

Approved: 2-7-06
Date

MINUTES OF THE SENATE FEDERAL AND STATE AFFAIRS COMMITTEE

The meeting was called to order by Chairman Pete Brungardt at 10:30 a.m. on January 19, 2006 in Room 231-N of the Capitol.

All members were present.

Committee staff present:

Athena Andaya, Kansas Legislative Research Department
Dennis Hodgins, Kansas Legislative Research Department
Mary Ann Torrence, Revisor of Statutes Office
Connie Burns, Committee Secretary

Conferees appearing before the committee:

Tuck Duncan, KS Wine & Spirit Wholesalers Association
Greg Shipe, KS Viticulture & Farm Winery Assoc.
Norm Jennings, KS Grape Growers & Winemakers Assoc.
Amy Campbell, KS Association of Beverage Retailers
Dave Corbin, KS Dept of Revenue

Others attending:

See attached list.

Dan Hermes, Kansas Alcohol and Drug Service Providers Association appeared before the committee to request a bill introduction. The proposed bill would dedicate resources for problem gaming amending KSA 2005 Supp 79-4801 and 79-4806. (Attachment 1)

Senator Reitz made the motion that this request should be introduced as a committee bill. Senator Gilstrap seconded the motion. The motion carried.

SB 370 - Wine manufacturers permitted to sell wine directly to consumers subject to requirements to maintain three-tier distribution system

Chairman Brungardt opened the hearing on **SB 370**.

Tuck Duncan, Kansas Wine & Spirit Wholesalers, appeared before the committee in support of the bill. (Attachment 2) The bill allows consumers to order wine directly from a winery while requiring the delivery to be completed in a face-to-face transaction through a licensed retail establishment. This non-discriminatory approach, consistent with the new FDA bioterrorism rules for tracking beverage alcohol is also applied to instate producers as well as out of state producers. This action responds to concerns of the Court and still protect the Kansas's right to regulate alcohol sales through the three-tier system.

Greg Shipe, Kansas Viticulture & Farm Winery Association, spoke in opposition to the bill. (Attachment 3) The current bill makes absolutely no provision to help Kansas wineries by allowing direct shipping and urged the committee to amend the bill by incorporating the "direct shipping model."

Norm Jennings, Kansas Grape Growers & Wine Makers Association appeared neutral on the bill. (Attachment 4) Mr. Jennings recommended amending the bill with the "direct shipping model" currently in place in a majority of states that allow wine shipping, including those that have modified the laws after the Supreme Court ruling. This model allows for fast efficient deliveries, age verification, collection of all taxes, completely traceable shipments, annual reports and can include wording pertaining to "wine not currently distributed and locally available within the state."

Philip Bradley, Kansas Licensed Beverage Association, provided neutral testimony on the bill. (Attachment 5) The Association supports a workable legal bill that would allow for state control, equal regulation on underage access, appropriate tax collection and access to all sectors; the bill in its current

form needs adjustment to meet those criteria.

Amy Campbell, The Kansas Association of Beverage Retailers, provided neutral information on the bill. (Attachment 6) The Association supports a Task Force to study wine shipment laws and review the potential impact to Kansas and is willing to participate in a cooperative process to review the options and learn from the experiences of other states.

Dave Corbin, Department of Revenue Alcoholic Beverage Control, requested of the committee the time to review the bill as the Department had just received it. (Attachment 7) The bill would probably require one additional staff to track and monitor the process and account for the taxes owed to the State, and the proposed fee of \$25 does not come close to covering the projected costs foreseen in the administration and regulation of the provisions of the bill, and several statutory and regulatory amendments and internal policy changes would need to be implemented if the bill passes as written.

Chuck McGrigg and Larrie Ann Lower, Wine Institute provided written comments on the bill. (Attachment 8)

The meeting was adjourned at 11:58 am. The next scheduled meeting is January 24, 2006.

BILL No. _____
By Committee on _____

AN ACT concerning state gaming revenues, related to authorized uses, amending K.S.A. 2005 Supp. 79-4801 and 79-4806 and repealing the existing sections.

Be it enacted by the Legislature of the State of Kansas:

Section 1. K.S.A. 2005 Supp. 79-4801 is hereby amended to read as follows: 79-4801. State gaming revenues fund; authorized uses; limitation on amounts credited thereto; transfers to state general fund. There is hereby created the state gaming revenues fund in the state treasury. All moneys credited to such fund shall be expended or transferred only for the purposes and in the manner provided by this act and all expenditures from the state gaming revenues fund shall be made in accordance with appropriation acts. All moneys credited to such fund shall be allocated and credited monthly to the funds and in the amounts specified by this act except that the total of the amounts credited to such funds in any one fiscal year pursuant to this act shall not exceed ~~\$50,000,000~~ 53,000,000. All amounts credited to such fund in any one fiscal year which are in excess of ~~\$50,000,000~~ 53,000,000 shall be transferred and credited to the state general fund on July 15, 1996, and June 25, 1997, and each year thereafter on June 25.

Section 2. K.S.A. 2005 Supp. 79-4806 is hereby amended to read as follows: 79-4806. Transfers to problem gambling grant fund. On July 1 of each year or as soon thereafter as sufficient moneys are available, ~~\$80,000~~ 3,080,000 credited to the state gaming revenues fund shall be transferred and credited to the problem gambling grant fund established by K.S.A. 2004 Supp. 79-4805, and amendments thereto.

Section 3. K.S.A. Supp. 79-4801 and 79-4806 are hereby repealed.

Section 4. This act shall take effect and be in force from and after July 1, 2007.

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**Kansas Wine & Spirits
Wholesalers Association
212 SW 8th Avenue, Suite 202
Topeka, Kansas 66603
785-233-9370**

**R.E. "Tuck" Duncan
Executive Secretary and
General Counsel**

January 19, 2006

To: Senate Federal and State Affairs Committee
From: R.E. "Tuck" Duncan
RE: SB 370

We support SB370 as introduced.

The United States Supreme Court ruled on May 16 that states must treat in-state producers of alcohol the same as out-of-state producers of alcohol. Initially this decision did not have an immediate impact on Kansas, but this ruling requires that laws on the books in our state not give a preference to in-state alcohol producers over out of state producers. Our state is now faced with a stark choice: to allow unregulated, unaccountable alcohol sales -- which is clearly unacceptable -- or develop an alternative system where all alcohol sales be sold in face-to-face transactions through the state's licensed system, a system that has served Kansas well since 1949.

Some of the proponents of unregulated alcohol sales characterized the Supreme Court's decision inaccurately as their spin was that the Court endorsed the concept of the direct sale of alcohol. Nothing could be further from the truth. Those who so proclaimed have a vested interest in loosening restrictions on alcohol and we believe it has become clear that their goal is to cripple Kansas' and other the states' licensed system of sales and distribution. In reality the decision of the Court clearly reaffirmed the principle that the 21st Amendment to the Constitution gives states "virtually complete control over whether to permit importation or sale of liquor and how to structure the liquor distribution system." However, it also made clear that state authority does not extend to giving "discriminatory preference" to in-state producers.

Kansas now has a policy decision to make. We recognize that alcohol is a socially sensitive product and no segment of the industry should be allowed to bypass our licensed system while avoiding our taxes. As such all alcohol sales should be done face-to-face, where a retailer licensed by the state to sell to the consumer checks IDs. In addition, out-of-state retailers in some states are demanding the right to ship directly to in-state consumers. Neither did the recent decision did not sanction out-of-state retailers not licensed by Kansas to ship to Kansans when Kansas law does not permit Kansas retailers to ship to Kansans.

Sen Fed & State Affairs
1-19-06
Attachment 2

Kansans do not want to eliminate alcohol regulation thereby creating an "alcohol anarchy" in our markets leaving the state with little ability to track sales, collect taxes, keep alcohol away from minors, or ensuring orderly markets. SB370 allows consumers to order wine directly from a winery while requiring the delivery to be completed in a face-to-face transaction through a licensed retail establishment. This non-discriminatory approach, consistent with the new FDA bioterrorism rules for tracking beverage alcohol is also applied to instate producers as well as out-of-state producers.

By taking action in this manner, you will both respond to the concerns of the Court and still protect the Kansas's right to regulate alcohol sales through the "unquestionably legitimate" three-tier system. In doing so, you will also ensure the integrity of our revenue collection system and keep important barriers in place to keep beverage alcohol out of the hands of those who consume it irresponsibly or who are too young to purchase it legally.

We propose two amendments to the bill:

1. Eliminate the supplier-direct-to-retail provision in the farm winery law as follows:

Chapter 41.--INTOXICATING LIQUORS AND BEVERAGES

Article 3.--LICENSING AND RELATED PROVISIONS; CITY OPTION

41-308a. Farm winery license; rights of licensee. (a) A farm winery license shall allow:

- (1) The manufacture of domestic table wine and domestic fortified wine and the storage thereof;
- (2) the sale of wine, manufactured by the licensee, to licensed wine distributors, ~~retailers, clubs, drinking establishments and caterers;~~
- (3) the sale, on the licensed premises in the original unopened container to consumers for consumption off the licensed premises, of wine manufactured by the licensee;
- (4) the serving on the licensed premises of samples of wine manufactured by the licensee or imported under subsection (f), if the premises are located in a county where the sale of alcoholic liquor is permitted by law in licensed drinking establishments; and
- (5) if the licensee is also licensed as a club or drinking establishment, the sale of domestic wine, domestic fortified wine and other alcoholic liquor for consumption on the licensed premises as authorized by the club and drinking establishment act.

BUT do not make the elimination of the foregoing provisions effective until January 1, 2008 to allow wineries to adjust their marketing activities; and,

2. ADD the following language to the rights of a farm winery licensee:

- (6) the sale and shipment of wine manufactured by the licensee to persons or entities in other states in conformity with the laws of the foreign states.

If you have any questions regarding this matter please do not hesitate to give me a call.
Thank you for your attention to and consideration of this matter.

Kansas Viticulture and Farm Winery Association

January 19, 2006

To: Senate Federal & State Affairs Committee

From: Greg Shipe

On behalf of: Kansas Viticulture and Farm Winery Association

(Member Kansas Farm Wineries include: Davenport Vineyard & Winery;
Holy-Field Vineyard & Winery; Somerset Ridge Vineyard & Winery;
Slough Creek Vineyard & Winery.)

RE: SB370-Opposed

Mr. Chairman and members of the committee, thank you for the opportunity to offer this testimony. The Kansas Viticulture and Farm Winery Association is a Kansas association of farm wineries, grape growers and Kansas wine enthusiasts. We support the growth of grape growing and winemaking in Kansas using Kansas-grown grapes. We believe grape-growing offers Kansas farmers an exciting and lucrative crop alternative and that the current farm winery statute affords the opportunity for Kansans to grow, produce, market and sell a value-added Kansas agricultural product, while increasing agri-tourism within the state.

Let me first state that we support and concur with the testimony offered by Norm Jennings on behalf of the Kansas Grape Growers & Wine Makers Association. He points out the many defects in the current bill being offered.

By way of additional testimony, we would first note that the primary interest of our members is to have all sales channels available to promote and sell our Kansas wine. Currently, Kansas Farm Wineries are prohibited by state law from directly shipping to consumers either within or outside of the state. This makes no economic or regulatory sense. Our Kansas wineries get literally thousands of requests yearly to ship our wines all over the state and the country. We lose significant sales of Kansas product and Kansas tax revenues every year because of this prohibition. The current bill makes absolutely no provision to help Kansas wineries by allowing direct shipping. That is the primary reason we oppose the bill.

The farm winery statutes could easily be amended to allow direct shipments to consumers into the state *and* to allow Kansas wineries to direct ship in state and out of state, while collecting taxes on all those transactions and satisfying the US Supreme Court decision in *Granholm v. Heald*. We urge the committee to amend this bill by incorporating the suggested direct shipping legislation attached to this letter.

If the committee believes adopting the current bill would be the best method for collecting taxes on direct wine shipments, we respectfully submit that that belief is

illusory. The current bill would make it so cumbersome, unwieldy and expensive for an individual consumer to ship wine into the state that we would be surprised if a single transaction actually took place. This scheme is not the current trend being adopted by other states. It is difficult to see the current bill as anything but a roadblock to direct shipping that is primarily designed to protect the already considerable interests of the two major wine wholesalers in the state.

Thank you again for the opportunity to offer testimony this morning.

41-308a

Chapter 41.--INTOXICATING LIQUORS AND BEVERAGES Article 3.-- LICENSING AND RELATED PROVISIONS; CITY OPTION

41-308a. Farm winery license; rights of licensee. (a) A farm winery license shall allow:

(1) The manufacture of domestic table wine and domestic fortified wine and the storage thereof;

(2) the sale of wine, manufactured by the licensee, to licensed wine distributors, retailers, clubs, drinking establishments and caterers;

(3) the sale, on the licensed premises in the original unopened container to consumers for consumption off the licensed premises, of wine manufactured by the licensee;

(4) the serving on the licensed premises of samples of wine manufactured by the licensee or imported under subsection (f), if the premises are located in a county where the sale of alcoholic liquor is permitted by law in licensed drinking establishments; and

(5) if the licensee is also licensed as a club or drinking establishment, the sale of domestic wine, domestic fortified wine and other alcoholic liquor for consumption on the licensed premises as authorized by the club and drinking establishment act.

(6) the direct shipping, in the original unopened container to consumers within the State of Kansas, of wine manufactured by the licensee; provided that the licensee ensures that all containers of alcoholic beverages shipped directly to a resident in this state are conspicuously labeled with the words "CONTAINS ALCOHOL: SIGNATURE OF PERSON AGE 21 OR OLDER REQUIRED FOR DELIVERY."

(7) the direct shipping, in the original unopened container to licensed retailers, clubs, drinking establishments and caterers, of wine manufactured by the licensee.

(8) the direct shipping, in the original unopened container to consumers outside of the State of Kansas, of wine manufactured by the licensee; provided that the licensee complies with all relevant laws and regulations of the governmental entity into which the wine is shipped.

(b) Upon application and payment of the fee prescribed by K.S.A. 41-310, and amendments thereto, by a farm winery licensee, the director may issue not to exceed two winery outlet licenses to the farm winery licensee. A winery outlet license shall allow:

(1) The sale, on the licensed premises in the original unopened container to consumers for consumption off the licensed premises, of wine manufactured by the licensee; and

(2) the serving on the licensed premises of samples of wine manufactured by the licensee or imported under subsection (f), if the premises are located in a county where the sale of alcoholic liquor is permitted by law in licensed drinking establishments.

(c) Not less than 60% of the products utilized in the manufacture of

domestic table wine and domestic fortified wine by a farm winery shall be grown in Kansas except when a lesser proportion is authorized by the director based upon the director's findings and judgment. The label of domestic wine and domestic fortified wine shall indicate that a majority of the products utilized in the manufacture of the wine at such winery were grown in Kansas.

(d) A farm winery having a capacity of 50,000 gallons per year or more which sells wine to any distributor shall be required to comply with all provisions of article 4 of chapter 41 of the Kansas Statutes Annotated and of K.S.A. 41-701 through 41-705 and 41-709, and amendments thereto, in the same manner and subject to the same penalties as a manufacturer.

(e) A farm winery or winery outlet may sell domestic wine and domestic fortified wine in the original unopened container to consumers for consumption off the licensed premises at any time between 6 a.m. and 12 midnight on any day except Sunday and between 12 noon and 6 p.m. on Sunday. If authorized by subsection (a), a farm winery may serve samples of domestic wine, domestic fortified wine and wine imported under subsection (f) and serve and sell domestic wine, domestic fortified wine and other alcoholic liquor for consumption on the licensed premises at any time when a club or drinking establishment is authorized to serve and sell alcoholic liquor. If authorized by subsection (b), a winery outlet may serve samples of domestic wine, domestic fortified wine and wine imported under subsection (f) at any time when the winery outlet is authorized to sell domestic wine and domestic fortified wine.

(f) The director may issue to the Kansas state fair or any bona fide group of grape growers or wine makers a permit to import into this state small quantities of wines. Such wine shall be used only for bona fide educational and scientific tasting programs and shall not be resold. Such wine shall not be subject to the tax imposed by K.S.A. 41-501, and amendments thereto. The permit shall identify specifically the brand and type of wine to be imported, the quantity to be imported, the tasting programs for which the wine is to be used and the times and locations of such programs. The secretary shall adopt rules and regulations governing the importation of wine pursuant to this subsection and the conduct of tasting programs for which such wine is imported.

(g) A farm winery license or winery outlet license shall apply only to the premises described in the application and in the license issued and only one location shall be described in the license.

(h) No farm winery or winery outlet shall:

(1) Employ any person under the age of 18 years in connection with the manufacture, sale or serving of any alcoholic liquor;

(2) permit any employee of the licensee who is under the age of 21 years to work on the licensed premises at any time when not under the on-premise supervision of either the licensee or an employee of the licensee who is 21 years of age or over;

(3) employ any person under 21 years of age in connection with mixing or dispensing alcoholic liquor; or

(4) employ any person in connection with the manufacture or sale of alcoholic liquor if the person has been convicted of a felony.

(i) Whenever a farm winery or winery outlet licensee is convicted of a violation of the Kansas liquor control act, the director may revoke the licensee's license and order forfeiture of all fees paid for the license, after a hearing before the director for that purpose in accordance with the provisions of the Kansas administrative procedure act.

(j) This section shall be part of and supplemental to the Kansas liquor control act.

History: L. 1983, ch. 161, § 3; L. 1985, ch. 170, § 25; L. 1987, ch. 182, § 141; L. 1988, ch. 165, § 1; L. 1990, ch. 178, § 1; L. 1992, ch. 201, § 2; L. 1998, ch. 191, § 3; July 1.

Kansas Grape Growers & Wine Makers Association

February 19, 2006

To: Senate Federal & State Affairs Committee

From: Norman M. Jennings

On behalf of: Smoky Hill Vineyards & Winery (Owner)

Kansas Grape Growers & Wine Makers Association (Legislative Chair)

RE: SB370 (Neutral)

Mr. Chairman and members of the committee, thank you for the opportunity to offer this testimony. The Kansas Grape Grower & Wine Maker Association (KGGWA) is a state association established by the growers and wineries of Kansas, with the mission statement of furthering the growth and development of both of these industries, and therefore the economic impact in Kansas. The grape and wine industry in Kansas is one that has the potential to be a major contributor to the state agritourism and value-added agricultural industries, as well as state alcohol tax revenue sources. Over the past 3 years, we have seen the considerable growth in both these industries, evidenced by the number of wineries increasing from 7 to 16 and grape acreage set to double within 5 or less years.

The Kansas Grape Grower & Wine Makers Association supports shipping of wine. Shipping is an important method of providing access to our products. SB370 on the surface would allow for customers to have access to wines that are not currently available to them, but is used in very few states. Following are our comments on the nature of this bill.

1. Section 1-c-3 seems to make it illegal for a restaurant owner, retailer, winery, etc... to have access to the same wines as the residents of Kansas would. Provisions should be made for "personal use" and not for "resale" purposes.
2. Section 5-b notes a paperwork system that rivals the most cumbersome systems in existence. Five total pieces of paper that can be "lost" at anytime, resulting in the failure to properly deliver and collect taxes on the shipment.
3. Section 6-c states the distributor is not to place the shipment into their system, rather deliver it with the next delivery. Note that these shipments are not on a traceable grid!

4. Section 7-c notes the retailer will contact the customer, but does not state the method. This can lead to shipments not picked up "promptly", resulting in what we do not know as the bill does not address this issue.
5. Section 8-b notes the customer must "promptly" take delivery, but does not define "promptly", nor does it define what the retailer is to do if the customer is not prompt.
6. Section 8-c-3 allows for a fee of \$5. Given this nice sized payment, some retailer may just prefer to gather their margin in this fashion. For a \$15 bottle of wine this profit can equal that of the winery. Additionally the fee must be known by the customer in advance.
7. Section 9-b is the big "catch-22". By not wording this as "locally available", a small town resident is not allowed the same access as some around the corner from one of the big wine retail stores.
8. Section 10-b seems to set up a shipping label that would list the shipping winery (from), receiving distributor (to) and the retailer (second to?) the customer has selected. We can not see the means in which this label will be done.

In all, we see this bill as a very confusing, management burdened and cost prohibitive way of allowing Kansas Residents to obtain wine. Placing my self in the customer shoes, I may just give up knowing it will take many weeks to get here, having to making sure I could find time in my busy schedule to "promptly" go across town and pick-up the wine and the general fear that I just may never get what I paid my money to receive. This system has often resulted in "lost" wine after they are taken off the traceable shipping grid (Fed Ex, etc...) and fall between the distributor and retailer. In these cases, the dispute is not between if it made it from the distributor to the retailer or even if the retailer did call and leave a message, rather that the wine shipper collected payment for something that was not received. In that case, go back to step one, generate 5 invoices, etc...

So, what is the answer? We recommend the direct shipping model currently in place in the vast majority of the states that allow wine shipping, including those that have modified their laws after the Supreme Court ruling. This model allows for fast efficient deliveries, age verification, collection of all taxes, completely traceable shipments, annual reports and can include wording pertaining to "wine not currently distributed and locally available within the state".

Again, we support the legal shipping of wine allowing Kansas residents to have the access to the same wines the residents of the states that borders Kansas have access to. We would strongly advise amending this bill to that of the direct shipping model attached to this letter. If that is not possible, this frustrating and cumbersome method may be better than nothing for the residents of Kansas. Thank you for the time and opportunity to offer this testimony.

MODEL DIRECT SHIPMENT BILL

Adopted by the National Conference of State Legislatures, Task Force On The Wine Industry, November 5, 1997, Washington D.C. Proposed by Family Winemakers of California, Coalition for Free Trade, The Wine Institute and the American Vintners Association.

Add new Section ---- to the Alcohol Beverage Control Act as follows:

1. Notwithstanding any law, rule or regulation to the contrary, any person currently licensed in any other state as an alcoholic beverage producer, supplier, importer, wholesaler, distributor or retailer who obtains an out-of-state shipper's license, as provided below, may ship up to twenty-four (24) bottles per month of any alcoholic beverage directly to a resident of [State] who is at least 21 years of age for such resident's personal use and not for resale.
2. Before sending any shipment to a resident of [State] the out-of-state shipper must first:
 - (a) File an application with the Department of Alcoholic Beverage Control (Department),
 - (b) pay a \$50.00 registration fee,
 - (c) provide to the Department a true copy of its current alcoholic beverage license issued in another state, and
 - (d) obtain from the Department an out-of-state shipper's license.
3. All out-of-state shipper licensees shall:
 - (a) Not ship more than twenty-four (24) bottles per month to any person.
 - (b) Not ship to any address in an area identified by the Department as a "dry" or local option area.
 - (c) Ensure that all containers of alcoholic beverages shipped directly to a resident in this state are conspicuously labeled with the words "CONTAINS ALCOHOL: SIGNATURE OF PERSON AGE 21 OR OLDER REQUIRED FOR DELIVERY."
 - (d) Report to the Department annually the total of alcoholic beverages, by type, shipped into the state the preceding calendar year.
 - (e) Annually pay to the [State Revenue Agency] all sales taxes and excise taxes due on sales to residents of [State] in the preceding calendar year, the amount of such taxes to be calculated as if the sale were in [State] at the location where delivery is made.
 - (f) Permit the Department or the [State Revenue Agency] to perform an audit of the out-of-state shipper's records upon request.
 - (g) Be deemed to have consented to the jurisdiction of the Department or any other state agency and the [State] courts concerning enforcement of this section and any related laws, rules or regulations.
4. The out-of-state shipper may annually renew its license with the Department by paying a \$10.00 renewal fee and providing the Department a true copy of its current alcoholic beverage license issued in another state.
5. The Department and the [State Revenue Agency] may promulgate rules

and regulations to effectuate the purposes of this law.

6. The Department may enforce the requirements of this section by administrative proceedings to suspend or revoke an out-of-state shipper's license, and the Department may accept payment of an offer in compromise in lieu of suspension, such payments to be determined by rule promulgated by the Department.
7. Shipments of alcoholic beverages from out-of-state direct to consumers in [State] from persons who do not possess a current out-of-state shipper's license or other permit or license from the Department are prohibited, Any person who knowingly makes, participates in, transports, imports or receives such a shipment from out-of-state is guilty of a misdemeanor punishable by [insert fine and/or jail]. Without limitation on any punishment or remedy, criminal or civil, any person who knowingly makes, participates in, transports, imports or receives such a shipment from out-of-state commits an unfair trade practice.

41-308a

Chapter 41.--INTOXICATING LIQUORS AND BEVERAGES Article 3.--LICENSING AND RELATED PROVISIONS; CITY OPTION

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(2) the sale of wine, manufactured by the licensee, to licensed wine distributors, retailers, clubs, drinking establishments and caterers;

(3) the sale, on the licensed premises in the original unopened container to consumers for consumption off the licensed premises, of wine manufactured by the licensee;

(4) the serving on the licensed premises of samples of wine manufactured by the licensee or imported under subsection (f), if the premises are located in a county where the sale of alcoholic liquor is permitted by law in licensed drinking establishments; and

(5) if the licensee is also licensed as a club or drinking establishment, the sale of domestic wine, domestic fortified wine and other alcoholic liquor for consumption on the licensed premises as authorized by the club and drinking establishment act.

(6) *the direct shipping, in the original unopened container to consumers within the State of Kansas, of wine manufactured by the licensee; provided that the licensee ensures that all containers of alcoholic beverages shipped directly to a resident in this state are conspicuously labeled with the words "CONTAINS ALCOHOL: SIGNATURE OF PERSON AGE 21 OR OLDER REQUIRED FOR DELIVERY."*

(7) *the direct shipping, in the original unopened container to consumers outside of the State of Kansas, of wine manufactured by the licensee; provided that the licensee complies with all relevant laws and regulations of the governmental entity into which the wine is shipped.*

(b) Upon application and payment of the fee prescribed by K.S.A. 41-310, and amendments thereto, by a farm winery licensee, the director may issue not to exceed two winery outlet licenses to the farm winery licensee. A winery outlet license shall allow:

(1) The sale, on the licensed premises in the original unopened container to consumers for consumption off the licensed premises, of wine manufactured by the licensee; and

(2) the serving on the licensed premises of samples of wine manufactured by the licensee or imported under subsection (f), if the premises are located in a county where the sale of alcoholic liquor is permitted by law in licensed drinking establishments.

(c) Not less than 60% of the products utilized in the manufacture of domestic table wine and domestic fortified wine by a farm winery shall be grown in Kansas except when a lesser proportion is authorized by the director based upon the director's findings and judgment. The label of domestic wine and domestic fortified wine shall indicate that a majority of the products utilized in the manufacture of the wine at such winery were grown in Kansas.

(d) A farm winery having a capacity of 50,000 gallons per year or more which sells wine to any distributor shall be required to comply with all provisions of article 4 of chapter 41 of the Kansas Statutes Annotated and of K.S.A. 41-701 through 41-705 and 41-709, and amendments thereto, in the same manner and subject to the same penalties as a manufacturer.

(e) A farm winery or winery outlet may sell domestic wine and domestic fortified wine in the original unopened container to consumers for consumption off the licensed

premises at any time between 6 a.m. and 12 midnight on any day except Sunday and between 12 noon and 6 p.m. on Sunday. If authorized by subsection (a), a farm winery may serve samples of domestic wine, domestic fortified wine and wine imported under subsection (f) and serve and sell domestic wine, domestic fortified wine and other alcoholic liquor for consumption on the licensed premises at any time when a club or drinking establishment is authorized to serve and sell alcoholic liquor. If authorized by subsection (b), a winery outlet may serve samples of domestic wine, domestic fortified wine and wine imported under subsection (f) at any time when the winery outlet is authorized to sell domestic wine and domestic fortified wine.

(f) The director may issue to the Kansas state fair or any bona fide group of grape growers or wine makers a permit to import into this state small quantities of wines. Such wine shall be used only for bona fide educational and scientific tasting programs and shall not be resold. Such wine shall not be subject to the tax imposed by K.S.A. 41-501, and amendments thereto. The permit shall identify specifically the brand and type of wine to be imported, the quantity to be imported, the tasting programs for which the wine is to be used and the times and locations of such programs. The secretary shall adopt rules and regulations governing the importation of wine pursuant to this subsection and the conduct of tasting programs for which such wine is imported.

(g) A farm winery license or winery outlet license shall apply only to the premises described in the application and in the license issued and only one location shall be described in the license.

(h) No farm winery or winery outlet shall:

(1) Employ any person under the age of 18 years in connection with the manufacture, sale or serving of any alcoholic liquor;

(2) permit any employee of the licensee who is under the age of 21 years to work on the licensed premises at any time when not under the on-premise supervision of either the licensee or an employee of the licensee who is 21 years of age or over;

(3) employ any person under 21 years of age in connection with mixing or dispensing alcoholic liquor; or

(4) employ any person in connection with the manufacture or sale of alcoholic liquor if the person has been convicted of a felony.

(i) Whenever a farm winery or winery outlet licensee is convicted of a violation of the Kansas liquor control act, the director may revoke the licensee's license and order forfeiture of all fees paid for the license, after a hearing before the director for that purpose in accordance with the provisions of the Kansas administrative procedure act.

(j) This section shall be part of and supplemental to the Kansas liquor control act.

History: L. 1983, ch. 161, § 3; L. 1985, ch. 170, § 25; L. 1987, ch. 182, § 141; L. 1988, ch. 165, § 1; L. 1990, ch. 178, § 1; L. 1992, ch. 201, § 2; L. 1998, ch. 191, § 3; July 1.



*Kansas
Licensed
Beverage
Association*

President
James "Jim" Fager

Vice Presidents
Tammy Davis
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Robert Farha
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Curt Melzer
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Testimony on SB-370, January 19, 2006
Senate Federal and State Affairs Committee

Mr. Chairman, and Senators of the Committee,

I am Philip Bradley representing the Kansas Licensed Beverage Assn., the men and women, in the hospitality industry, who own and manage bars, clubs, caterers, restaurants, breweries and hotels where beverage alcohol are served. Thank you for the opportunity to submit testimony today.

We support a workable legal bill that would allow for state control, equal regulation on underage access, appropriate tax collection and access to all sectors.

A level playing field for those who sell alcohol is essential. Currently a seller of beverage alcohol is held criminally responsible for an under ager accessing their product , *knowingly or unknowingly*. The same standards must apply to these sales.

We also urge you to create access to unavailable products to those licensees who wish to feature a particular label for a small batch purchase. Many of our fine Kansas hospitality venues have customers that are requesting these products and would like to promote small vineyards for their patrons.

Of course we support the appropriate steps necessary to achieve all of these goals and still have a workable system. It appears that this measure in it's current form needs adjustment to meet those criteria.

Thank you for your time.

Philip Bradley
Executive Director

Drink Responsibly.
Drive Responsi

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The Kansas Association of Beverage Retailers

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Martin Platt, President

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**TESTIMONY PRESENTED TO THE
SENATE COMMITTEE ON FEDERAL AND STATE AFFAIRS
January 19, 2006
Amy A. Campbell, Executive Director**

Thank, Chairman Brungardt and members of the committee for the opportunity to represent the Kansas Association of Beverage Retailers regarding Senate Bill 370. Our members are Kansas citizens who own Kansas businesses.

Our members appreciate the intent of the proposed legislation in meeting the requirements of the recent Supreme Court decision. In drafting the bill, great care has been taken to address concerns which have been raised in the past and to streamline the process as much as possible. Clearly, the process allows for the safe and legal sale of the product to someone of legal age, it preserves the three tier distribution system (putting everyone on equal footing), collects the taxes and provides a legal method for consumers to purchase product not currently available to them.

As Kansas retailers, we are still a bit uneasy with the current proposal, primarily due to the possibility of unintended consequences. We would be most comfortable maintaining the current prohibition on shipping for both the in-state wineries and the out-of-state wineries because we know that the Court has upheld our current law.

However, if it is imperative that Kansas law be altered, KABR encourages the Kansas Senate to pass a joint resolution to establish a task force which would include the state agencies who are responsible for enforcing and defending the Liquor Control Act: the Division of ABC and the office of the Attorney General. The task force would also include parties who would be participants in any altered distribution system.

Without the "buy-in" of the ABC and Attorney General, the new system will prove ineffective and possibly inefficient. The ABC will need to be able to provide retailer information to the wine sellers in an efficient manner and information about the wine sellers to the retailers. We do not want to go down another legislative trek which creates unforeseen enforcement issues against retailers who accept shipments from the wrong seller or perhaps the wrong buyer. This bill suggests that a restaurant owner could not purchase wine from a direct wine seller for his or her own use. This is probably a good policy, but who enforces it? Would the retailer be expected to refuse such a sale? Would the ABC be required to follow up on a complaint of this nature? What happens if the customer does not pick up the product?

Does the Attorney General's office feel confident that this language would stand up in federal court? What about manufacturers who want to sell their distilled spirits or specialty beers? Does the bill need a definition of wine?

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Retailers are happy to seek new solutions to provide access to more products for our customers. It appears that this could be an excellent method to do so.

Three years ago, KABR testified in support of House Concurrent Resolution 5016 which charged the attorney General and the Division of ABC with the task of studying wine shipment laws and reviewing the potential impact to Kansas. That Task Force was never convened – at least in part to the pending Supreme Court decision. There are no simple answers to the questions that arise related to shipping, and we are willing to participate in a cooperative process to review the options and learn from the experiences of other states.

Thank you again for the opportunity to speak to this issue. Please be aware that more information may be forthcoming as our members have the opportunity to review the language of this legislation.

Please feel free to contact me to discuss this or any other issue:

Amy A. Campbell

Mobile: 785-969-1617



K A N S A S

JOAN WAGNON, SECRETARY

DEPARTMENT OF REVENUE
ALCOHOLIC BEVERAGE CONTROL

KATHLEEN SEBELIUS, GOVERNOR

**Before Federal & State Affairs
ABC's Concerns with SB 370 as introduced
January 19, 2006**

Ladies and Gentlemen:

ABC received a copy of the bill before you yesterday and the agency feels that it needs additional time to review and analyze all possible statutory, regulatory, licensing and taxation affects. What we have discovered so far is that this bill will probably require at least one additional staff to track and monitor the process and account for the taxes owed to the State. Also, the proposed fee of \$25 does not come close to covering the projected costs foreseen in the administration and regulation of the provisions of this bill. Additionally, a cursory review of the liquor control act reveals several statutory and regulatory amendments and internal policy changes that will need to be implemented if the bill passes as written.

A brief example of a concern is Section 4, subsection (g), which as written would require KDOR/ABC to perform a background check on applicants. ABC is not permitted to access the federal criminal database except for criminal investigations, and accessing criminal conviction databases of other states will be time consuming and may incur additional fees. Additionally, under subsection (g) of Section 4, a violation of any law would disqualify an applicant. This would include all misdemeanor convictions and traffic offenses, and the subsection as written states that only violations of law by the entity are relevant, not violations of the law by the officers or majority holders of the entity.

ABC is currently in the process of performing a section by section review of the bill and will have this information available to the Committee next week. We respectfully ask the Committee to allow ABC to provide it with additional information before acting upon the bill.



WINE INSTITUTE

CHARLES E. MCGRIGG
CENTRAL STATES COUNSEL

January 19, 2006

TO: MEMBERS OF FEDERAL AND STATE AFFAIRS
FROM: CHUCK MCGRIGG, LARRIE ANN LOWER
SUBJECT: SB 370 SALE AND SHIPMENT OF WINE

Mister Chairman and members of the Committee. We appreciate the opportunity to provide written comments on SB 370 which attempts to allow the sale and shipment of wine into the state of Kansas.

The Wine Institute is a trade association comprised of some nine hundred wineries. The Wine Institute strongly supports the concept of granting Kansas consumers the ability and privilege to purchase and have wine shipped to them. We do have several concerns with SB 370.

Page 1 Sec.3. (2) ship such wine to a licensed distributor, who shall deliver the wine to a licensed retailer, designated by the personal consumer, for the ultimate delivery to the personal consumer at the retailer's licensed premise.

This concept was attempted in Massachusetts and has not been successful due to the multi level of deliveries. *(See Attachments)*

Page 2 Sec.4.(f) registers with the office of the secretary of state to do business within this state: and

This section has the potential of unintended consequences. It requires further recordkeeping and could trigger further tax liability.

Page 2 Sec. 4. (g) passes a background check . . .and regulations of this state.

These entities are licensed in other states. We are not aware of this provision contained in any other direct shipping legislation.

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Page 4 Sec. 9. (a) A personal consumer shall not receive more than 24 bottles of wine in total from one or more direct wine sellers in a calendar month.

This provision does not include an enforcement mechanism. Our research indicates that New York and California have recently reacted to the Supreme Court case on this issue and have eliminated bottle limits in their legislation.

Page 4 Sec. 9. (b) A direct wine seller shall not sell in this state a wine that is distributed in this state by a licensed wine distributor.

This provision also lacks an enforcement mechanism and leads to much consumer and winery confusion.

Finally, included at the end of page 2 and pages 3 & 4 are the requirements a consumer, supplier, wholesaler, and retailer must complete in order for the consumer to receive their wine. These types of requirements have been unsuccessfully attempted in other jurisdictions. Either the legislation has not passed, has been vetoed or there is actual direct shipping activity in that state due to these restrictions.

The Wine Institute has advocated for a change to direct shipping limitations for over twenty-five years. However, it is our belief that the legislation before you does not realistically allow for the direct sale and shipping of wine to Kansas Consumers. We will be happy to continue to work with the Committee and the interested parties on this issue. Thank you for your interest in this topic, we will try to answer any questions you may have.

State Gross Revenue from Alcohol Permits

Permits Issued FY 2005		Revenue Annual Fee	Collected	Total
22	Alcohol Awareness Program	\$15.00	\$330.00	
324	Alcohol Awareness Instructor	5.00	1,620.00	
16	Public Storage	75.00	1,200.00	
14	Public Storage and Transportation	100.00	1,400.00	
447	Public Transportation	75.00	33,525.00	
12	Import and Export	75.00	900.00	
1,036	Non-Resident Dealer	100.00	103,600.00	
49	Individual Storage	50.00	2,450.00	
2,049	Solicitor's	50.00	102,450.00	
302	Bulk Transfer	100.00	30,200.00	
52	Change of Domicile	5.00	260.00	
10	Non-Beverage	50.00	500.00	
55	Individual Transportation	10.00	550.00	
53,265	Vehicle Identification Cards	10.00	532,650.00	
1	Wine Exhibition	50.00	50.00	
17	Non-Resident Storage	500.00	8,500.00	
10	Charity Wine Auction	10.00	100.00	
2	Family Beer and Wine	400.00	800.00	
1	Direct Wine Sellers	10.00	10.00	
2	Private Bulk Sale	25.00	50.00	
15	Winery Special Event	25.00	375.00	
<hr/>				
57,701				
Grand Total Permits Issued				<u><u>\$821,520.00</u></u>

Note: The permit year begins November 1st and ends the following October 31st.

Romney re-files legislation to regulate mail-order wine shipments

January 17, 2006

BOSTON --Gov. Mitt Romney favors Massachusetts residents buying wine by mail, but after a failed effort to regulate sales by the Legislature last fall, he is proposing new guidelines himself.

Under a bill filed Tuesday, the governor is proposing unrestricted wine sales, saying they would "satisfy consumer demand for choice in wine without imposing burdensome restrictions on this type of commerce."

The bill also includes safeguards aimed at preventing minors from buying liquor illegally, such as a requirement that someone of legal drinking age sign for the package.

Massachusetts consumers have been able to buy mail-order wine without restriction since the Supreme Court approved such wine shipments last year. Yet last fall, the Legislature passed a bill limiting state residents to purchases from wineries producing no more than 30,000 gallons a year.

Romney vetoed that measure, calling it anti-consumer. The Legislature never tried to override the veto.

A Romney aide said the new bill brings a regulatory framework to the sales allowed by the Supreme Court decision. It would also allow consumers to bring home unused bottles of wine from restaurants, a provision in the vetoed bill that the governor supported. ■

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These comments are intended to address constitutional, public policy, and other legal issues which may arise if states legislate in the area of direct shipments by either (a) allowing only wineries of a certain size to be eligible for the shipment privilege or (b) by denying wineries the right to sell wine through the use of licensed wholesalers if the winery chooses to sell wine directly to consumers.

While *Granholm* addresses factual circumstances where the discrimination against interstate commerce is much more obvious (i.e., prohibiting out-of-state wineries from shipping but allowing in-state wineries to ship direct to consumers), the *Granholm* decision focused its discussion on whether the object and design of the Michigan and New York statutes grant to in-state wineries a competitive advantage over out-of-state wineries.

Winery Size Restrictions:

Legislatures contemplating statutory remedies to cure *Granholm*-type discrimination will look to different solutions that will eliminate the facially obvious impact on interstate commerce. One of the ways that has been suggested by some legislators is to remove the apparent language of discrimination in favor of a classification that would be border-neutral, yet may have border-specific effect. Allowing wineries of a specific size the ability to ship wine direct to consumers is still discrimination.

Legislators take their cues from the existence of federal and state laws that address the plight of the small business and attempt to provide incentives or advantages to small, as opposed to larger, businesses. These laws, like the federal Regulatory Flexibility Act (5 USC 601, et seq., which seek to provide regulatory relief from compliance burdens by requiring efforts to tailor regulations so that the impact on small businesses is reasonable, justified and necessary) have not been Constitutionally scrutinized for its effects on interstate commerce. In the case of the Regulatory Flexibility Act, the application of the law is nationwide and to all businesses regardless of where situated, and the national interest is clearly articulated.

In the case of direct shipments, however, the discriminatory effect on interstate commerce may very well be the same, regardless of whether a statute discriminates on its face against out of state wineries or impliedly discriminates based on winery size. For example, if a state with wineries that do not exceed a specific size passed a law that would permit only wineries of that size or smaller to ship directly to consumers, one could argue that the discrimination against interstate commerce complained about in *Granholm* has been cured, since wineries that meet the size requirement, regardless of where situated, could avail themselves of the shipping privilege. However, it is not only the statutory language, but also the effect, that is subject to Constitutional review. While legislation may modify the discriminatory character of the shipping privilege, both *Granholm* and its predecessor, *Bacchus v. Dias*, look to the *effect* of the statute to assess its Constitutional soundness. In other words, simply replacing the language of a statute to disguise an otherwise interstate

discriminatory effect will not save a statute from Constitutional scrutiny. A statute that is discriminatory in effect is no less an interstate commerce clause violation.

Language in *Granholm*, *Bacchus*, and other cases repeat this principle and is relevant to this discussion. From *Granholm*:

Finally, and most relevant to the issue at hand, the Court has held that state regulation of alcohol is limited by the nondiscrimination principle of the Commerce Clause. *Bacchus*, 468 U. S., at 276; *Brown-Forman Distillers Corp. v. New York State Liquor Authority*, 476 U. S. 573 (1986); *Healy v. Beer Institute*, 491 U. S. 324 (1989). **“When a state 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.”** *Brown-Forman, supra*, at 579.

The development of statutory language that, in one form or another, results in economic protectionism and in-state preferences, will bring into question whether the holding in *Granholm* has been adequately met. While such language suggestions may have been tolerable in a pre-*Granholm* world, the Supreme Court decision provides us with some guidance as to how to structure Constitutionally sound legislation (all quotes from *Granholm*):

- **A state statute cannot mandate differential treatment of in-state and out-of-state interests when it results in a preference for in-state businesses.**

Time and again this Court has held that, in all but the narrowest circumstances, state laws violate the Commerce Clause if they mandate “differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter.” *Oregon Waste Systems, Inc. v. Department of Environmental Quality of Ore.*, 511 U. S. 93, 99 (1994). See also *New Energy Co. of Ind. v. Limbach*, 486 U. S. 269, 274 (1988).

- **The 21st Amendment is not a defense to Commerce Clause violations.**

State laws that discriminate against interstate commerce face “a virtually per se rule of invalidity.” *Philadelphia v. New Jersey*, 437 U. S. 617, 624 (1978).

- **Legislation that is discriminatory in effect is as much a Commerce Clause violation as legislation that is discriminatory on its face (see above).**

Making Direct Shipments Exclusive of Wholesale Distribution

While the licensing provisions appear to be consistent with other states' laws that have adopted the model legislation, the Massachusetts legislation contains a troubling provision which mandates a forced, statutory election to be made by wineries. Wineries must decide whether to have their brands distributed by wholesalers, or through the licensed direct shipment system. Devoid of reasons for requiring this election, the forced election provision is a glaring departure from the model direct shipments legislation.

Granholm instructs us that States, in the exercise of their 21st Amendment power, cannot discriminate in interstate commerce. The current Massachusetts legislation removes the more obvious interstate commerce element and substitutes in its place a requirement that raises a more disguised form of discrimination, in addition to antitrust, consumer, and protectionist concerns. While the legislature properly attempts to remove any interstate discrimination element, whether on its face or in effect, it substitutes provisions that will invite litigation and public scrutiny because of the consumer and antitrust issues the legislation raises.

When one analyzes what is being attempted by the Massachusetts legislation in the context of the continuing rhetoric of direct shipments, one of the most significant developments is in what is NOT being advocated; the original arguments espoused by wholesaler groups appears to have been forsaken in favor of a more direct and concentrated political statement from the anti-direct shipping lobby. By requiring provisions that force wineries to make a choice, at the outset, about how its products should be sold in the state of Massachusetts, the proposed legislation makes the wholesale distribution channel unavailable to a winery who chooses to exercise its direct shipment rights. There is no flexibility in this initial decision: a winery must either choose to ship directly to consumers, or ship through wholesale licensees, and this decision may be influenced as much by existing distribution contracts that a winery cannot extract itself from, even if it wishes to choose to ship direct.

While the requirement is clear, the effect of the requirement and the reasons for it remain unexplained. Massachusetts' forced election provision removes a viable distribution method for wineries that choose to ship direct. Silent with respect to the reasons for why wineries must make such an election, the effects of such a provision can be characterized as punitive and anticompetitive. The legislative analysis must include the identification of eligible wineries who can take advantage of such a privilege, and whether the provisions are fair and responsive to the principles of competition.

The legislation creates two separate kinds of wineries: those that ship direct to consumers, and those that do not. Those that do not will retain the ability to sell products to wholesalers who will sell products to retailers. Retail opportunities, once available to wineries from out of state, will be denied for those choosing to ship direct to Massachusetts consumers. As with monopoly protection laws, also unique to the alcoholic beverage industry, the Massachusetts legislation is more an example of political power than common sense. Instead of gaining Constitutionally recognized

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rights in *Granholm*, the legislation seeks to take away the distribution system once available to wineries that choose to direct ship. In this way, the legislation perpetuates in-state economic protectionism, with the result now recast as wholesaler protectionism.

Only a Small Group of Out-of-State Wineries Will Be Eligible for The Direct Shipment Privilege

Monopoly protection laws do not exist in any other commodity sector for any other product, from agriculture to pharmaceuticals to telecommunications because of their antitrust affect. The current legislation only strengthens the wholesaler's monopoly by removing those wineries that interfere with their business by shipping direct to consumers.

Existing Massachusetts monopoly protection statute currently requires out-of-state wineries shipping into the state to sell through wholesalers, and makes it unlawful for an out-of-state winery to refuse to sell to a wholesaler after six months of regular sales.¹ The current direct shipment legislation does not provide any relief from the monopoly protection statute. Wineries that have relationships with wholesalers in Massachusetts cannot discontinue shipping wine to these wholesalers because of the operation of the monopoly protection law, negating any gains for Massachusetts consumers. The only wineries that will be able to take advantage of the direct shipment privilege are those wineries that currently do not have a retail presence within the state.

Notwithstanding the interplay of the current legislation with existing monopoly protection law, the forced-election provisions of the current legislation substitutes the *Granholm* type discrimination for a system that creates an environment that will stifle competition and increase consumer prices. It is the very kind of state action that renders alcoholic beverage regulation so perplexing. If one were to apply the same principles embodied in the current legislation to any other goods or services, it would meet with great consumer opposition. If you can imagine a talented musician being told that he or she can sell his music either through the internet, or through retail music stores, but not both, the public would be left to ponder the wisdom of the legislature. Similarly, forcing automobile producers to sell either at dealer lots or on the internet, or insurance as an either/or proposition, would strongly suggest something punitive.

The Internet is a revolutionary means of communication and commerce that can dramatically enhance consumer sovereignty and promote robust competition, but its benefits are only available if access is kept open, unfettered, and unbiased. For out-

¹ Massachusetts Chapter 138, Section 25E, states, in part:

“It shall be an unfair trade practice and therefor unlawful for any manufacturer, winegrower, farmer-brewer, importer or wholesaler of any alcoholic beverages, to refuse to sell, except for good cause shown, any item having a brand name to any licensed wholesaler to whom such manufacturer, winegrower, farmer-brewer, importer or wholesaler has made regular sales of such brand item during a period of six months preceding any refusal to sell.”

of-state wineries, Massachusetts' current direct shipment legislation isolates the internet and divides the winery retail wine market into web-based and non-web-based components, the web-based environment consisting not only of wineries who can ship direct to consumers, but retailers as well.

Wineries should not be forced to weigh the commercial impact of one distribution system over the other. As with automobiles and insurance, the world has not been completely destroyed by allowing products to be sold in the best possible way. As the political rhetoric over direct shipments evolves and industry and legislators learn to respond to the impact of *Granholm*, we need to examine early solutions to determine whether they are disguised forms of discrimination or result in unintended, inappropriate, or inadequate results in other public policy areas. We would refer legislators to the findings of the Federal Trade Commission with respect to anticompetitive barriers to e-commerce for further information.²

Bullet points follow.

- **Proposed Legislation Perpetuates a Wholesaler Monopoly**

The legislation is disingenuous because while it appears to grant direct shipment privileges to a small class of eligible wineries, the class is actually even smaller through the operation of the monopoly protection law. Notwithstanding the market division that the forced election provision creates, the legislation provides no relief from the operation of the monopoly protection statute which requires wineries to sell to wholesalers after a relationship is established. Wineries already with a presence in Massachusetts are required by statute to make their products available to wholesalers within the state. Those wineries that are outside the operation of that law are forced to make an election and will not be able to take advantage of wholesale distribution efficiencies if they decide to ship direct. The overall effect of the legislation maintains the status quo of wholesalers. Massachusetts consumers will not realize any significant increase in product availability, because most wineries will not be eligible to take advantage of the direct shipment privilege.

Even removing the impact of the monopoly protection law on the market, the public policy conclusion is overwhelmingly clear: conditioning entry into a distribution arrangement with wholesalers based on a promise by the winery that it will not ship direct to consumers makes little sense at the start of this century of internet availability.

² FTC workshop information, testimony, and conclusions are at <http://www.ftc.gov/>. The FTC's agenda, participants' written statements, and public submissions in the agency's Public Workshop on the Possible Anticompetitive Efforts to Restrict Competition on the Internet are available at <http://www.ftc.gov/opp/e-commerce/anticompetitive/index.htm>. Legislators should also be directed to the Progressive Policy Institute's web page on removing obstacles to e-commerce beginning at http://www.ppionline.org/ppi_ci.cfm?contentid=251950&knlgAreaID=139&subsecid=272.

The current Massachusetts legislation is an Old Economy restraint of trade, intended more to secure the wholesaler's place as the exclusive conduit for wine in the state's retailer channel.

As with music distribution and automobile sales, new economy mechanisms are an option for the market, not a condition of distribution. Imagine requiring a recording artist to make a decision about whether his or her music can be sold through prerecorded music CDs OR iTunes, but not both? Or informing consumers that products sold on TV must make a choice about whether it can be sold online or in stores?

Why should wholesalers be given such statutory protection in a distribution scheme where it holds a traditional monopoly on goods sold to the public? What is the state interest that requires such protection?

The model market that the legislation should emulate is an open market, tempered only by articulable state interests that the legislation seeks to address. In this case, the legislation is silent on that point.

- **The Legislation Will Result in Higher Consumer Prices**

The legislation creates a vertical restraint of trade that will result in higher consumer prices and less availability and frustrates open and vigorous competition. Higher consumer prices, because wineries are forced to segregate their markets and compete in only one of them. Those wineries choosing to sell direct will be required to remove their brands from retail shelves, and consumers will eventually be victimized by market forces and laws that preclude competitors from reentering the retail sector.

There is no state that requires such an election, and states that allow direct shipments to coexist with three-tier distribution report no problem. American economic history is filled with industries that use government to protect their markets when buffeted by change, but it wasn't a good idea then, and it isn't a good idea now. We encourage legislators to embrace a free market economy where consumer choices, not vested interests, determine how commerce is structured. Policy should be decided on its merits, not on the interests of the disintermediated. We respectfully suggest that the marketplace, not the government, be the factor that determines business winners and losers.

- **The Legislation is Punitive**

The legislation does not protect any articulated state interest. It is punitive and is meant to evade Granholm, but not respond to it.

The Granholm arguments of taxes and control and the state's assertion of its power under the 21st Amendment failed to persuade the Supreme Court that the discrimination against out-of-state wineries was justified.

(b)

With no expression of the state's interest, the Massachusetts legislation advances an equally oppressive statute, its apparent purpose to perpetuate the wholesaler's market position for wine within the state. The effect of the proposed legislation is a division of markets by punishing direct shippers with loss of retail shelf space. This quid pro quo is unjustified, protects no state interest, and only serves to punish consumers and direct shippers.

- **The Legislation Provides No Relief from the Monopoly Protection Laws**

The legislation provides no relief from existing distribution contracts that wineries have with wholesalers. Wineries may not have the legal ability to exit existing distribution contracts.

More importantly, the public policy goal of legislation should be to establish available methods of distribution, but not to require that participants decide on one to the exclusion of other methods. Distribution decisions should remain private ones, best left to the competitor with the ability to contract with vendors for services and performance.

- **The Legislation is a Restraint of Trade**

The legislation is a state-mandated and anticompetitive market division, contrary to the principles of open and fair competition. The legislation corrals out-of-state wineries into those that have a relationship with a wholesaler and those that don't, and forcing those that don't into a Hobson's Choice: either take your chances selling wine directly to consumers, or pay the markup and find a presence in retail establishments. The prevailing public policy interest, that the more competition, the better it is for consumers, is clearly not a factor.

Granholm did not remove the right of the state to legislate and regulate alcoholic beverages, but it did proclaim that states may not discriminate in doing so. Commerce Clause discrimination, whether on its face or in effect, will not meet the holdings in *Granholm*.

Hopefully this will provide you with some insight into the potential legal issues raised by Sen. Morrissey's proposed draft direct shipping legislation of 10/6/05.

Respectfully submitted,
Carol Martel
Northeastern Counsel
Wine Institute

