

MEMORANDUM

TO: Scope and Program Committee

CC: Steve Willborn
Lisa Jacobs

FROM: Study Committee on Uniform Direct to Consumer Sales of Distilled Spirits Act
Steve Frost, chair

DATE: June 11, 2019

RE: Uniform Direct to Consumer Sales of Distilled Spirits Act – Study Committee Report

The Executive Committee formed our Study Committee to consider whether to recommend to the Scope and Program Committee the appointment of a drafting committee for a Uniform Direct to Consumer Sales of [Distilled Spirits] Act. The memorandum from Stephen B. Humphress to Steve Wilborn and John McGarvey suggesting consideration of a direct-to-consumers uniform act is attached as Exhibit [A]. The Study Committee has completed its review and has prepared this report.

Summary of Conclusions:

The Study Committee has reviewed literature and heard from observers that existing statutes governing direct-to-consumer sales of wine have resulted in significant noncompliance with existing registration and tax statutes and also lack the rules necessary to prevent sales to underage purchasers. As a result, by a vote of [nine] to [three] Commissioners ([one] Commissioner did not express his views), the Study Committee recommends that a drafting committee be appointed to draft a uniform act with the following objectives and focus:

1) The Act would apply to spirits and wine and would allow an enacting state to select coverage for spirits, wine, or both. (The Study Committee spent little time discussing beer because it believes that the need for refrigeration makes direct-to-consumer sales of beer unlikely, and while it suggests that beer not be added to the products covered by this act at this time, as noted below, it would leave this decision to a drafting committee, if appointed.)

2) The Act would only apply to direct sales of spirits and/or wine by producers to consumers, both intrastate and interstate, and would not apply to (a) other sales by producers (e.g. sales to wholesalers or retailers) or (b) any sales by wholesalers or retailers.

3) The Act would have the following three principal areas of focus: a) rules to encourage compliance with registration and reporting requirements, b) rules to encourage compliance with tax reporting and payment and c) rules to reduce sales and deliveries of any alcohol products to

underage purchasers (and consider rules for other persons prohibited from purchasing alcohol products under other law).

4) If a drafting committee is established on the basis of points 1) through 3) above, the Study Committee recommends changing the name of the Act to a name that reflects the fact that provisions may apply to all sales of alcoholic beverages (likely other than beer) selected by the enacting jurisdiction, such as the “Uniform Act on Direct-to-Consumer Sales of Wine and Distilled Spirits.” If the drafting committee is appointed and decides to include the sale of beer, then a different title would be appropriate.

Please note that while they did not take part in the vote, the Division E Chair Member, the Scope and Program liaison to the Study Committee and the Chair of the Study Committee also recommend that a drafting committee be appointed with the objectives and focus outlined above.

While [nine] Commissioners on the Study Committee are in favor of establishing a drafting committee because of all the problems with existing statutes governing sales by producers directly to consumers (“*direct-to-consumers*” or “*DTC*”), [three] Commissioners on the Study Committee are against establishing a drafting committee for the following reasons: 1) the subject matter will be highly controversial and therefore less likely to be considered by states (one of the three Commissioners voting “no” indicated her state would not consider this legislation); 2) alcohol-related laws are local in nature and that it may be difficult to separate and draft a uniform law relating principally to the three areas identified by the majority (compliance, tax collection and underage purchases); 3) lack of compliance is to some degree, if not a large degree, driven by a lack of funding, and while the Study Committee would include the ability to direct some funds from increased tax collections to enforcement, members of our Study Committee are concerned that addressing how revenue is shared is not a function of a uniform law drafting committee; 4) any proposed change in alcohol laws will result in a “turf war” (adding to controversy); and 5) a consequence of creating a drafting committee is that eventually the ULC may be viewed as promoting a uniform act that facilitates the sale of alcohol because the ULC Constitution (sec 6.1(6), bylaw 27.1) imposes a duty on Commissioners to seek introduction and enactment of uniform laws (whether this view is correct, this perception may be a consideration in determining whether an act, if drafted, is promulgated as a uniform or model act, but that determination would be made at a later time).

As noted, Scope and Program should be aware that a uniform act on DTC sales of any alcohol would have opposition. There is significant disagreement between our observers about the appropriateness of a uniform act addressing the direct sale of spirits to consumers. Observers to the Study Committee who represent the interests of spirits producers are in favor of an act, while observers who represent interests of wholesalers and retailers, as well as observers who focus on public health policy considerations, are against a uniform act. Paul Pisano, of the National Beer Wholesalers Organization, made clear his view that direct sales should be left to state legislatures and lobbyists to develop responses to these issues. Several of their arguments are summarized in our discussion of issues below. Also, retailers who were not represented by observers may feel differently, depending on who may ship and who is the retailer. While some retailers may object to producers having DTC privileges, the National Association of Wine Retailers, headed by Tom Wark, is filing suits in numerous jurisdictions for the right of retailers to ship

DTC. (See: <https://www.winespectator.com/webfeature/show/id/Michigan-Court-Overturms-Ban-on-Wine-Retailer-Direct-Shipping>). In general, there is a split among retailers on this issue, with big box retailers like Costco and Walmart (but not Total Wine) wanting DTC for retailers and the “independent” retailers (mom-and-pop shops) against it, except that there are some very high-end, boutique retailers in big cities who favor DTC because they sell rare, expensive wines to a niche market. It would be fair to say that the Scope and Program and Executive Committees should be aware of these strongly held opinions and the stakeholders who support or object to any further efforts on the part of the ULC.

ULC Study Committee guidelines

The Study Committee considered the ULC Study Committee Guidelines and concluded as follows:

- (a) The subject matter is appropriate for state legislation because it is reserved to state law by the 21st amendment to the U.S. Constitution and already addressed by state statute (43 states permit DTC sales of wine and eight states permit DTC sales of distilled spirits) and, as discussed below, should not be preempted by federal law.
- (b) The proposed act would promote uniformity on a subject matter where uniformity is desirable and practicable because having a uniform set of state rules governing registration of producers, reporting by producers and their agents, and for confirming sales and deliveries are not made to underage persons would simplify compliance, improve tax collections, and help prevent sales and deliveries to underage purchasers. It should also make cross border enforcement more effective and promote commerce.
- (c) (1) There is a need for a uniform act given non-compliance under existing DTC statutes with registration requirements, applicable tax laws and prohibitions on sales to underage purchasers.

(2) We would like to poll Commissioners to have better information about the likelihood of adoption in the states given the effects summarized in item (c)(1). Because alcohol-related legislation will be controversial, it is likely that a number of states would not consider a uniform act, although we understand some states would welcome provisions they could adopt from a uniform act that address “low hanging fruit” increasing the likelihood of compliance, increase tax collections and reduce underage drinking, particularly if a state could elect to adopt provisions for wine, which it already permits, without adopting provisions relating to distilled spirits.

(3) A complaint of producers is the wide variety of rules that apply across state lines so that uniformity on this subject matter would facilitate interstate commerce. Creating a uniform set of rules that increases compliance with laws that apply to other sales of alcohol would also produce public benefit.
- (d) We anticipate that we would better identify proponents and opponents and describe controversy an act would generate after polling Commissioners.

Discussion:

We began our project in the fall of 2018. An initial task was to identify stakeholders, ABA observers and others to invite to participate in the project. We were fortunate that a number of people we invited who are experts in their fields agreed to assist us. A roster of our ABA advisors and others who participated as observers is attached as Exhibit [B]. Please note that: (i) certain persons we initially contacted did not wish to participate (law enforcement personnel did not respond to written or phone requests and taxing authorities expressly declined to participate), (ii) we accepted additional observers as the project progressed to be certain anyone expressing an interest could participate (e.g., the chair personally contacted and invited every person any Study Committee member or observer recommended as an additional observer, including four additional public health professionals, but most declined to participate), and (iii) we circulated drafts of this report to all our Study Committee members and observers, invited comments and corrections and, admittedly in the discretion of the chair, incorporated many of the comments received in this draft (the chair also invited observers to submit letters – two such letters are attached as Exhibits and one more letter will be submitted and forwarded to the Scope and Program Committee when received). Finally, note that we have been advised that all comments of observers reported in this memorandum are personal views and not the views of the organizations represented by these observers.

We discussed the issues raised by this project over the course of several months in a series of web conference calls. As a preliminary matter, the Scope and Program Committee should understand several aspects of the current regulation of alcohol in the United States. With only two possible exceptions (the National Alcohol Beverage Control Association lists Washington and Oklahoma as having varied their rules to varying degrees), every state imposes what is called the “three tier system” in regulating the distribution of alcohol. Under this system, producers sell directly to wholesalers, wholesalers sell directly to retailers, and retailers sell to consumers. Supporters argue that the three-tier system prevents tainted alcohol from entering the market and that it has other economic and commercial benefits. DTC sales are an exception to the sale of alcoholic beverages through the three-tier system. Over 40 states have enacted some form of DTC statute for the sale of wines, and eight states have enacted DTC statutes for the sale of distilled spirits. In 17 states and jurisdictions in several other states, the government controls the sale of distilled spirits and, in some cases, wine and beer through government agencies at the wholesale level. Thirteen of these “control” jurisdictions also exercise control over retail sales through government operated stores or agents.

During our web conferences we identified and considered a number of issues that are discussed below. Some of these issues have been heavily influenced by recent judicial decisions, including: *South Dakota v. Wayfair Inc.*, 138 S. Ct. 2080 (2018) (the Supreme Court overruled *Quill Corp.*, and held that an out-of-state seller’s physical presence in a taxing state is no longer necessary for the state to require the seller to collect and remit sales tax, which instead would be tested on the basis of whether the seller had a substantial nexus with the taxing state), *Granholm v. Heald*, 125 S. Ct. 1885 (2005) (the Supreme Court held that Michigan statutes prohibiting out-of-state wineries from shipping wine directly to in-state consumers, but permitting in-state wineries to do so if licensed, and New York statutes imposing additional burdens on out-of-state wineries seeking to ship wine directly to New York consumers both discriminated against interstate

commerce) and *Byrd v. Tennessee Wine and Spirits Retailers Association*, 883 F. 2d 608 (6thth Cir. 2018) (holding that the 21stst amendment did not immunize a durational residency requirement imposed by Tennessee on out-of-state retailers from commerce clause scrutiny). The *Byrd* decision is on appeal to the U.S. Supreme Court, and oral arguments were heard on January 16, 2019. We are awaiting a determination by the Supreme Court. (An article on *Byrd* and the oral arguments written by one of our Study Committee Commissioners is available at <https://www.wisbar.org/newspublications/wisconsinlawyer/pages/Article.aspx?Volume=92&Issue=4&ArticleID=26968>.)

We also reviewed a number of existing DTC statutes to identify terms and issues addressed in existing law. A summary of these terms and issues is attached as Exhibit [C]. As noted throughout this report, existing DTC wine and distilled spirits acts do not appear to address many of the issues raised in this report.

We also spoke with legislators and/or their staff who have been involved with recent legislation to identify issues and concerns raised in their efforts. Their comments and observations are summarized below.

Several observers directed us to a study published by Fosdick and Scott entitled “Toward Liquor Control,” a study completed in 1933, that outlines the basis of today’s liquor regulation. Interestingly, while the study does conclude the alcohol industry must be strictly regulated and sets forth the entire ecosystem that is the current basis of alcohol regulation in this country today, it also concludes with the following observation: “[n]o recommendations which we or anyone else could make carry with them an element of finality. The only service that law can render is to give effect to the necessities and ideals of a given time and place, and necessities and ideals cannot escape the processes of change. We need to be on our guard against any system of control that has outlived its usefulness or that no longer represents the prevalent ideas and attitudes of the community. Our legal prescriptions and formulas must be living conceptions, capable of growing as we grow. For law itself is a social phenomenon and has no meaning apart from the uses and necessities from which it springs.” pp. 97-8.

Detailed Issues List (no particular order):

There are several reasons for including a detailed list of the issues we discussed in this report. First, we want to give the Scope and Program Committee as complete a picture as possible of the background we believe may be useful in its evaluation of whether to recommend the creations of a drafting committee. Second, while some of these comments may not relate directly to whether a drafting committee should be established, they do identify issues that a drafting committee, if appointed, should consider. The issues we discussed are as follows:

1) Scope of a uniform act.

- a. The scope of our discussions is limited to sales by producers to consumers, either directly or through agents, such as fulfillment centers and other third parties, both in-state and out-of-state, *and not* sales by: i) producers to wholesalers or retailers; ii) wholesalers; or iii) retailers. The Committee

received several comments that an act should address only sales by producers, primarily because sales by and to wholesalers and retailers and the rules applicable to wholesalers and retailers are so varied that it would be difficult to draft a uniform law that would be widely acceptable.

- b. We initially determined we are discussing spirits, wine and beer, though beer is an unlikely candidate because of the issues raised by the need for refrigeration. If a drafting committee is appointed, it may even allow an enacting state to elect coverage (of wine, distilled spirits and/or beer). Suggestions varied from (a) an act should cover only spirits to (b) an act should cover all three classes of alcohol and, as discussed further below, noncompliance in current on-line sales of wine may argue for at least wine and spirits to be included. Any decision should be left to a drafting committee, if one is appointed.
- 2) Compromise positions. Whatever the scope, a drafting committee, if appointed, may consider alternatives for states that are unwilling to permit unlimited DTC sales, such as only permitting in-person (sometimes referred to as “face-to-face”) sales, in which case the drafting committee would need to consider this type of compromise limitation and the impact of *Cherry Hill Vineyards, LLC v Lilly*, 553 F.2d 423 (6th Cir 2008), which ruled that an in-person purchase requirement for direct shipments violated the Commerce Clause, but see *Baude v. Heath*, 538 F3d 608 (7th Cir. 2008), which held that a requirement that a purchase appear at least once in-person at a vineyard did not violate the commerce clause, and *Churchill Downs Inc v Trout*, 589 F.2d 233 (5th Cir. 2014) and other decisions that distinguish *Cherry Hill*.
- 3) Regulatory issues. The act would need to consider areas that might require regulation, such as assuring compliance by out-of-state producers with licensing requirements; verification of compliance; and penalties for failure to comply. For each of these issues, a drafting committee would need to consider and address the need for uniformity.

The Study Committee discussed current practices regarding wine and spirit sales. Producers ship product to consumers in various ways, including directly and through so-called fulfillment centers. Fulfillment centers are warehouses operated by third parties who maintain inventories of product from various producers and who then ship product to consumers (more information at <https://www.winedirect.com/>). One observer has noted they are a critical component of noncompliance with wine statutes.

The Study Committee concluded that reporting under existing DTC statutes is not effective for virtually any purpose. Common carriers report shipments to state authorities, but they only report shippers’ names and addresses (which may be the name and address of the fulfillment center), consignee names and addresses, and weight of packages. Thus, if the shipper is not the producer, a state cannot easily confirm the identity of the seller or determine whether appropriate taxes are being paid. The standard form for reporting this information is impracticable. Common carriers generally do not have information about producers when the person shipping is a

fulfillment center. Compliance could be improved if an act required the person delivering product for shipping to provide producer information in a format that enables the state to enforce all laws and regulations.

There is significant evidence of noncompliance with licenses and payment of taxes. Wisconsin studied its laws in 2018 and discovered significant illegal shipments and underreporting of taxes. For example, a random sampling of monthly tax reports revealed that only two of more than 500 direct wine shipper permittees reported shipments for tax purposes. (<https://www.revenue.wi.gov/DORReports/liqstat1812.pdf>.) One study for Virginia for the period of June 2108 to September 2018 indicated that unlicensed shipments constituted 38% of all shipments during this period. (http://sfc.virginia.gov/pdf/Public%20Safety/2019/010819_No1_ABC.pdf). More than one observer noted that noncompliance is often attributable to a lack of enforcement because of the lack of funding at the state level. Donovan Borvan, who was director of the Illinois Liquor Control Commission when Illinois recently improved enforcement policies (discussed further below), explained that Illinois changed its laws to require a portion of license fees to be segregated in a fund for use by the regulatory agency for enforcement, after which enforcement improved and tax collections in Illinois increased. If a drafting committee is appointed, an issue for it will be to consider whether a uniform act could require/suggest some portion of taxes and fees collected be deposited in a fund for enforcement and administration. Note that one member of the Study Committee expressed the view that drafting an act that earmarks funds for compliance is not a role of a uniform act. One paper prepared by the Center for Alcohol Policy highlights the funding challenges and lists at least four options for addressing these challenges, see https://www.centerforalcoholpolicy.org/wp-content/uploads/2013/03/The_Need_for_State_Alcohol_Regulatory_Funding.pdf.

Note, UPS does not accept spirits for shipment, only wine. Matt Dogali, of the President's Forum of the Distilled Spirits Industry, indicated that persons shipping spirits may simply mark a container as containing "alcohol," in which event common carriers will pick up and deliver the containers. Jill Termini, of UPS, confirmed that common carriers do not (for various reasons - may not) open or inspect the content of containers shipped by them. This practice may deserve further attention if a drafting committee is appointed.

The Study Committee discussed responses by states to noncompliance. It appears part of the problem may be nexus or jurisdiction over out-of-state producers, though more examination may be necessary (for general jurisdiction) and recent tax decisions may make nexus much simpler (at least for tax purposes). One Mississippi case on appeal where the judge did not allow the Mississippi attorney general to enforce Mississippi laws against an out-of-state shipper should be monitored (opinion and appeal at <http://alcoholawreview.com/mississippi-ag-to-appeal-shipping-ruling/>). (Steve Humphress sent the Study Committee an email with further explanation about the basis of the case to which he attached an email from John Hinman, the attorney for all

defendants in the case, with briefs and other information. The observers to our Study Committee disagree on the significance of this decision.)

New York has a regulation that authorizes the state to terminate the license of a New York producer who does not comply with shipping rules in other states. [We believe this result is possible under 9 CRR-NY 53.1(n) as a violation of other law may constitute “improper conduct” under the New York rules. See <https://www.nyslsa.com/news/news.asp?id=195516&hhSearchTerms=%22195516%22>.] (Aaron Gary also sent an email to the group, dated Feb 14) with other information on both the Mississippi decision and on New York’s approach.) Donovan Borvan also explained that Illinois took several steps to improve compliance and enforce rules, including increasing penalties, setting aside a portion of collections of taxes and fees for administration of laws, adding agents and adding personnel to compare reports of common carriers to filings with the state by producers. Illinois also took steps to identify individuals driving their cars out of state to make purchases and returning to sell in-state. These steps increased compliance in Illinois and, together with other steps, should be considered if a drafting committee is established.

New Hampshire provides another example of useful reporting. Out-of-state shippers are required to obtain an out of state shipper’s permit. The state keeps a non-compliant list which the state shares with carriers. The carriers monitor shipments to New Hampshire and intercept non-compliant shipments. (See <https://www.nh.gov/liquor/enforcement/licensing/direct-shipping.htm>.) More review is necessary. Interestingly, New Hampshire is a control state that permits direct sales of wine and spirits to persons in New Hampshire.

If appointed, a drafting committee should consider all alternatives to try and remedy compliance across state lines. One of our observers has been in contact with the Treasury Department Alcohol and Tobacco Tax and Trade Bureau (“TTB”). All distilleries in the United States must have a basic permit issued by the TTB. By ATF Ruling 2000-1, <https://ttb.gov/rulings/2000-1.htm>, the TTB held that a violation of the Webb-Kenyon Act (27 U.S.C. § 122) (sales and shipping alcoholic beverages in violation of state law) constituted a violation of the Federal Alcohol Act (27 U.S.C. § 203 et seq). The TTB has nationwide jurisdiction and can take enforcement action to revoke or suspend distillery basic permits (civil) for FAA violations nationwide. It may be possible to include TTB in a drafting committee project to consider that results in TTB enforcement with state partner cooperation. While the TTB statement on direct shipping (see, https://www.ttb.gov/publications/direct_shipping.shtml) notes “[w]e want to remind industry members who engage in direct shipping that they are responsible for remaining in compliance with current State rules. Furthermore, industry members should remember that their Federal basic permits could be at risk if they fail to comply with State rules,” ATF Ruling 2000-1 clearly holds that ATF will only intervene in very limited circumstances. The Treasury has been supportive and interested in prior ULC drafting projects on topics of interest to them. If a drafting committee is established, it should further consider this avenue for enforcement.

An interesting situation in the case of wine is a Model Direct Shipping Bill that was approved by a Task Force on Wine of the National Conference for State Legislatures (“NCSL”) in 1997. However, this model was NOT reviewed by the NCSL Executive Committee or adopted as policy of the NCSL, yet apparently some (see the online warning below) are inaccurately claiming the model was adopted by the NCSL, which lead the Executive Director of the NCSL to post a letter online warning the public it is not policy of the NCSL (See, http://www.ncsl.org/documents/standcomm/sccomfc/NCSL_WineIndustryModelDirectShipmentBill.pdf). The model bill approved by the Task Force includes language provided by wine industry associations. (See <https://freethegrapes.org/model-direct-shipping-bill/>). The bill is one page long. We do not know if this approach has been adopted in any states. Significantly, whether it has been enacted, it has not apparently lead to increases or improvement in compliance.

Fulfillment centers are not always subject to registration or tax. Thus, solutions that might be considered include registration and reporting by any person, not only producers, shipping alcohol into a state (e.g., including, but not limited to, fulfillment centers), and adding penalties for failure to report that would equal the taxes owed by the producer if the sales had been reported properly. [The form of reporting must be considered so that shipment information from common carriers and persons shipping on behalf of producers can be matched to information from producers.]

In conclusion, at a minimum, existing DTC statutes raise significant enforcement problems by for wine and distilled spirits.

- 4) State tax issues raised by imposition of privilege taxes on out of state vendors (*South Dakota vs Wayfair, Inc.*, 585 US ____ (2018)).

The 2018 Supreme Court decision in *Wayfair* eliminated a requirement that sellers have physical presence in a taxing state to require sellers to collect and remit sales tax (the decision did not address excise taxes or alcohol excise taxes or VAT or city taxes on alcohol). The decision should make enforcement of state and local sales tax collection easier if compliance is improved. If a drafting committee is appointed, it would need to evaluate other taxes, particularly excise and alcohol related taxes, and steps necessary to improve compliance as well.

- 5) Impact of “control states” where the government sells alcoholic beverage sales, including total control and partial control states. What are their issues and concerns? Are they different than other states?

Neal Insley of the National Alcohol Beverage Control Association (“NABCA”) indicated that control jurisdictions take ownership of the alcohol product at the wholesale and/or retail level. There are 17 control jurisdictions, and they account for approximately 25-30% of the spirits market in the United States. Under the control model, the state controls the sale of distilled spirits and, in some cases, wine and beer through government agencies at the wholesale level. The NABCA maintains a website

that includes an information sheet for each control jurisdiction explaining how that state controls the distribution and sale of alcohol. See, <https://www.nabca.org/control-state-directory-and-info>. While control varies from state to state, the state controls which alcohol products are sold, at what price, and how the products are distributed and sold. 15 of the 17 control jurisdictions permit direct sales of wine and 1 control state, New Hampshire, permits DTC sales of spirits.

The sense of the Chair of the Study Committee is that control jurisdictions are strong supporters of the 21st amendment and states' rights in controlling the distribution and sale of alcohol. Therefore, it would be important for a uniform act, if drafted, to make clear in the preamble or comments that (1) the ULC is a state supported organization made up of representatives from each state, appointed by state governments, (2) the policy decisions of whether and how alcohol should be distributed and sold within a state is a state determination (not made by the ULC), and (3) the purpose of the uniform act is to provide rules and procedures for those states that choose to permit DTC sales of wine or spirits to improve compliance with existing state regulatory, tax and other requirements applicable to alcohol.

Note that we received some comments by legislators and staff in control states that are included at item [12] below.

6) Public health, law enforcement, and other relevant policy issues.

Diane Riibe, of the U.S. Alcohol Policy Alliance, indicated that in her organization's view, any legislation that increases alcohol availability will increase consumption and underaged drinking and is against public policy, regardless of any other benefits. She believes a DTC act would increase alcohol availability. When pressed on why an act that increases compliance, increases collection of taxes, and reduces underage drinking would be bad, Elyse Grossman, of the Johns Hopkins Bloomberg School of Health, indicated that research shows that all legislation that increases availability of alcohol has these negative consequences. It will help to understand why past legislative efforts have failed and have had negative consequences, and Elyse agreed to provide this research, but neither Diane nor Elyse has not done so yet (we will forward this research if we receive it). Elyse and Diane have written a letter critical of the chair and the Study Committee's work that is attached as Exhibit [D].

Paul Pisano of the National Beer Wholesalers Association believes that any legislation not consumer driven will be controversial, and he does not believe a direct-to-consumer act is consumer driven. Paul provided me with a survey conducted by New Bridge Strategy, dated May 1, 2019 (and available at <https://www.centerforalcoholpolicy.org/wp-content/uploads/2019/04/2019-Survey-Results-Memo-4-18-19-.pdf>), that notes 87% of the Americans surveyed indicated they are satisfied with the variety of alcohol products available in their communities). He also believes the ULC should not consider a uniform act and should allow lobbyists to negotiate these provisions on a state-by-state basis for some additional period of time before attempting to draft a uniform act. At the same time, Paul has informed the chair

that there have been over 1700 changes to alcohol laws since 2012 alone, or approximately 5 a year per state. In his view, it has been “a slow, consensus driven change.” Finally, Paul also expressed his view that a number of relevant legal issues have not been considered by the study committee, which appear more to be issues that are raised by decisions made by a drafting committee as opposed to issues relating to whether a drafting committee should be established. Several observers expressed the view that these rules should be left to the states. When told that the ULC drafts laws for states to consider and that no state is forced to enact a uniform law, one observer noted that an act drafted by the ULC would essentially be viewed as having a “stamp of approval.” A letter from Heather Calio of the Wine & Spirits Wholesalers of America expressing a view that expanding alcohol sales would not be appropriate is attached as Exhibit [E]. Other observers disagreed with Paul and expressed the contrary view with respect to whether this legislation is consumer driven. Dan Farber of the American Crafts Spirits Association indicated that the Association’s members are frequently asked to ship spirits to customers or they would not be seeking relief legislatively. A letter from Dan Farber describing the state of the market for smaller producers is attached as Exhibit [F].

There is clear disagreement among our observers as to whether spirits should be treated differently than wine. Observers representing distillers believe the markets are evolving and that spirits should be treated no differently than wine, and representatives of wholesalers and retailers believe spirits are different than wine and should be treated differently under the law. One observer noted that wine is not flammable, but spirits are flammable, which would impact shipping. The point was also made that for some purposes, such as excise taxes, spirits are treated differently. Also, youth tend to drink beer and spirits, not wine, though two-thirds of deaths from alcohol poisoning are middle aged non-hispanic men (as opposed to youth). See <https://www.cdc.gov/vitalsigns/alcohol-poisoning-deaths/index.html>. Clearly, this is a running dispute within the industry, but while some of our observers may disagree, the view of the commissioners is that these differences would likely drive some policy decisions if a drafting committee is appointed, but should not impact the decision to establish a drafting committee.

The research our observers have provided is informative and helpful. (Attached as Exhibit [G] is a copy of this research.) In one study by Rebecca Williams, MHS, PhD, and Kurt Ribisl, PhD, the authors selected 100 popular alcohol vendor websites and studied purchases by 18 to 20 year old individuals who lived in the county where the study was conducted, which, coincidentally was in North Carolina – a control state that controls all sales of spirits but not wine or beer. Alcohol ordered from a county in North Carolina in the study included wine (65%), liquor (17%) and beer (14%). Of those purchases, 42% of wine, 53% of liquor and 57% of beer, were successfully received by the minors, and 46% of wine, 12% of liquor and 36% of beer purchases failed because of age verification techniques (and varying percentages of purchases failed for other reasons). The authors concluded that most age verification strategies do not effectively verify age (e.g., submitting order is “deemed” to verify age and user clicks are particularly useless) and in 41% of the orders there was no attempt to verify

age at all. Age verification strategies noted in the study that could potentially block youth access include entering a driver's license number and requiring the purchaser to submit a copy of a driver's license, in which case no orders in the study were successfully received (though the number of these purchases may not be high enough to draw further conclusions). See also, Exhibit I.35 in the State Performance and Best Practices study provided by Elyse, in which the table indicates that for direct sales (of mostly wine) 16 states do not require any age verification before shipment can be made.

This study provided by Elyse Grossman does ask whether better methods for verifying age could effectively reduce underage purchases if adopted uniformly. A drafting committee may identify more effective approaches from non-alcohol related sources. For example, the "Children's Online Privacy Protection Act of 1998," 15 USC §6501 et seq., requires any person who operates a website directed to children and who collects information from children to obtain verifiable parental consent for the collection, use or disclosure of personal information from children. Regulations have been adopted at 16 CFR §312.5(b) identifying methods for verifiable parental consent, which include requiring a parent, in connection with a monetary transaction, to use a credit card, debit card, or other online payment system that provides notification of each discrete transaction to the primary account holder and verifying a parent's identity by checking a form of government-issued identification against databases of such information. Uniformly requiring by law these methods (or combinations of these and other methods) of age verification may reduce underage purchases of all forms of alcohol as well. A drafting committee, if appointed, would need to evaluate the effectiveness of this federal act and other alternatives for improving compliance.

- 7) Compliance with other state laws, e.g., purchasers other than minors, labeling, and so forth, that should be addressed in a uniform act.

There are other scope-related questions that a drafting committee, if appointed, must consider. Some existing alcohol statutes include classes of persons other than minors to whom sellers may not sell. For example, §5-01-09(1) of the North Dakota statutes provides (after amendment in 2019) as follows: "Any individual knowingly delivering alcoholic beverages to an individual under twenty-one years of age, except as allowed under section 5-02-06, or to an incompetent, or an obviously intoxicated individual is guilty of a class A misdemeanor, subject to sections 5-01-08, 5-01-08.1, and 5-01-08.2." How should these other classes of prohibited purchasers be addressed? For example, is it sufficient for a shipper to be able to say it does not "know" of the condition? Examples of other scope-related issues include compliance with laws regarding labeling and dram shop liability. The Study Committee did not review existing statutes to address these issues.

- 8) Consider the ability to address direct to consumer sales in an act without having to integrate with other liquor related legislation in each state (ability to draft a uniform law).

The Study Committee identified many shortcomings and failures of existing DTC statutes for wine and distilled spirits. Because of the complexity of alcohol laws, the committee's initial reaction is to consider an act would permit sales by producers directly to consumers, but that would have a narrow focus and include limited provisions addressing compliance with registration, reporting and tax requirements found in underlying alcohol statutes. In effect, can we draft a uniform act that (a) only addresses pieces of alcohol legislation and (b) gives states the ability to enact those pieces it wants (e.g., allows a state to enact provisions that apply to sales of wine without adopting provisions for distilled spirits)? In a sense, the ULC recently approved the Uniform Protected Series Act, which was drafted as a module that would supplement and work in tandem with a state's underlying LLC statute. Also, John McGarvey, our Division E Chair Member, indicated that the Uniform Act on Prevention of and Remedies for Human Trafficking also allows states to elect to adopt certain provisions. While the sense of the Study Committee is that a DTC act can be drafted in this fashion, to some extent we need to engage in the drafting process to find out if our initial expectation is correct.

Further, if this approach is adopted, does the approach undercut the benefit of uniformity? This issue was raised in conversations with legislators, and at least initially we heard that states may be interested in "low hanging fruit," which was described to me as tools for increasing compliance and tax collections, while (depending on the state) avoiding more controversial legislation. Thus, having an act with provisions that can be used piecemeal may actually be more attractive to states.

- 9) Do existing statutes expressly prohibit DTC sales of distilled spirits? If so, it would be much less likely states would adopt provisions from a uniform act.

This issue was added to our issues list early in the Study Committee deliberations and was raised by questions posed by Diane Riibe, an observer to our study committee, who indicated 33 states expressly prohibit direct sales of spirits, and Elyse Grossman, another observer to our study committee, who indicated a majority of the states expressly prohibit direct sales of spirits. At least initially, it appears from a review of materials provided to us by Elyse and prepared by the Substance Abuse and Mental Health Services Administration, as of January 1, 2017, only seven (7) states expressly prohibit direct sales of spirits. The data sheets on direct sales in this research indicate that seven (7) states prohibit all direct shipments of alcohol and seven (7) states explicitly permit direct shipments of distilled spirits. Of the remaining 36 states, ULC staff reviewed 27 states (which is most of the states that are not listed in Elyse's materials as either expressly permitting or expressly prohibiting direct shipments) and only one (1) statute explicitly prohibits direct shipments of distilled spirits. However, another observer pointed out that most state alcohol codes ban everything that is not permitted so that focusing on whether DTC sales of spirits are expressly or impliedly prohibited is a distinction without significance and does not signify whether a state is more or less likely to consider a uniform DTC statute. Importantly, the focus of the recommended project has been changed to address compliance issues with the statutes enacted by at least 43 states that have enacted DTC wine statutes as well. Aside from

feedback received from legislators (and discussed in point 12 below), we will not have more information about likelihood of consideration of DTC distilled spirits or DTC wine provisions until we poll Commissioners, as noted on page 3 of this report.

10) Are there feasible alternatives to a direct-to-consumer sales act?

Heather Calio, with the Wine and Spirits Wholesalers of America, indicated that there are alternatives for small distillers to find a market for their products within the current system and pointed us to <https://libdib.com>. In her view, DTC statutes are not necessary so long as viable alternatives exist. According to the LibDib website, “LibDib is a distributor of alcoholic beverages enabled through a web platform. Restaurants, Bars & Retailers legally and efficiently purchase boutique wines and craft spirits made by Makers of all Sizes. LibDib is currently selling to accounts throughout California, New York and Wisconsin. Expansion to new markets coming soon.”

11) Impact of litigation on a uniform act.

An observer noted that there is and will continue to be major litigation over alcohol regulatory matters and that the Tennessee Wine and Spirits Supreme Court case is but one decision that could impact the direction of the industry. This point essentially asks whether drafting a uniform act now is premature or timely. The general view of the Study Committee is that there will likely be ongoing litigation in this area and beginning in the aftermath of the *Tennessee Wine and Spirits* decision, whatever it may be, is timely.

A related point is the impact on this process of the pending decision the *Tennessee Wine and Spirits* case by the Supreme Court. The initial reaction of the Study Committee is that the decision may have a significant impact on the work and direction of a drafting committee, if established, but it should have no impact on whether a drafting committee is established.

12) Comments by legislators. The chair spoke with legislators and legislative staff from three (3) states, including one control state (although he contacted many more). These legislators and staff made several comments and observations of interest.

- a. All of the people with whom the chair spoke indicated they are aware of noncompliance with existing rules for DTC sales of wine in their states and that provisions in a uniform act that help address these issues would be key.
- b. Increasing correct revenue collections is paramount to everyone. Several people referred to this issue and to requiring everyone to pay their fair share, which several acknowledged is not happening.
- c. One staff member told the chair that there are lots of changes that will be proposed to their alcohol related statutes in the next several years. While they are not ready now in this state to consider any changes to their alcohol

legislation, the timing would be much better in a few years. In fact, this person anticipates major changes beginning in a few years.

- d. Several of the persons with whom the chair spoke said that having the ULC name associated with the act would give the act more immediate credibility.
- e. One person advised the chair that a drafting committee, if appointed, must consider technology changes that will occur in the near future and what a uniform act should include to address technology challenges. This person believes these changes will be significant, and a uniform act might be best positioned to address these concerns.
- f. A general theme in the chair's conversations is that people are not interested in attacking divisive issues in the current political environment, and expanding alcohol distribution would likely be divisive.
- g. One legislator suggested that if an act is drafted, the drafting committee should consider permitting DTC sales only after the producer has attempted to try and sell to retail outlets in the state.
- h. In some jurisdictions where unions have more power and state stores are unionized, the chair was told unions may be against the legislation if they perceive it could impact jobs.
- i. A common theme in the chair's conversations was safety, and in this regard an act that improves compliance and reduces underage drinking would be well received even if alcohol legislation is normally divisive. Noncompliance is extremely frustrating.
- j. Another person told the chair that staffers want to know what other states are doing, which would make a uniform act that is being considered more broadly more appealing.
- k. Another comment was that spirits carry a stigma that could make related legislation more difficult.
- l. In control states, there is a wide variety of availability with some states being more adept and having greater inventory in stores. To the extent states are willing to consider DTC legislation in the first place, states with better inventory maybe less likely to consider DTC legislation at all.
- m. In some control states, politics may dictate timing of efforts as some politicians want to weaken state control and would support DTC for that reason.

13) Would federal law preempt a state law based on a uniform act?

A question considered by the Study Committee is whether a uniform act could impose requirements on shippers IF such requirements are considered necessary by a drafting committee. One observer noted the Supreme Court decision in *Rowe v. New Hampshire Motor Transport Ass'n*. (discussed below) raises this issue. Our observer from a shipping company believes that decision would not apply to alcohol regulations because of the 21st Amendment. One of our Study Committee members believes that *Rowe* is not necessarily an impediment to drafting a uniform act. The case was decided more than 10 years ago and at least one circuit has signaled that *Rowe* might not apply to alcohol in the same way it applies to tobacco because of the 21st amendment. Because the effect of the case is still unclear, it should not be a reason for the committee to decline to proceed with drafting. Also, as a practical matter, carriers do not want to deliver alcohol to underage persons and will still be subject to general state laws against providing alcohol to underage persons, so we can expect an element of "voluntary" compliance by carriers even if there is a federal preemption argument that could be made. His text notes as follows:

Federal law may limit a state's ability to enforce restrictions on delivery of alcohol beverage shipments, such as the requirement that the recipient not be underage or intoxicated. In *Rowe v. New Hampshire Motor Transport Ass'n*, 552 U.S. 364 (2008), the Supreme Court addressed the issue of federal preemption, under the Federal Motor Carrier Deregulation Act, of Maine statutes that imposed certain recipient verification requirements when tobacco products were shipped, including that the tobacco not be delivered to an underage person, that the recipient produce identification, and that shipment only be to or from a Maine-licensed tobacco retailer. *Id.* at 367–69. The Supreme Court found these state-law requirements, which attempted to regulate motor carrier services, to be preempted by federal law. *Id.* at 375–77. Federal law prevents a state from requiring particular delivery procedures or services. States cannot regulate significant aspects of a motor carrier's package pickup and delivery service, even when the state's reason for the regulation is to keep cigarettes out of the hands of minors. *Id.* at 371–74. Presumably the same principle applies with respect to alcohol beverages. Federal law "preempt[s] state regulation of the essential details of a motor carrier's system for picking-up, sorting, and carrying goods." *Id.* at 373. "The state statutes require motor carrier operators to perform certain services ... and they do so simply because the State seeks to enlist the motor carrier operators as allies in its [underage tobacco] enforcement efforts." *Id.* at 376. See also *Lebamoff Enters., Inc. v. Huskey*, 666 F.3d 455 (7th Cir. 2012) (noting that *Rowe v. New Hampshire Motor Transport Ass'n*, 552 U.S. 364 (2008), did not involve the shipment of alcohol so there was no 21st Amendment interest for the court to consider, but not suggesting the outcome in *Rowe* would have been different had the case involved alcohol instead of cigarettes).

Gary, *Alcohol Beverages Regulation in Wisconsin* (2nd. Ed. 2016), at 6-22.

Another observer cited us to *US Airways, Inc. vs O'Donnell*, 627 F.3d 1318 (1st Cir. 2016) as an example of when a court may hold federal law preempts state regulation of alcohol. In *US Airways*, the Court of Appeals held that applying New Mexico's alcohol regulatory scheme to flights to and from New Mexico implicated the field of aviation safety that Congress intended to regulate exclusively, and it remanded for the district court to balance New Mexico's core powers and the federal interests underlying the FAA. Though the issue was never resolved because the case was dismissed without prejudice after the parties reached a settlement, the opinion is helpful where the Court of Appeals offered the following "guidance" to the district court:

The key inquiry in balancing state and federal interests is "whether the interests implicated by a state regulation are so closely related to the powers reserved by the Twenty-first Amendment that the regulation may prevail, notwithstanding that its requirements directly conflict with express federal policies." *Crisp*, 467 U.S. at 714, 104 S.Ct. 2694.

In conducting this balancing, the court should be guided by the following three-step framework:

First, the court should examine the expressed state interest and the closeness of that interest to those protected by the Twenty-first Amendment.... Second, the court should examine whether, and to what extent, the regulatory scheme serves its stated purpose.... Simply put, is the scheme effective? ... [T]he answer to this question may ultimately rest upon findings and conclusions having a large factual component. Finally, the court should balance the state's interest ... (to the extent that interest is actually furthered by the regulatory scheme) against the federal interest....

On balance, the Study Committee was not concerned about federal preemption. A drafting committee, if appointed, should confirm this conclusion.

Exhibits

Exhibit [A] – Memorandum from Stephen B Humphress to Steve Wilborn and John McGarvey suggesting consideration of a direct-to-consumers uniform act

Exhibit [B] - Roster of ABA Advisors and Observers

Exhibit [C] – Summary of Terms in Existing Direct to Consumer Sales of Spirits Acts

Exhibit [D] – Letter from Elyse and Diane have.

Exhibit [E] - Letter from Heather Calio of the Wine & Spirits Wholesalers of America

Exhibit [F] – Letter from Dan Farber of the American Craft Spirits Association

Exhibit [G] - Study on Underage Alcohol Orders by Rebecca Williams, MHS, PhD, and Kurt Ribisl, PhD

