Because the district court held that the Act fell in its entirety, the court did not reach Defendants' alternative arguments. We return this case to the three-judge panel for its consideration of the remaining issues. We leave to the panel's discretion the decision whether to address those issues on the merits or to remand them for the district court's determination in the first instance.

REMANDED to the three-judge panel.

REINHARDT, Circuit Judge, concurring in part and dissenting in part.

In 1976, California passed the California Resale Royalty Act (the Act) – a law that, for the last 39 years, has secured invaluable benefits for talented artists. The Act requires that when a fine art sale takes place in California or the seller of the art (sometimes referred to in this opinion as the owner) resides in California, the seller or the seller's agent must pay a five-percent royalty to the artist. Cal. Civ.

Code § 986(a).[1] Under the Act, when a wealthy collector of modern art purchases for several million dollars a work of art that the prior owner bought for a minimal amount from a then-unknown young artist, the now-well-known artist will for the first time receive a measure of reasonable compensation for the art that he created.[2]

In the case before us, the defendants who challenge the statute are not the seller, the buyer, or even the artist, but two New York auction houses who under the Act are the sellers' agents.[3] The Act imposes certain duties on them with respect to the disbursement of the royalty payments. The auction houses argue that because the Act imposes those duties in connection with art sales that take place outside of

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[1] The statute contains various exceptions. *See* Cal. Civ. Code § 986(b). It does not apply, for example, to resales after the death of the artist, *id.* § 986(b)(3), unless the artist died after January 1, 1983, in which case "the rights and duties created under [the Act] shall inure to his or her heirs, legatees, or personal representative, until the 20th anniversary of the death of the artist," *id.* § 986(a)(7).

[2] Of course, the compensation the artist receives is by no means excessive. If a painting sells for $1 million, the artist does not become a millionaire; he receives $50,000, while the individual who was wise enough to purchase the painting originally retains $950,000.

[3] The third defendant, eBay, is not an "agent" within the meaning of the Act, and is therefore not subject to the Act. *Cf.* Cal. Att'y Gen. Op. No. 02-111 (2003) ("eBay does not act as an 'agent' for either the seller or buyer during the auction bidding process." (citing Cal. Civ. Code § 2295)).

California, it violates the dormant Commerce Clause.[4] I agree that, for better or worse, the majority is compelled to conclude that, under the Supreme Court's dormant Commerce Clause jurisprudence, the out-of-state regulation of out-of-state entities is unconstitutional and that, as a result, the auction-house defendants cannot be subjected to the obligations required of them in connection with sales that take place outside of California. That, however, has little to do with the fundamental purpose and operation of the Act, or with the majority's unwarranted extension of the dormant Commerce Clause to declare a substantial portion of the Act unconstitutional – specifically, the portion that obligates Californians to pay to the creators of the work of art a small part of the proceeds from the fine art that they sell at a profit regardless of where the actual sale takes place.

It is unfortunate that the majority goes far beyond deciding the constitutionality of the Act as applied to the out-of-state auction-house defendants. It decides a question entirely unnecessary to the resolution of this case when it holds the Act unconstitutional as applied to California art owners who ultimately receive proceeds from out-of-state sales and are then responsible for the payments to the artists. The majority does so despite the fact that no California art owners are a party to the case, and despite the fact that we could and should affirm the

[4] The defendant auction houses in this case are Christie's, Inc., and Sotheby's, Inc.

district court's grant of the auction-house defendants' motion to dismiss on far narrower constitutional grounds.

To make matters worse, the majority not only decides an unnecessary, highly disputable question regarding California art owners, but it decides it incorrectly. Indeed, I strongly disagree with the majority that Californians who sell their art by means of out-of-state transactions may not be required by California law to remit a portion of the proceeds they ultimately receive to the artists who created the works of art. If I found it necessary or even permissible to reach this issue, I would hold that the Act as applied to California art owners is not an extraterritorial regulation. In fact, the California statute represents only a minor regulation of the proceeds received from art sales by a small number of wealthy Californians.[5] It in no way regulates the actual extraterritorial *sales*. Indeed, it in no way affects such sales, but only imposes on Californians

[5] The majority takes exception to my characterization of the Act as constituting only a "minor regulation of the proceeds." *See* Majority Op. at 10 n.1. Although I disagree with the majority's view that requiring wealthy art owners to remit a five-percent royalty payment from profitable art sales to the artists of the works sold is more than "minor," that disagreement is entirely immaterial to the legal issue before us: whether the Act, as-applied to California art owners, regulates out-of-state transactions and thus violates the dormant Commerce Clause.

who dispose of their art for profit[6] an obligation to remit a small part of the proceeds to a third party *after* the transaction has been completed. Moreover, unlike in the Court's extraterritorial regulation cases under the dormant Commerce Clause, the Act does not regulate the price or terms of sales in other states, nor require Californians whose art is sold out-of-state, or the buyers of such art, to seek regulatory approval in California before the institution or completion of such sales. For the above reasons, I dissent from the majority opinion to the extent that it holds the Act unconstitutional as applied to the actions of a California owner whose work of art is sold out-of-state.

As to the only question it is necessary for the court to answer – the application of the Act to out-of-state "agents" of California art sellers whose business is to sell art whether its owners are in-state or out-of-state residents – this case presents an entirely different legal question. That question is whether under the dormant Commerce Clause a California law may impose duties on out-of-state business entities that engage in out-of-state transactions. The defendant auction houses that sell the art work of Californians and the residents of numerous other states are New York entities engaged in the business of selling art primarily in New York. That the defendants are

[6] The Act does not apply "[t]o the resale of the work of fine art for a gross sales price less than the purchase price paid by the seller." Cal. Civ. Code § 986(b)(4).

called agents of the owners of the art work is, for purposes of the dormant Commerce Clause, of no legal significance. The Supreme Court's current case law requires us to hold unconstitutional the requirement by state laws that out-of-state entities take or refrain from taking actions outside of the regulating state. The California statute does just that. Therefore, although I have serious doubts that this aspect of the Supreme Court's dormant Commerce Clause jurisprudence is wise, I reluctantly concur in the majority's judgment that the Act is not constitutional as applied to the imposition of obligations on out-of-state agents (i.e., professional sellers of art, including the auction houses) of California art owners with respect to sales that are conducted outside of California.

I. California Art Owners

A. The Majority's Unnecessary and Improper Decision

The Supreme Court has made clear that we are "bound by two rules . . . : one, never to anticipate a question of constitutional law in advance of the necessity of deciding it; the other, never to formulate a rule of constitutional law broader than is required by the precise facts to which it is to be applied." *United States v. Raines*, 362 U.S. 17, 21 (1960) (citation

and internal quotation marks omitted).[7] By deciding a constitutional question entirely unnecessary to the resolution of this case, the majority flagrantly violates both of these rules.

We have before us two lawsuits in which the defendants are out-of-state auction houses that acted as agents in New York for California art owners. They have moved to dismiss lawsuits filed against them as a result of their alleged noncompliance with the Act. We may affirm the district court's grant of the defendants' motions to dismiss by simply holding that the Act is unconstitutional as applied to the out-of-state agents. We need do no more, and under *Raines*, we therefore *must* do no more. By striking down not only the Act's out-of-state applications to the two out-of-state agents, but also its applications to the in-state

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[7] *See also New York v. Ferber*, 458 U.S. 747, 768 (1982) ("By focusing on the factual situation before us, and similar cases necessary for development of a constitutional rule, we face 'flesh-and-blood' legal problems with data 'relevant and adequate to an informed judgment.' " (footnotes omitted)); *Broadrick v. Oklahoma*, 413 U.S. 601, 610-11 (1973) ("[U]nder our constitutional system courts are not roving commissions assigned to pass judgment on the validity of the Nation's laws. Constitutional judgments . . . are justified only out of the necessity of adjudicating rights in particular cases between the litigants brought before the Court. . . ." (citations omitted)).

The above principles, of course, do not apply to the First Amendment overbreadth doctrine, under which the Supreme Court has "allowed persons to attack overly broad statutes even though the conduct of the person making the attack is clearly unprotected and could be proscribed by a law drawn with the requisite specificity." *Ferber*, 458 U.S. at 769.

actions of California art owners who receive money from out-of-state sales, the majority opinion goes far beyond what is necessary to decide the case. Indeed, it decides a constitutional question regarding the application of the dormant Commerce Clause to California residents that is both highly disputable and wholly unprecedented. In doing so, the majority formulates a constitutional rule far broader than is necessary to decide this case, in direct contravention of *Raines*.

The justification the majority puts forth for not narrowing its constitutional decision is plainly insufficient. The majority "decline[s]" to narrow its decision "for the simple reason that the constitutional doctrine that we apply operates without regard to" the distinction between out-of-state agents and in-state sellers. Majority Op. at 11. Here, the majority "simply" assumes the answer to the fundamental question in this case – whether the imposition of obligations on out-of-state agents conducting business outside of the regulating state is constitutionally indistinguishable from that state's regulation of monetary proceeds received by its own residents. However one may ultimately resolve that question, it is at least clear that it is a highly controversial one on which we lack clear precedent. When such a question

exists, but it is not necessary to decide it in the case before us, *Raines* is clear: we must *not* decide it.[8]

There is no other justification for the majority's decision to disregard Supreme Court precedent and decide an unnecessary constitutional issue. That the defendants have asked us to decide a broader question that does not affect them is no excuse for such an unnecessary constitutional holding. Nor is the majority's approach justified by the fact that the district court relied on broader reasoning than is necessary to grant the motions to dismiss. "We may affirm a district court's judgment on any ground supported by the record, whether or not the decision of the district court relied on the same grounds or reasoning we adopt." *Atel Financial Corp. v. Quaker Coal Co.*, 321 F.3d 924, 926 (9th Cir. 2003). The majority has simply decided an unnecessary constitutional question

[8] In contrast to the distinction between out-of-state agents and in-state sellers, the hypothetical distinctions offered by the majority – between New York agents and Pennsylvania agents, and between corporate agents and natural persons – obviously do not present highly controversial questions relevant to this case; indeed, they do not present *any* questions relevant to this case, and thus would provide no basis for narrowing the decision. The majority's hypothetical distinctions, unlike the differences that lie at the heart of the constitutional question that divides us, are, for all purposes, as irrelevant as the brown-cow/spotted-cow distinction about which most first-year law students learn during their first week's class attendance, even at the law school that the majority opinion's author and I attended.

without any need or cause to do so, in blatant disregard of the Supreme Court's instructions to the contrary.[9]

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[9] The majority is incorrect that the limited approach that *Raines* requires would, if applied here, compel the invalidation of the entire Act. *See* Majority Op. at 13 n.2. To the contrary, under California law, were we to hold the statute unconstitutional *as applied* to the defendants "the appropriate remedy . . . is to disapprove, or disallow, *only the unconstitutional application* of [the Act], thereby preserving any residuary constitutional application with regard to the other provisions of the [Act]." *People v. Kelly*, 222 P.3d 186, 213 (Cal. 2010). The Act's severability clause expressly provides that "[i]f any . . . *application* [of the Act] to any person or circumstance is held invalid for any reason, such invalidity shall not affect any other provisions or applications of [the Act] which can be effected, without the invalid . . . application . . . ." Cal. Civ. Code § 986(e) (emphasis added). "A severability clause, although not conclusive, 'normally calls for sustaining the valid part of the enactment . . . . The final determination depends on whether "the remainder . . . is complete in itself and would have been adopted by the legislative body had the latter foreseen the partial invalidation of the statute."'" *Walnut Creek Manor v. Fair Emp't & Hous. Comm'n*, 814 P.2d 704, 717 (Cal. 1991) (citation omitted) (internal quotation marks omitted). These requirements are clearly met in this case, as all of the duties imposed by the Act on agents are imposed in the alternative on California art owners. Indeed, after holding the Act unconstitutional as applied to the defendants, all of the duties imposed by the Act in connection with out-of-state sales would be fully "effected," as they would simply fall on California art owners alone, and all could be performed in California following the receipt of the proceeds by those owners. As to what the legislature would have done, even the majority acknowledges that it would have adopted the Act regardless of its partial invalidation.

The majority also protests that the application of the *Raines* requirement would fail the grammatical separability test. The

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B. The Act Is Not Extraterritorial As Applied to Californians

Although the majority should not have reached the issue whether the Act is constitutional as applied to the conduct of California art owners, it compounded its error by deciding it incorrectly. The Supreme Court has explained that "the 'Commerce Clause . . . precludes the application of a state statute to commerce that takes place wholly outside of the State's borders, whether or not the commerce has effects within the state.'" *Healy v. Beer Inst.*, 491 U.S. 324, 336 (1989) (citation omitted). From this principle, the majority concludes that the Act must fall as to Californians who arrange for the sale of their art in New York or other states outside of California. Its rationale is that requiring Californians to give the

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grammatical separability requirement exists, however, only when we sever invalid *portions* of a statute, as the majority mistakenly does. *See Cal. Redev. Assn. v. Matosantos*, 267 P.3d 580, 607 (Cal. 2011) (applying that requirement when determining "whether the invalid *portions* of a statute can be severed" (emphasis added)). In contrast, the limited approach that is required here would not invalidate any *portions* of the Act, but would rather hold only that its *application in particular circumstances* is unconstitutional, as the court did in *Kelly* and *Walnut Creek*. No grammatical separability requirement applies in California when a court holds a statute unconstitutional as applied in particular circumstances, as no words of the Act must be stricken in doing so. *See Walnut Creek*, 814 P.2d at 716. Indeed, neither *Kelly* nor *Walnut Creek* applied the grammatical separability requirement, despite the fact that such requirement preceded those cases in California law. *See Calfarm Ins. Co. v. Deukmejian*, 771 P.2d 1247, 1256 (Cal. 1989).

artists a portion of the proceeds they receive from out-of-state sales of the art they created "facially regulates a commercial transaction that 'takes place wholly outside of the State's borders.'" Majority Op. at 9 (quoting *Healy*, 491 U.S. at 336). Contrary to the majority, were we permitted to resolve this question I would hold that the Act's requirement that California art owners remit to the original artist a portion of the proceeds they receive from art sales is not in any respect a "regulat[ion of] a commercial transaction." In my view, what the Act regulates is the use of the money that Californians ultimately receive from the transaction – not the transaction itself, and certainly not any out-of-state transaction.

Nowhere in its opinion does the majority explain *how* requiring Californians to remit a small percentage of the proceeds they ultimately receive from an out-of-state sale of art constitutes "regulat[ing] a commercial transaction," let alone a "commercial transaction that 'takes place wholly outside of the state's borders.'" In fact, the Act in no way regulates the sale.[10] With respect to Californians whose art is sold out of state, the Act operates only after the transaction is completed, just as it does in the case of

[10] In this section, I assume that the obligations placed on out-of-state agents by the Act are stricken, and *all* of the proceeds from the sale are transmitted to the California seller. Under this assumption, it is the Californian and not the agent who has the obligation to remit a small royalty payment to the artist.

art sold in-state. In both cases, the Act deals solely with the income received by Californians – a clearly permissible subject of California's regulatory authority. The Act tells Californians only that when they receive profits from a sale of fine art, they must comply with the obligations the law places on them. As applied to Californians, the Act is plainly a regulation of Californians' in-state obligations – not a regulation of out-of-state entities, and not a regulation of out-of-state transactions. In sum, the Act is simply a regulation of the proceeds that Californians have received from the sale of art, regardless of where the sale takes place.

My conclusion is further supported by the Court's cases that strike down laws as having an impermissible extraterritorial reach. In all such cases, the laws at issue have had a direct effect on out-of-state commercial transactions by regulating the price or terms of such transactions, *see, e.g.*, *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511 (1935), or by otherwise requiring "an out-of-state merchant to seek regulatory approval in one State before undertaking a transaction in another," *Healy*, 491 U.S. at 337 (citation omitted); *Brown-Forman Distillers Corp. v. New York State Liquor Auth.*, 476 U.S. 573 (1986); *Edgar v. MITE Corp.*, 457 U.S. 624, 641-43 (1982) (plurality opinion). The Act, as applied to California art owners, is far different. It does not in any respect affect out-of-state actors or their transactions. Indeed, nothing in the Act dictates the price that a California art seller may charge when selling art outside of the state, and

California does not impose any preconditions whatsoever on sales by Californians who wish to dispose of their art out-of-state. The Court's cases striking down state laws as extraterritorial regulations simply do not apply.

If we were permitted to reach this issue, I would uphold the Act as applied to Californians who sell their art in-state or out-of-state, in this country or elsewhere. I would hold that the Act's requirement that Californians pay to the artists a portion of the proceeds they receive as a result of the sale of their art does not violate the dormant Commerce Clause.

II. Out-of-State Agents of California Art Owners

The constitutionality of the Act as applied to out-of-state agents of California art sellers presents a far different constitutional question. In an attempt to make the Act more effective, the legislature provided that whenever fine art is sold by an agent of a Californian – even if the agent is not a Californian, and even if the sale takes place outside of California – "the agent shall withhold 5 percent of the amount of the sale, locate the artist and pay the artist." Cal. Civ. Code § 986(a)(1). The agents that the law contemplates are primarily major auction houses, such as defendants Christie's and Sotheby's, which, along with major auction houses in other countries, have the ability and experience to obtain the widest buyer pool and the highest prices for the sale of fine art.

They also have the resources necessary to locate artists all over the world and to comply with the terms of the Act by remitting to them a portion of the proceeds. By relying on major auction houses to locate and pay artists, however, the Act imposes obligations on out-of-state entities with respect to transactions that occur outside of California. That obligation is a part of the transaction they conduct, and their role in that transaction is not completed until they have disbursed a portion of the funds they have received to the artist when he can be located.

Unlike the obligations imposed by the Act on Californians after they receive monetary proceeds from the sale of their art regardless of where it is sold, it cannot be said that the Act's imposition of special obligations on out-of-state agents for out-of-state transactions represents a regulation solely of the actions of the residents of the regulating state. Nor can it be said that as applied to out-of-state agents this case is a "practical effects" case – i.e., a case concerning an intrastate regulation with possibly significant practical effects on out-of-state commerce. Majority Op. at 9. Instead, as applied to the actions of out-of-state agents in conducting a sale of art outside of California, the Act *directly* applies "to commerce that takes place wholly outside of the State's borders," and is therefore *per se* invalid under the Court's dormant Commerce Clause jurisprudence. *Healy*, 491 U.S. at 336 (citation omitted); *see also Valley Bank v. Plus System, Inc.*, 914 F.2d 1186, 1190 (9th Cir. 1990).

I have serious doubts that such a *per se* rule is wise as a matter of policy or that it is within the purview of the dormant Commerce Clause as properly framed. The Supreme Court has explained that the "crucial inquiry" under the dormant Commerce Clause is whether the law at issue is "a protectionist measure, or whether it can fairly be viewed as a law directed to legitimate local concerns." *City of Philadelphia v. New Jersey*, 437 U.S. 617, 624 (1978); *see also McBurney*, 133 S. Ct. at 1719 ("Our dormant Commerce Clause jurisprudence . . . is driven by a concern about 'economic protectionism – that is, regulatory measures designed to benefit in-state economic interests by burdening out-of-state competitors.'" (citation omitted)). In its extraterritoriality cases, however, the Court neglects this central concern of the dormant Commerce Clause. Indeed, the Court's requirement that we invalidate all state laws that apply extraterritorially "has nothing to do with favoritism. Even state laws that neither discriminate against out-of-state interests nor disproportionately burden interstate commerce may run afoul of extraterritoriality . . . ." *American Beverage Ass'n v. Snyder*, 735 F.3d 362, 378 (6th Cir. 2013) (Sutton, J., concurring).

This case is one such example. The Act imposes obligations on out-of-state entities not to serve any protectionist purpose, but rather to make the law's valid requirement that Californians remit a portion of the proceeds they receive from art sales more effective. It does not provide any incentive for auction

houses to sell the art of Californians relative to other states' residents, nor does it impose more stringent regulations on out-of-state auction houses than it does on California auction houses. The Act, in short, is simply not the type of law to which the Court's dormant Commerce Clause jurisprudence is primarily aimed; it in no way provides an advantage to California residents or discriminates against out-of-state businesses, and it serves a clearly legitimate local goal – strengthening an in-state regulation benefitting the arts.

Circuit courts in recent years have been compelled by the Court's extraterritoriality doctrine to invalidate other state laws that serve no protectionist purpose whatsoever and that further clearly legitimate state goals, for the sole reason that they apply to out-of-state conduct directly. Michigan, for example, promoted recycling by requiring consumers for each beverage container purchased to pay a ten-cent deposit that is redeemable upon returning an empty container. *Id.* at 366 (majority opinion). In order to prevent the fraudulent redemption of ten cents for a container not purchased in Michigan, the state passed a law requiring that containers sold in Michigan bear a unique mark, and that the unique mark used on Michigan containers not be used on containers sold in other states. *Id.* at 367. Although the Sixth Circuit concluded that the law does not discriminate against interstate commerce in any manner, *id.* at 370-73, it held that the law's unique-mark requirement was extraterritorial in violation of the dormant

Commerce Clause because it regulated the marks on containers sold in other states, *id.* at 373-76. Like its Big Ten rival (though surely not its primary one) to the north, Indiana also had a laudable goal when it sought to protect its residents from predatory lending. It did so by subjecting all loan companies that advertise in Indiana and enter into a loan transaction with a resident of Indiana – irrespective of whether the loan company operates in Indiana – to Indiana lending regulations. *Midwest Title Loans, Inc. v. Mills*, 593 F.3d 660, 662-63 (7th Cir. 2010). Despite the fact that this law, like the Michigan unique-mark law, did not discriminate against or disadvantage out-of-state companies, *id.* at 665, the Seventh Circuit – correctly under the Supreme Court's cases – held that the law's application to an Illinois loan company violated the dormant Commerce Clause, *id.* at 665-69.

It is unfortunate that Supreme Court jurisprudence compels our Court in this case, and has compelled our fellow circuit courts in others, to invalidate the extraterritorial application of such innocuous and beneficial state laws. I suspect that, in our increasingly interconnected country, we will continue to see efforts from states to further legitimate local goals even though, in some respects, they may directly affect conduct outside of their borders. Some efforts may well intrude on the autonomy of other states, and federal courts may be forced to intercede. I have serious doubts, however, that we should invalidate *every* state law that applies to out-of-state conduct. In short, I would hope that, given the numerous changes

in commerce that have recently occurred, the Supreme Court would reconsider whether the *per se* rule it articulated in *Healy* remains a necessary aspect of our dormant Commerce Clause jurisprudence.

In the meantime, I regret that my colleagues in the majority have extended the extraterritoriality doctrine far beyond where it has ever previously been invoked by invalidating the California Resale Royalty Act not only as it applies to out-of-state agents who conduct out-of-state auctions or sales, but also as to its provisions that require Californians to pay a royalty to artists following a profitable fine art sale regardless of the site of the sale.

BERZON, Circuit Judge, with whom Circuit Judge PREGERSON joins, concurring in part.

I concur in the majority opinion insofar as it holds the California Resale Royalty Act, Cal. Civ. Code § 986 ("the Act"), unconstitutional as applied to out-of-state art sales conducted by out-of-state agents. As the Act so applied "directly controls commerce occurring wholly outside the boundaries" of California, it violates the dormant Commerce Clause. *Healy v. Beer Inst.*, 491 U.S. 324, 336 (1989); *see also Valley Bank of Nev. v. Plus Sys., Inc.*, 914 F.2d 1186, 1189-90 (9th Cir. 1990).

But I would stop there. The majority opinion, in my view, unnecessarily decides that the Act is unconstitutional as applied to out-of-state art sales

conducted by California residents as well. The partial dissent also reaches this issue, arriving at the opposite conclusion. Yet none of the parties before us are California sellers, nor does the record contain any evidence pertaining to out-of-state sales by California residents. Furthermore, the Act imposes somewhat different obligations on California sellers and sellers' agents. *Compare* Cal. Civ. Code § 986(a) *with id.* § 986(a)(1).

That the Act's requirement that out-of-state agents "withhold 5 percent of the amount of [an out-of-state] sale, locate the artist and pay the artist," *id.*, directly regulates extraterritorial commercial transactions in violation of the Supreme Court's dormant Commerce Clause jurisprudence is clear. It is not so clear to me, however, that the royalty obligations the Act imposes on California sellers similarly regulate commercial *transactions*, as opposed to the post-sale income of Californian residents. But we need not decide the latter question. Indeed, the disagreement between the majority opinion and the partial dissent as to whether the Act "directly regulates the conduct of the seller," Majority Op. at 10-11, or simply "regulat[es] . . . the proceeds that Californians have received from the sale of art," Partial Dissent at 24, illustrates why we should not, in the absence of sufficient information concerning the Act's operation on out-of-state sales by California residents, determine the constitutionality of the Act more generally.

Consequently, I would hold the Act unconstitutional as applied to out-of-state art sales by out-of-state agents, such as the New York auction houses party to this case, and go no further.

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

SAM FRANCIS FOUNDATION; ESTATE OF ROBERT GRAHAM; CHUCK CLOSE; LADDIE JOHN DILL, Plaintiffs-Appellants, v. CHRISTIE'S, INC., a New York corporation, Defendant-Appellee.	No. 12-56067 D.C. No. 2:11-cv-08605-MWF-FFM Central District of California, Los Angeles ORDER (Filed Jul. 16, 2015)

SAM FRANCIS FOUNDATION; ESTATE OF ROBERT GRAHAM; CHUCK CLOSE; LADDIE JOHN DILL, Plaintiffs-Appellants, v. EBAY, INC., a Delaware corporation, Defendant-Appellee.	No. 12-56068 D.C. No. 2:11-cv-08622-MWF-PLA Central District of California, Los Angeles

ESTATE OF ROBERT GRAHAM; CHUCK CLOSE; LADDIE JOHN DILL, individually and on behalf of all others similarly situated, Plaintiffs-Appellants, v. SOTHEBY'S, INC., a New York corporation, Defendant-Appellee.	No. 12-56077 D.C. No. 2:11-cv-08604-MWF-FFM Central District of California, Los Angeles

Before: FERNANDEZ, N.R. SMITH, and MURGUIA, Circuit Judges.

This case is remanded to the district court for further proceedings consistent with the en banc panel's opinion in *Sam Francis Foundation v. Christies, Inc.*, 784 F.3d 1320 (2015).

FOR PUBLICATION

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

SAM FRANCIS FOUNDATION; ESTATE OF ROBERT GRAHAM; CHUCK CLOSE; LADDIE JOHN DILL, Plaintiffs-Appellants, v. **CHRISTIE'S, INC.**, a New York corporation, Defendant-Appellee.	No. 12-56067 D.C. No. 2:11-cv-08605-MWF-FFM **ORDER** (Filed Oct. 30, 2014)

SAM FRANCIS FOUNDATION; ESTATE OF ROBERT GRAHAM; CHUCK CLOSE; LADDIE JOHN DILL, Plaintiffs-Appellants, v. **EBAY, INC.**, a Delaware corporation, Defendant-Appellee.	No. 12-56068 D.C. No. 2:11-cv-08622-MWF-PLA

ESTATE OF ROBERT GRAHAM; CHUCK CLOSE; LADDIE JOHN DILL, individually and on behalf of all others similarly situated, Plaintiffs-Appellants, v. **SOTHEBY'S, INC.**, a New York corporation, Defendant-Appellee.	No. 12-56077 D.C. No. 2:11-cv-08604-MWF-FFM

THOMAS, Circuit Judge:

Upon the vote of a majority of nonrecused active judges, it is ordered that this case be reheard en banc pursuant to Federal Rule of Appellate Procedure 35(a) and Circuit Rule 35-3.

Judges Wardlaw and Nguyen did not participate in the deliberations or vote in this case.

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

SAM FRANCIS FOUNDATION; et al., Plaintiffs-Appellants, v. CHRISTIES, INC., a New York corporation, Defendant-Appellee.	No. 12-56067 D.C. No. 2:11-cv-08605-MWF-FFM Central District of California, Los Angeles ORDER (Filed Aug. 29, 2014)

SAM FRANCIS FOUNDATION; et al., Plaintiffs-Appellants, v. EBAY, INC., a Delaware corporation, Defendant-Appellee.	No. 12-56068 D.C. No. 2:11-cv-08622-MWF-PLA Central District of California, Los Angeles

ESTATE OF ROBERT GRAHAM; et al., Plaintiffs-Appellants, v. SOTHEBY'S, INC., a New York corporation, Defendant-Appellee.	No. 12-56077 D.C. No. 2:11-cv-08604-MWF-FFM Central District of California, Los Angeles

Before: FERNANDEZ, N.R. SMITH, and MURGUIA, Circuit Judges.

Pursuant to General Order 5.4.c.3, the parties are directed to file simultaneous briefing setting forth their respective positions on whether this case should be heard en banc. The parties' briefs shall address whether there is a conflict in our case law regarding the applicability of *Healy v. Beer Inst.*, 491 U.S. 324 (1989). *Compare Rocky Mountain Farmers Union v. Corey*, 730 F.3d 1070, 1101 (9th Cir. 2013) ("[T]he dormant Commerce Clause holds that any 'statute that directly controls commerce occurring wholly outside the boundaries of a State exceeds the inherent limits of the enacting State's authority.'" (quoting *Healy*, 491 U.S. at 336)), *with Ass'n des Eleveurs de Canards et d'Oies du Quebec v. Harris*, 729 F.3d 937, 951 (9th Cir. 2013) ("[T]he [Supreme] Court has held that *Healy* . . . [is] not applicable to a statute that does not dictate the price of a product and does not 't[ie] the price of its in-state products to out-of-state prices.'" (quoting *Pharm. Research & Mfrs. of Am. v. Walsh*, 538 U.S. 644, 669 (2003)).

The parties shall file their briefs on or before September 19, 2014. The parties must file the original supplemental brief plus 50 paper copies.

UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

ESTATE OF ROBERT GRAHAM et al, Plaintiffs, vs. SOTHEBY'S INC., Defendant;	CASE NOS. 2:11-cv-08604-JHN-FFM (Sotheby's) 2:11-cv-08605-JHN-FFM (Christie's) **ORDER GRANTING JOINT MOTION TO DISMISS**
SAM FRANCIS FOUNDATION et al, Plaintiffs, vs. CHRISTIE'S, INC., Defendant;	Judge: Hon. Jacqueline H. Nguyen

This matter comes before the Court on Defendants Sotheby's, Inc. ("Sotheby's") and Christie's, Inc.'s ("Christie's") (collectively, "Defendants") Joint Motion to Dismiss ("Jt. Mot."). (2:11-cv-8604-JHN-FFM, docket no. 17.)[1] The Court has read and considered the briefs filed by the parties in this matter. The Court has also considered the oral argument that took place on March 12, 2012.

[1] All citations to the docket in this opinion are to the 2:11-cv-8604-JHN-FFM docket, unless otherwise stated.

For the reasons herein, the Joint Motion is **GRANTED** with prejudice.

I.

BACKGROUND

Defendants are world-renowned auction houses. Sotheby's is a New York corporation, with its principal place of business in New York. (Sotheby's Compl. ¶ 5; Jt. Mot. 10.) Christie's is also a New York corporation, with its principal place of business in New York. (Christie's Compl. ¶ 6; Jt. Mot. 10.)

On October 18, 2011, Plaintiffs – a collection of artists and their heirs – brought the instant Class Action Complaints (the "Complaints"), alleging that Defendants failed to comply with the California Resale Royalties Act ("CRRA"), Cal. Civ. Code § 986. Specifically, Plaintiffs allege, *inter alia*, that Defendants – acting as the agents for California sellers – sold works of fine art at auction but failed to pay the appropriate resale royalty provided for under the CRRA. (Sotheby's Compl. ¶¶ 9-12.)

On January 12, 2012, Defendants filed a Joint Motion to Dismiss the Complaints, arguing that the Court should strike down the CRRA because it (1) violates the Commerce Clause of the United States Constitution; (2) effects a taking of private property in violation of the United States and California constitutions; and (3) is preempted by the Copyright Act of 1976. (Jt. Mot. 7, 17, 24.) Because the Court

finds that the CRRA "cannot withstand Commerce Clause scrutiny," *Nat'l Collegiate Athletic Ass'n v. Miller*, 10 F.3d 633, 638 (9th Cir. 1993), it need not address Defendants' preemption and Takings Clause arguments.

II.

LEGAL STANDARD

A defendant may seek dismissal of a complaint that "fail[s] to state a claim upon which relief can be granted." Fed. R. Civ. P. 12(b)(6). In evaluating a motion to dismiss, the Court generally cannot consider material outside the complaint, such as facts presented in briefs, affidavits, or discovery materials, unless such material is alleged in the complaint or judicially noticed. *McCalip v. De Legarret*, No. 08-2250, 2008, U.S. Dist. LEXIS 87870, at *4 (C.D. Cal. Aug. 18, 2008); *see also Jacobson v. AEG Capital Corp.*, 50 F.3d 1493, 1496 (9th Cir. 1995). The Court must accept as true all material factual allegations in the complaint and construe them in the light most favorable to the plaintiff. *Nursing Home Pension Fund, Local 144 v. Oracle Corp.*, 380 F.3d 1226, 1229 (9th Cir. 2004). However, this tenet is inapplicable to legal conclusions. *Ashcroft v. Iqbal*, 129 S. Ct. 1937, 1949 (2009). The Court need not accept as true "[t]hreadbare recitals of the elements of a cause of action, supported by mere conclusory statements." *Id.* The Court, based on judicial experience and common

sense, must determine whether a complaint plausibly states a claim for relief. *Id.* at 1950.

III.

DISCUSSION

Defendants argue that by purporting to regulate transactions that take place wholly outside of California, the CRRA violates the Commerce Clause of the United States Constitution. (Jt. Mot. 7); U.S. Const. art. I, § 8, cl. 3. The Court conducts its analysis mindful of the "time-honored presumption" that "[e]very legislative act is to be presumed to be a constitutional exercise of legislative power until the contrary is clearly established." *Reno v. Condon*, 528 U.S. 141, 148 (2000); *Close v. Glenwood Cemetery*, 107 U.S. 466, 475 (1883).

A. The CRRA

The CRRA provides for a *droit de suite*, or resale royalty right, for fine artists. Cal. Civ. Code § 986. The *droit de suite* creates a "continuing remunerative relationship between a visual artist and his creation," by providing the artist with a right to a royalty payment – consisting of a percentage of an original work's resale price – each time the "original, tangible embodiment" of the artist's work is resold. Elliot Alderman, *Resale Royalties in the United States for Fine Visual Artists: An Alien Concept*, 40 J. Copyright Soc'y U.S.A. 265, 267 (1992); 2 Melville B. Nimmer &

David Nimmer, Nimmer on Copyright § 8C.04[A][1] (2011) [hereinafter "Nimmer"].[2]

The CRRA provides that "[w]henever a work of fine art is sold and the seller resides in California or the sale takes place in California, the seller or the seller's agent shall pay to the artist of such work of fine art or to such artist's agent 5 percent of the amount of such sale." Cal. Civ. Code § 986(a). An artist can waive the right to this royalty "only by a contract in writing providing for an amount in excess of 5 percent of the amount of such sale." *Id.* The CRRA excludes any resale where the gross sales price is less than $1,000. *Id.* § 986(b)(2).

The CRRA defines a work of "[f]ine art" as "an original painting, sculpture, or drawing, or an original work of art in glass." *Id.* § 986(c)(2). An "[a]rtist" is defined as "the person who creates a work of fine art and who, at the time of resale, is a citizen of the United States, or a resident of the state who has resided in the state for a minimum of two years." *Id.* § 986(c)(1). Therefore, the CRRA applies to all artists who are U.S. citizens, regardless of the state in which

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[2] The *droit de suite* is best understood as an "attempt to equalize the copyright status of fine artists" with that of authors and composers. Nimmer, § 8C.04[A][1]. For while authors and composers are compensated each time their works are performed or reproduced, visual artists "create one-of-a-kind objects, which cannot be copied," and thus receive their income from a work almost solely from its initial sale. Michael B. Reddy, *The Droit de Suite: Why American Fine Artists Should Have a Right to a Resale Royalty*, 15 Loy. L.A. Ent. L. Rev. 509, 517 (1995).

they reside. Here, for example, Plaintiff Chuck Close resides in New York. (Sotheby's Compl. ¶ 3; Christie's Compl. ¶ 4.)

The CRRA additionally requires the seller's *agent* to effect payment of the resale royalty. Cal. Civ. Code § 986(a)(1). Specifically, the CRRA provides that "[w]hen a work of fine art is sold at an auction or by a gallery, dealer, broker, museum or other person acting as the agent for the seller the agent shall withhold 5 percent of the amount of the sale, locate the artist and pay the artist." *Id.*

If the agent is unable to locate the artist within 90 days, the agent must pay the applicable royalty to the California Arts Council, which is then required to search for the artist for seven years. After that time, if the artist is not located, the funds pass to the California Arts Council for "use in acquiring fine art." *Id.* §§ 986(a)(3), (a)(5). If the seller or the seller's agent fails to pay the appropriate royalty, "the artist may bring an action for damages within three years after the date of sale or one year after the discovery of the sale, whichever is longer." *Id.* § 986(a)(3). The heirs of a deceased artist may assert the artist's rights under the CRRA for 20 years after the artist's death. *Id.* § 986(a)(7). The CRRA excludes any resale for "a gross sales price of less than one thousand dollars ($1,000)" or "a gross sales price less than the purchase price paid by the seller." *Id.* § 986(b)(2), (b)(4).

Although such legislation is common among European nations, including France, Germany and the

United Kingdom, California's passage of the CRRA in 1976 represented the first *droit de suite* legislation in the United States. *See, e.g.*, William Bates, *Royalties for Artists: California Becomes The Testing Ground*, N.Y. Times, August 14, 1977; Alderman at 268-69; Nimmer, § 8C.04[A][1]; The Artist's Resale Right Regulations 2006, 2006 No. 346, available at http://www.legislation.gov.uk/uksi/2006/346/contents/made (last viewed, May 16, 2012); *see also* Judicial Improvements Act of 1990, Pub. L. No. 101-650, § 608(b), 104 Stat. 5089 (1990).

Notably, several attempts by Congress to introduce resale royalty legislation have failed. Reddy at 511; *see also* U.S. Copyright Office, *Droit de Suite*: The Artist's Resale Royalty (1992) [hereinafter "Report"]. In December 1992, the Copyright Office issued a report concluding that it was "not persuaded that sufficient economic and copyright policy justification exists to establish droit de suite in the United States." Report at 149; *see also* Nimmer at § 8C-13. Other states, including New York, have considered similar legislation, but have not adopted any measure creating a resale royalty right for visual artists. (*See, e.g.*, Russell Decl., Ex. 23, at 693-716.)[3]

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[3] According to commentators and news reports, enforcement of the CRRA has been spotty. The *New York Times* recently reported that, since the CRRA was passed in 1977, approximately 400 artists have received a total of $328,000 in resale royalties. Patricia Cohen, *Artists File Lawsuits, Seeking Royalties*, N.Y. Times, Nov. 1, 2011, http://www.nytimes.com/2011/11/02/arts/

(Continued on following page)

B. The Commerce Clause

The Commerce Clause of the United States Constitution states: "The Congress shall have Power . . . To regulate Commerce . . . among the several States . . . ." U.S. Const. art. I, § 8, cl. 3. "Although the Commerce Clause is phrased as an affirmative grant of regulatory power to Congress, the Supreme Court . . . has long interpreted the Clause to have a 'negative aspect,' referred to as the dormant Commerce Clause . . . ." *Conservation Force, Inc. v. Manning*, 301 F.3d 985, 991 (9th Cir. 2002). The Supreme Court's dormant Commerce Clause jurisprudence holds that States do not have the "power [to] unjustifiably . . . discriminate against or burden the interstate flow of articles of commerce." *Id.* (quoting *Or. Waste Sys., Inc. v. Dep't of Envtl. Quality*, 511 U.S. 93, 98 (1994)). The dormant Commerce Clause is thus a "limitation upon the power of the States." *Edgar v. MITE Corp.*, 457 U.S. 624, 640 (1982) (quoting *Great Atl. & Pac. Tea Co., Inc. v. Cottrell*, 424 U.S. 366, 370-71 (1976)). While "not every exercise of state power with some impact on interstate commerce is invalid," a state law must even-handedly regulate to "effectuate a legitimate public interest," and its impact on interstate

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design/artists-file-suit-against-sothebys-christies-and-ebay.html?pagewanted=all (last viewed, January 24, 2012). A 1986 survey of artists conducted by the Bay Area Lawyers for the Arts found that 32% of respondents "said dealers had refused to give them the name or address of the buyer or even the resale price, despite their right under the [CRRA] to assign collection of the royalty to another." Reddy at 523.

commerce must only be "incidental." *Id.* (quoting *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970)).

C. Applicability of the Dormant Commerce Clause

As an initial matter, although Plaintiffs rely heavily upon the Ninth Circuit's decision in *Morseburg v. Baylon*, 621 F.2d 972 (9th Cir. 1980), arguing that it "rejected constitutional challenges brought against the [CRRA]," the Court finds that *Morseburg* does not control here. (Opp'n 1.) *Morseburg* did not involve a dormant Commerce Clause challenge to the CRRA; rather, it involved preemption, Contracts Clause, and due process challenges. *Morseburg*, 621 F.2d at 974-75. Moreover, the *Morseburg* court explicitly stated that its decision "concern[ed] the preemptive effect of the 1909 [Copyright] Act *only*." *Id.* at 975 (emphasis added). As such, the Court addresses the dormant Commerce Clause issue as one of first impression and is not bound by *Morseburg*.[4]

A state statute implicates the dormant Commerce Clause if the activity it regulates could likewise be regulated by Congress. *Manning*, 301 F.3d at

[4] The Court also notes that its decision in *Baby Moose Drawings, Inc. v. Valentine*, No. 11-00697, 2011 WL 1258529 (C.D. Cal. Apr. 1, 2011), a case also involving a challenge to the CRRA, was decided solely on preemption grounds – indeed the parties did not fully brief the issue of whether the CRRA violated the Commerce Clause – and thus is not relevant to the instant dormant Commerce Clause challenge.

993. Thus, the Court must first determine whether the CRRA regulates an activity subject to federal control. *See id.* at 992. The Supreme Court has "identified three broad categories of activity that Congress may regulate under its commerce power." *United States v. Lopez*, 514 U.S. 549, 558 (1995). Congress may regulate (1) the use of the channels of interstate commerce; (2) the instrumentalities of interstate commerce, or persons or things in interstate commerce; and (3) "those activities that substantially affect interstate commerce." *Id.* at 558-59.

1. Works of Fine Art Constitute "Things" in Interstate Commerce

First, the Court finds that where works of fine art are sold from one state into another, each piece of fine art itself constitutes a "thing" in interstate commerce. Therefore, Congress may regulate such transactions under the Commerce Clause. *See Lopez*, 514 U.S. at 558-59.

2. The CRRA Substantially Affects Interstate Commerce

Second, the Court finds that the CRRA substantially affects interstate commerce. One factor that a Court should "consider when evaluating whether a law has a 'substantial effect' on interstate commerce [is] . . . whether the statute has anything to do with 'commerce or any sort of economic enterprise, however broadly one might define those terms.'" *San Luis*

& Delta-Mendota Water Auth. v. Salazar, 638 F.3d 1163, 1174 (9th Cir. 2011) (quoting *Lopez*, 514 U.S. at 561). This factor is surely met. In fact, the Ninth Circuit has specifically described the CRRA as "an *economic* regulation to promote artistic endeavors generally." *Morseburg*, 621 F.2d at 979 (emphasis added).

The Supreme Court has held that Congress may exercise its Commerce Clause power so long as "in the aggregate the economic activity in question would represent a general practice . . . subject to federal control." *Citizens Bank v. Alafabco, Inc.*, 539 U.S. 52, 56-57 (2003) (alteration in original) (quotation marks and citation omitted); *see also San Luis*, 638 F.3d at 1175 ("When a statute is challenged under the Commerce Clause, courts must evaluate the aggregate effect of the statute (rather than an isolated application) . . . ."). When the number of art sale transactions throughout the United States that the CRRA purports to regulate are considered in the aggregate, the Court finds little doubt that the CRRA has a "substantial effect" on interstate commerce such that Congress could regulate the activity. *Citizens Bank*, 539 U.S. at 56-57. Therefore, the Court finds that the dormant Commerce Clause applies to the CRRA.

D. Whether the CRRA Violates the Dormant Commerce Clause

Although the Court has concluded that the CRRA implicates the dormant Commerce Clause, this "does

not answer the question of whether the [CRRA] *violates* the dormant Commerce Clause." *Manning*, 301 F.3d at 995 (emphasis added).

The Supreme Court has "outlined a two-tiered approach" to analyzing state economic regulations under the dormant Commerce Clause:

> When a statute directly regulates or discriminates against interstate commerce, or when its effect is to favor in-state economic interests over out-of-state interests, we have generally struck down the statute without further inquiry. When, however, a statute has only indirect effects on interstate commerce and regulates evenhandedly, we have examined whether the State's interest is legitimate and whether the burden on interstate commerce clearly exceeds the local benefits.

Valley Bank of Nev. v. Plus Sys., Inc., 914 F.2d 1186, 1189 (9th Cir. 1990) (quoting *Brown-Forman Distillers Corp. v. New York State Liquor Auth.*, 476 U.S. 573, 579 (1986)); *see also Miller*, 10 F.3d at 638; *S.D. Myers, Inc. v. City and Cnty. of S.F.*, 253 F.3d 461, 466 (9th Cir. 2001).

Therefore, the Court "must first ask whether the Statute: 1) directly regulates interstate commerce; 2) discriminates against interstate commerce; or 3) favors in-state economic interests over out-of-state interests." *Miller*, 10 F.3d at 638. If it does any of these things, "it violates the Commerce Clause per

se, and we must strike it down without further inquiry." *Id.*

1. The CRRA Violates the Commerce Clause Per Se

The Supreme Court has held that "a statute that directly controls commerce occurring wholly outside the boundaries of a State exceeds the inherent limits of the enacting State's authority and is invalid regardless of whether the statute's extraterritorial reach was intended by the legislature." *Healy*, 491 U.S. at 336. This is so "whether or not the commerce has effects within the state." *Id.* The Ninth Circuit has held that "[s]uch a statute is invalid per se, regardless of whether the state intended to inhibit interstate commerce." *Valley Bank*, 914 F.2d at 1190. The "critical inquiry is whether the practical effect of the regulation is to control conduct beyond the boundaries of the State." *Healy*, 491 U.S. at 336 (quoting *Edgar*, 457 U.S. at 642-43 (1982) (plurality opinion)).

The Court finds that the CRRA explicitly regulates applicable sales of fine art occurring wholly outside California. *See* Cal. Civ. Code § 986(a). Under its clear terms, the CRRA regulates transactions occurring anywhere in the United States, so long as the seller resides in California. *Id.* Even the artist – the intended beneficiary of the CRRA – does not have to be a citizen of, or reside in, California. Cal. Civ. Code § 986(c)(1).

The following example illustrates the CRRA's problematic reach: Assume a California resident places a painting by a New York artist up for auction at Sotheby's in New York, and at the auction a New York resident purchases the painting for $1,000,000. In such a situation, the transaction that the CRRA regulates – the one between the New York auction house and the New York purchaser[5] – occurs wholly in New York. Despite the fact that even the artist receiving the royalty is a New York resident, the CRRA reaches out to New York and regulates the transaction by mandating that Sotheby's (1) withhold $50,000 (i.e., 5% of the auction sale price); (2) locate the artist; and (3) remit the $50,000 to the New York artist. Cal. Civ. Code § 986(a)(1). Should Sotheby's in New York fail to comply, the New York artist may bring a legal action under California law (the CRRA) to recover the applicable royalty. Cal. Civ. Code § 986(a)(3). If the artist cannot be located, Sotheby's must send the money withheld in the transaction to the California Arts Council. *Id.*

California's own Legislative Counsel recognized this problem with the CRRA when the law was being considered in August of 1976. (Russell Decl. Ex. 5, at 32.)[6] In an opinion letter, Legislative Counsel George

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[5] Notably, the CRRA does *not* purport to regulate any potential agreement between a seller and the seller's agent; rather, it solely regulates the actual sale.

[6] The Court received Defendants' Request for Judicial Notice (docket no. 18). The Court grants the Request to take judicial

(Continued on following page)

H. Murphy wrote that "[w]hile the state has a legitimate local interest in furthering the fiscal rights of artists within this state, we find little such interest where the artist resides out of the state or country." (Id.) The Legislative Counsel further advised that the application of the CRRA to "out-of-state sales . . . would be invalid under the commerce clause." (Id. at 31.)

Plaintiffs' reliance on *S.D. Myers* is misplaced. (Opp'n to Jt. Mot. at 12.) In *S.D. Myers*, the Ninth Circuit confronted a wholly different set of facts. There, a San Francisco ordinance required that "contractors with the City provide nondiscriminatory benefits to employees with registered domestic partners." 253 F.3d at 465. An Ohio-based company filed suit, arguing that the ordinance was invalid under, *inter*

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notice of the legislative history of the CRRA, including, *inter alia*, prior versions of the bill, amendments, committee reports, and the written recommendations of the legislative counsel. *See, e.g.*, *Territory of Alaska v. Am. Can Co.*, 358 U.S. 224, 226-27 (1959) (taking judicial notice of, and analyzing, legislative history of a bill); *Chaker v. Crogan*, 428 F.3d 1215, 1223 n. 8 (9th Cir. 2005) (same); *In re Reeves*, 35 Cal. 4th 765, 777 n. 15 (2005) (same). The Court declines to take judicial notice of any other documents as they are unnecessary to this decision.

The Court, however, does not rely upon the judicially noticed documents in reaching its conclusions on the constitutionality of the CRRA. It uses them simply for the purpose of adding context to the analysis, and in considering severability. *See, e.g.*, *Traverso v. People ex rel. Dep't of Transp.*, 46 Cal. App. 4th 1197, 1206, 1209 n. 11 (1996); *People v. Soto*, 51 Cal. 4th 229, 239-40 (2011); *Carter v. Charter Coal Co.*, 298 U.S. 238, 312-17 (1936).

alia, the Commerce Clause. *Id.* at 466. In upholding the statute from the Commerce Clause challenge, the Ninth Circuit relied on the fact that "the Ordinance [would] affect an out-of-state entity only after that entity [had] affirmatively chosen to subject itself to the Ordinance by contracting with the City." *Id.* at 469. The Court found important that the Ordinance was imposed only by an affirmative contract, "rather than by legislative fiat." *Id.*[7]

Here, on the other hand, the Complaints contain no allegation that Defendants affirmatively chose to be governed by California law. Instead, Defendants, both New York corporations, find themselves subject to the law of California by virtue of selling art that is owned by a California seller – even if the transaction takes place wholly in New York, and even if the beneficiary of the 5% royalty is a New York artist. Cal. Civ. Code § 986(c)(1).

For these reasons, the Court finds that the CRRA has the "practical effect" of controlling commerce "occurring wholly outside the boundaries" of California even though it may have some "effects within the State." *Healy*, 491 U.S. at 336. Therefore, the CRRA

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[7] Plaintiffs' reliance on *Gravquick A/S v. Trimble Navigation Int'l Ltd.*, 323 F.3d 1219, 1224 (9th Cir. 2003), is similarly misplaced. There, as in *S.D. Myers*, the Ninth Circuit relied on the fact that the relevant state law applied only "because the parties chose to be governed by California law" in a contract. *Id.* at 1224.

violates the Commerce Clause of the United States Constitution.

E. The Entire Statute Must Fall

Although the CRRA contains a severability provision, the Court nonetheless agrees with Defendants that the offending portions of the CRRA cannot be severed, and thus the entire statute must fall. Cal Civ. Code § 986(e) ("If any provision of this section or the application thereof to any person or circumstance is held invalid for any reason, such invalidity shall not affect any other provisions or applications of this section which can be effected, without the invalid provision or application, and to this end the provisions of this section are severable."); (Jt. Reply 12).

The Supreme Court has held that "a court should refrain from invalidating more of [a] statute than is necessary." *Regan v. Time, Inc.*, 468 U.S. 641, 652 (1984). The established standard for determining severability is: "Unless it is evident that the Legislature would not have enacted those provisions which are within its power, independently of that which is not, the invalid part may be dropped if what is left is fully operative as a law." *Miller*, 10 F.3d at 640 (emphasis omitted) (quoting *Buckley v. Valeo*, 424 U.S. 1, 108-109 (1976) (per curiam)). In *Alaska Airlines, Inc. v. Brock*, the Supreme Court elaborated on this standard, holding that "[t]he more relevant inquiry in evaluating severability is whether the statute will function in a manner consistent with the intent of

Congress [i.e., the legislature]." 480 U.S. 678, 685 (1987).

The legislative history of the CRRA, debated as Assembly Bill 1391, reveals that the legislature abandoned the initial version of the CRRA that purported to regulate *only* sales that took place *in* California. (*See* Russell Decl. Ex. 1.)

Assembly Bill 1391, as introduced on April 2, 1975, provided for a resale royalty only where "an original work of fine art [was] sold at an auction or by a gallery or museum *in California*." (Russell Decl. Ex. 1, at 8) (emphasis added). The bill was then amended, to ensure the CRRA applied "[w]henever a work of fine art [was] sold *and the buyer or the seller resides in California or the sale takes place* in California." (Russell Decl. Ex. 4, at 22) (emphasis in original). The bill was then amended again, deleting the reference to California buyers, but continuing to require a resale royalty for sales outside of California where the "seller resides in California." (Russell Decl. Ex. 6, at 34.) After the initial introduction of the bill, all amended versions were consistent in one respect: they applied to sales taking place outside California so long as the seller resided in California.

Moreover, the legislature endorsed the CRRA's extraterritorial reach, despite the fact that California's Legislative Counsel advised both Assemblyman Sieroty and then-Governor Brown, in opinion letters, that the bill "would constitute an undue burden on interstate commerce in contravention of the Federal

Constitution in its application to sales which occur outside the State of California." (Id. Ex. 5, at 26; Ex. 7, at 42.) As Defendants pointed out in oral argument, the reason for the legislature's decision seems obvious: were the CRRA to apply *only* to sales occurring *in* California, the art market would surely have fled the state to avoid paying the 5% royalty. (Docket no. 39 at 21:10-17.)

For these reasons, the Court finds that the California legislature "would not have enacted" the CRRA without its extraterritorial reach. *Buckley*, 424 U.S. at 108-109. Were the Court merely to sever the extraterritorial provisions of the statute, it would create a law that the legislature clearly never intended to create. The Court declines to do so.

Therefore, the Court finds that the CRRA must fall in its entirety.

IV.

CONCLUSION

For the foregoing reasons, the Court finds that the California Resale Royalties Act, Cal. Civ. Code § 986, violates the Commerce Clause of the United States Constitution. Because the Court finds that the offending provisions cannot be severed, the entire statute is struck down. Therefore, Defendants' Joint Motion to Dismiss the Complaints (docket no. 17) is **GRANTED with prejudice**, as amendment would be futile.

IT IS SO ORDERED.

Dated: May 17, 2012

/s/ Jacqueline H. Nguyen
Jacqueline H. Nguyen
Circuit Judge, United States Court of Appeals for the Ninth Circuit, sitting by designation

Resale Royalties Act

Cal. Civ. Code § 986

Work of fine art; sale; payment of percentage to artist or deposit for Arts Council; failure to pay; action for damages; exemptions

(a) Whenever a work of fine art is sold and the seller resides in California or the sale takes place in California, the seller or the seller's agent shall pay to the artist of such work of fine art or to such artist's agent 5 percent of the amount of such sale. The right of the artist to receive an amount equal to 5 percent of the amount of such sale may be waived only by a contract in writing providing for an amount in excess of 5 percent of the amount of such sale. An artist may assign the right to collect the royalty payment provided by this section to another individual or entity. However, the assignment shall not have the effect of creating a waiver prohibited by this subdivision.

(1) When a work of fine art is sold at an auction or by a gallery, dealer, broker, museum, or other person acting as the agent for the seller the agent shall withhold 5 percent of the amount of the sale, locate the artist and pay the artist.

(2) If the seller or agent is unable to locate and pay the artist within 90 days, an amount equal to 5 percent of the amount of the sale shall be tranferred [sic] to the Arts Council.

(3) If a seller or the seller's agent fails to pay an artist the amount equal to 5 percent of the sale of a

work of fine art by the artist or fails to transfer such amount to the Arts Council, the artist may bring an action for damages within three years after the date of sale or one year after the discovery of the sale, whichever is longer. The prevailing party in any action brought under this paragraph shall be entitled to reasonable attorney fees, in an amount as determined by the court.

(4) Moneys received by the council pursuant to this section shall be deposited in an account in the Special Deposit Fund in the State Treasury.

(5) The Arts Council shall attempt to locate any artist for whom money is received pursuant to this section. If the council is unable to locate the artist and the artist does not file a written claim for the money received by the council within seven years of the date of sale of the work of fine art, the right of the artist terminates and such money shall be transferred to the council for use in acquiring fine art pursuant to the Art in Public Buildings program set forth in Chapter 2.1 (commencing with Section 15813) of Part 10b of Division 3 of Title 2, of the Government Code.

(6) Any amounts of money held by any seller or agent for the payment of artists pursuant to this section shall be exempt from enforcement of a money judgment by the creditors of the seller or agent.

(7) Upon the death of an artist, the rights and duties created under this section shall inure to his or her heirs, legatees, or personal representative, until

the 20th anniversary of the death of the artist. The provisions of this paragraph shall be applicable only with respect to an artist who dies after January 1, 1983.

(b) Subdivision (a) shall not apply to any of the following:

(1) To the initial sale of a work of fine art where legal title to such work at the time of such initial sale is vested in the artist thereof.

(2) To the resale of a work of fine art for a gross sales price of less than one thousand dollars ($1,000).

(3) Except as provided in paragraph (7) of subdivision (a), to a resale after the death of such artist.

(4) To the resale of the work of fine art for a gross sales price less than the purchase price paid by the seller.

(5) To a transfer of a work of fine art which is exchanged for one or more works of fine art or for a combination of cash, other property, and one or more works of fine art where the fair market value of the property exchanged is less than one thousand dollars ($1,000).

(6) To the resale of a work of fine art by an art dealer to a purchaser within 10 years of the initial sale of the work of fine art by the artist to an art dealer, provided all intervening resales are between art dealers.

(7) To a sale of a work of stained glass artistry where the work has been permanently attached to real property and is sold as part of the sale of the real property to which it is attached.

(c) For purposes of this section, the following terms have the following meanings:

(1) "Artist" means the person who creates a work of fine art and who, at the time of resale, is a citizen of the United States, or a resident of the state who has resided in the state for a minimum of two years.

(2) "Fine art" means an original painting, sculpture, or drawing, or an original work of art in glass.

(3) "Art dealer" means a person who is actively and principally engaged in or conducting the business of selling works of fine art for which business such person validly holds a sales tax permit.

(d) This section shall become operative on January 1, 1977, and shall apply to works of fine art created before and after its operative date.

(e) If any provision of this section or the application thereof to any person or circumstance is held invalid for any reason, such invalidity shall not affect any other provisions or applications of this section which can be effected, without the invalid provision or application, and to this end the provisions of this section are severable.

(f) The amendments to this section enacted during the 1981-82 Regular Session of the Legislature shall

apply to transfers of works of fine art, when created before or after January 1, 1983, that occur on or after that date.

U.S. Const. art I, § 8, cl. 3

The Congress shall have power . . . [t]o regulate commerce with foreign nations, and among the several states, and with the Indian tribes . . . .