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Mr. Steven G. Frost
Chairman
Uniform Law Commission
Study Committee on Direct to Consumer Sales of Wine, Beer, and Distilled Spirits
March 1, 2019

Steven,

We appreciate this opportunity to share our perspective on the subject of direct to consumer shipping expansion. As the ULC committee considers whether or not to move forward with drafting a uniform law regarding interstate shipment of spirits directly to consumers outside of a state's regulatory system, it is important to take a look at the realities of the current beverage alcohol shipping marketplace and the issues that have stemmed from the development of the wine shipping market.

The goal at this time in the committee's deliberations should not be "how" to create the same faulty environment for all beverage alcohol, but should be "if" lending credibility and weight to such a policy is in the ULC's best interest, consumers' best interest, and in the best interest of the states the ULC will recommend adopt these laws. Any decision on whether or not to move forward should absolutely answer whether or not creation of another marketplace outside of state control *can* adequately address any state regulatory and legal issues, which have real impacts not just to a state budget and in-state businesses' bottom lines, but on the public safety of consumers and non-consumers as well. Neither businesses nor consumers are well-served by an alcohol market that lacks appropriate regulatory oversight, undermines authority, and willfully enables bad actors.

Additionally, the Tennessee Retailer case currently before the U.S. Supreme Court will have a yet to be determined impact on the industry, and it would be unwise to act while that case is still pending.

WSWA does not believe this committee is in a position to recommend the drafting of any such uniform shipping expansion policies, and would strongly discourage moving forward with drafting.

Alcohol is unlike other products, and all policies surrounding its sale and distribution should take this into account. First and foremost, alcohol is an intoxicant and must be responsibly sold within a strong state-based regulatory structure. Not only has beverage alcohol been treated with caution in our nation's history and constitution, but each individual state was given the right to regulate alcohol in accordance with local customs, needs and social sensitivities- *meaning that alcohol laws were never meant to be uniform across all states*. Alcohol is regulated, and alcohol taxes are collected, differently in every state – even different among localities in certain states.

The 21st Amendment made the need for local control and respect very clear as it purposefully decentralized control of the alcohol marketplace. Respecting states' rights to regulate alcohol



sales within their borders under the 21st Amendment has been a key to a healthy alcohol marketplace, and a resounding success for over 85 years. The current three-tier system of alcohol distribution and sale works to serve customer needs and to keep the marketplace safe. It has prevented entrance of counterfeit product into retail stores for sales to consumers, and ensured the greatest variety of product available to consumers anywhere in the world.

This structure also allows for the market to innovate and answer consumer convenience needs without abandoning appropriate oversight. To insinuate that states must make a choice between proven public safety procedures and consumer choice is misleading, and ignores the many market solutions available to connect consumers with the products they desire within the established regulatory structure.

Before any policy advice is given that would further erode state regulatory authority, the full impact and extent of the current illegal shipping market must be further studied and dealt with. Therefore, it is our belief that consumers, businesses, and states would be better served by legislation and a ULC study to assist in a better understanding of the alcohol shipping marketplace through stronger methods of sales verification and enhancement of state enforcement abilities.

Many states are now facing the unfortunate situation of diverting state resources to identify illegal shipments of beverage alcohol that are undermining legitimate in-state businesses and eroding their tax base – which is harmful to consumers and non-consumers. Many state regulators still lack the appropriate tools to address this problem, which gives an advantage to illegal actors over legal businesses.

It is our belief that the committee would far better serve states by advocating for laws that empower states to look into the flow of untaxed and unlicensed alcohol over their borders – specifically by working to advance legislation that requires common carriers of alcohol shipments to report current beverage alcohol shipments to the state. This enables state regulators to compare the carrier list to their own license and tax data to identify illegal shippers and those who are not paying state taxes.

For example, requiring common carrier reporting recently allowed the Virginia ABC to identify over 650 **unlicensed** shipper entities. Over a four month period in 2018, the VA ABC discovered that over 38% of all alcohol shipments coming into the state of Virginia were unlicensed, untaxed, illegal shipments. This resulted in an estimated **excise tax loss** of over \$62,000. This does not account for other retail or local tax losses. The ABC testified that the “analysis of common carrier reports shows a multitude of violations.” (Virginia ABC Testimony before the Virginia Senate Finance Public Safety Subcommittee, January 8, 2019 http://sfc.virginia.gov/pdf/Public%20Safety/2019/010819_No1_ABC.pdf)

Keep in mind – most of these shippers COULD have obtained a license to ship legally into Virginia, but opted instead to circumvent the legal structure to evade taxes. Without carrier reporting, the high number of violators would have likely never been discovered, and Virginia



businesses and residents would have continued to pay the price for this illegal activity and tax evasion. As it is, however, even this “solution” requires an enormous amount of time and effort to pursue.

In the past, measures such as these were not necessary, as every sale within the three-tier system is verifiable through the chain of custody from licensee to licensee. This makes enforcement manageable. Wholesaler warehouses and retail stores can be inspected by state regulators to verify product and taxes paid, and existence of these in-state business ensure regulators are overseeing a manageable number of tax collection points. Expanding carve outs to this system not only increases the volume of bad actors and illegal sales that undermine in-state businesses, but creates an impossible regulatory challenge. Regulators from one state cannot accurately regulate the hundreds of thousands of alcohol suppliers and/or retailers from 49 other states and D.C.– they simply do not have the resources to accomplish this. Therefore, the abuse of state shipping laws is rampant, and state regulatory authority is constantly undermined at great cost.

Since the current shipping market has many problems that need addressing before any expansion is proposed, WSWA would respectfully recommend focusing on solutions to the issues at hand and developing better methods of preventing illegal sales and shipments, rather than opening up more avenues for these illicit sales to occur.

This issue is far too contentious, and nuanced, to benefit from a uniform policy, and is not a good candidate for this committee. Further, we have serious concerns that the scope of this committee is ill-defined and seems to have fluctuated from its original purpose and title. We also have concerns that not all stakeholders have been given adequate time to address such a broad set of complex issues, that the way in which each issue is considered is inconsistent, and that we do not have clear direction on process. For example, direct to consumer “Distillery” and “Retail” shipping are vastly different issues, with different impacts to states, yet they have been casually grouped together as this committee proceeds in its considerations, as if there is no difference.

Below are WSWA’s comments on the original proposed elements of a model spirits shipping bill that were provided at the outset of this committee. These comments reflect our experiences with these issues and the problems that arise with certain policies. **These comments are NOT in any way an endorsement of the proposed provisions. As we are continuously uncovering new issues, and the scope of the committee appears to change, these comments also likely do not encompass our final thoughts on the matter.**

We thank you again for the opportunity to submit our thoughts, and would strongly recommend the committee not move forward with the pursuit of a uniform law on this matter. We are happy to discuss further.

Sincerely,

Heather Calio
Senior Director, State Affairs
Wine and Spirits Wholesalers of America



ULC Proposed Spirits Shipping Elements are below, with WSWA's comments to each in italics and bold below the proposed elements.

Requirements for a license. The following potential requirements should be considered:

- 1) An applicant may be required to be licensed in the state where the customer is located (or where spirits are being shipped? Other?).

Yes. In addition, applicant should also be a proven DOMESTIC U.S. producer. Any product being sold by this applicant must be of their own production from a bonded production facility. This entity must hold the federal basic permit for a producer of beverage alcohol, and only ship products they actually produce. They must also be licensed as a manufacturer in the state of production. This will prevent an issue we have seen arise where non-producer entities use loopholes in state law to obtain a supplier license in one state, and use this to ship into other states in violation of their shipping laws.

- 2) The director of the licensing authority may have ability to determine that the person is capable and reliable and is qualified to hold a direct shipment license.

To ensure proper regulatory authority, this should be set out in statute, with other options for suspension.

- 3) The licensee may be required to consent to jurisdiction of agencies and courts of the licensing state and to audits of records and to maintenance of records for an appropriate period of time.

This should also include a "Reciprocal Enforcement" section, which would entail suspension of the entity's in-state license for violating laws in another state.

- 4) Deemed consent of jurisdiction for agencies to enforce these laws with respect to any person who knowingly ships to a purchaser in the licensing state.

Remove "Knowingly". There should also be penalties for shipments into dry territories.

- 5) Exemptions? Smaller licensees? (Nebraska provides an exception for wholesalers who may receive less than 3 gallons of wine per year from a person not licensed – is a similar exemption appropriate for wholesalers of spirits?)

There should be no exemptions for licensing. All participants in alcohol manufacture, sale and distribution should be held accountable for their sale of the product, and the market should be an even playing field. There should also be a prohibition for a retailer to ship itself beverage alcohol for resale (therefore avoiding state taxes). Nothing in this model should alter the privileges or permissions or restrictions that a state currently puts on their suppliers, retailers, and wholesalers and how they conduct

business with one another – this especially includes exempting certain out of state entities from the same requirements an in-state business must adhere to.

- 6) Is this license limited to producers or could wholesalers and retailers also ship under this act? (Nebraska and New Hampshire are examples of a state that allows “manufacturers” and others, including wholesalers and retailers of alcoholic liquor.)

This should be strictly limited to producers since they hold a federal basic permit that could be at stake. Retailers have no such equivalent permit or skin in the game, and therefore it is very difficult for states to enforce against out-of-state retailers that are illegally shipping. The license should never include anyone other than a federal basic permit holder. This should include an actual prohibition on an entity that is a retailer in any state or engages in retail activities.

- 7) How should fulfillment houses be treated for these purposes? Could a licensee use a fulfillment house for order processing, packaging and shipping? Would a wine club or other club be a fulfillment house for these purposes? How would licensing, reporting, and jurisdiction rules apply in these instances?

Fulfillment houses should be narrowly defined and licensed by any state they are shipping into. Fulfillment houses should have a permit or license with fee equivalent to wholesaler license fee. If a state allows the use of a fulfillment house, the producer must inform state of its use of a fulfillment house to ship its products.

States can create a “blacklist” of fulfillment houses that carriers cannot accept shipments from.

Fulfillment houses must submit monthly a list of entities/ wineries or retailers for whom they ship to each state/ are fulfilling orders.

The return address on any alcohol delivery package shall indicate that it came from a fulfillment center.

- 8) State would set license fees.

Fee should be equivalent to a supplier fee in the state, ensuring a level playing field for both in and out of state licensees.

Information included in application for license. Licensing may require disclosure of information regarding: 1) places of business, 2) person or persons authorized to represent the applicant in the licensing state, 3) disclosure of criminal convictions, 4) copies of current licenses (including a license in the state where located), 5) orders shipped to purchasers in the licensing state during prior [three] years, 6) applicant’s tax number issued by the department of revenue in licensing state, and 7) other information requested by licensing state.



Copies of current licenses should include ALL alcohol licenses in every state.

Statutory reasons to prohibit issuance of a license. Might include prior revocation of a license within [one] year of application and conviction of a felony within [five] years of application.

Also include: If applicant is a holder of a retail license ; If applicant has been shipping illegally in any state without a license/shipping products not allowed in the state/ evading taxes.

Bases of revocation of a license. [TBD]

Should Include: Nonpayment of taxes; illegally shipping into the state/ dry territories; violation of the shipping terms with a carrier; false statements about contents shipped; under-reporting actual sales gallonages into states; shipping in excess of state shipping limits.

Duration of license. [TBD]

Yearly, renewal dependent upon review of accurate reports and payment of taxes. Renewal fee same as initial license to ensure in-state businesses are on a level playing field.

Transferability of licenses. Licenses should explicitly be non-transferable.

Yes, and also product registration should be required.

Production and shipment limits. Limitations might include: 1) direct sales could be limited to smaller producers (if so, what limits would apply in measuring smaller producers?), 2) could include quantity limits on shipments, 3) could make explicit that licensee may only ship spirits produced by the licensee (if the licensee is a distillery) [Nebraska requires “manufacturers” to identify brands that will be sold in state], 4) New Hampshire allows lifting of limits for products not sold in New Hampshire, and 5) impose limits on shipments to licensees within state?

Gallonage should be equivalent to current state definitions of “small” distilleries/ wineries in state. Limited to products not available in the state otherwise/not in distribution.

Sale requirements imposed on licensees. Requirements might include: 1) licensee must verify the age of the purchaser and act should specify method of verification (e.g., copy of valid government photo identification), 2) a purchaser must have been eligible to carry wine lawfully within licensing jurisdiction, 3) only ship product owned by shipper, 4) not ship product wholesalers in licensing state have voluntarily agreed to not bring into state at request of state, 5) only permit shipment by common carrier, and 6) not permit sales into parts of a state where alcohol may not be sold.



Labeling requirements. For example, box must include statement to effect “contains alcohol, signature of person aged 21 or older required for delivery.”

Delivery requirements. Requirements may include: 1) delivery must be made to a person at least 21 years of age, 2) could require inspection by delivering agent of a valid government photo identification, and 3) could address whether stores, such as Walgreens or CVS, may accept shipment and deliver product after satisfying ID inspections of recipients.

Any store receiving such packages on behalf of consumer must be a licensee. If product is going to a retail licensee, it must pass through a distributor before it goes to a retailer. Delivery by unlicensed third party entities should be prohibited, and there must be clear definitions of “delivery” and “shipping”.

Payment. May require that payment must be collected by licensee not later than at time of delivery.

All payments processed by licensee - not an unlicensed third party- at the time of sale.

Licensee Reports with licensing state. Information required may include: 1) licensee must file a report [annually] describing shipments into jurisdiction during year, 2) require reporting of violations by shipper of home state violations or of direct shipping laws of other states, and 3) consider what information may be required by act.

Reports should be monthly and include tax liability. This should include the same information as carrier reports, to ensure for easier verification. It should also include if a shipment was fulfilled by a fulfillment house. If in-state licensees should have to post a bond, an out of state shipper should have to post a bond.

Penalties. Penalties for failure to comply with licensing jurisdiction’s direct shipment laws. [TBD]. New Hampshire also provides penalties for persons in New Hampshire that violate direct sale statutes of other states, including fines and suspension and revocation of New Hampshire liquor licenses.

This should include revocation of license and fines, as well as suspension. Penalties should be at least equivalent to penalties for the supplier in state illegal sale, if not stronger since the shipper is asking for additional privileges and should be held to a higher standard.

Common carrier requirements. Requirements may include: 1) should common carriers be required to maintain records, including records of product shipped to purchasers in licensing jurisdiction, including recipient names and addresses, shipment and delivery dates and products shipped. 2) Agreement by common carriers to remit records kept to authorities in licensing state.



3) Common carriers to report on whose behalf shipments are made within the jurisdiction to enable licensing state to audit licensees and check for illegal sales. Need to consider *Rowe v New Hampshire*, 128 S. Ct. 989 (2008).

Proposed language for Common Carrier Requirements: It shall be the duty of every railroad company, express company, common or contract carrier, and of every firm or corporation that shall bring, carry or transport wine, beer or distilled spirits [as defined by the state] from outside the State for delivery in the State to consumers, to prepare and file monthly with the Department [or on the same timeline as for licensed shippers of wine, beer or distilled spirits], a report of known wine, beer or distilled spirits shipments containing the name of the railroad company, express company, common or contract carrier, firm or corporation making the report, the period of time covered by said report, the name and business address of the consignor of such wine, beer or distilled spirits, the name and address of each consignee of such wine, beer or distilled spirits, the weight of the package delivered to each consignee, a unique tracking number, and the date of delivery. Reports received by the Department shall be made available by the Department to the public via the FOIA process in the same manner as other state alcohol filings.

Upon the Department's request, any records supporting the report, shall be made available to the Department within a reasonable time after the Department makes a written request for such records. Any records containing information relating to such reports shall be kept and preserved for a period of two years, unless their destruction sooner is authorized, in writing, by the Department, and shall be open and available to inspection by the Department upon the Department's written request. Reports shall also be made available to any law enforcement or regulatory body in the state in which the railroad company, express company, common or contract carrier making the report resides or does business.

Any railroad company, express company, common or contract carrier who willfully fails to make reports as provided by this section or any of the rules and regulations of the Department for the administration and enforcement of this section is subject to a notification of violation. In the case of a continuing failure to make reports, the railroad company, express company, common or contract carrier is subject to possible license suspension and revocation [if applicable based on state licensure requirements] at the Department's discretion.

Taxes.

1) Require licensees to pay taxes paid by domestic sellers and to add these taxes to sales price.

2) Require licensees to submit sworn returns with revenue agencies showing amount of product sold in state, accrued taxes and other information required by authorities.



- 3) Impose penalties for failure to pay tax when due, together with interest.
- 4) Consider electronic filing of returns (though more an issue for tax statutes that will not be addressed by uniform act).

Bonds.

Each direct shipment licensee that makes deliveries into state may be required to file a bond or bonds payable to state and conditioned on payment of all taxes, penalties and other obligations of direct shipment licensee. Amount of bond to be equal to [twice direct shipment licensee's estimated monthly tax, but not less than \$500]. Direct shipment licensees that have made timely payment of all taxes for the twelve consecutive months immediately preceding current month are exempt from bond requirement.

Make equivalent to in-state supplier compliance / waiving.