

**INTERSTATE ALCOHOL SALES AND
THE 21ST AMENDMENT**

HEARING

BEFORE THE

COMMITTEE ON THE JUDICIARY

UNITED STATES SENATE

ONE HUNDRED SIXTH CONGRESS

FIRST SESSION

ON

EXAMINING ISSUES RELATING TO INTERSTATE ALCOHOL SALES, INCLUDING LABELING, QUALITY CONTROL STANDARDS, CONSUMER FRAUD, AND ACCESS OF ALCOHOL BY MINORS AS WELL AS PROPOSED LEGISLATION THAT WILL PERMIT THE ATTORNEY GENERAL OF A STATE TO FILE AN ACTION IN FEDERAL COURT FOR AN INJUNCTION TO STOP ILLEGAL SHIPMENT OF ALCOHOL

MARCH 9, 1999

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INTERSTATE ALCOHOL SALES AND THE 21ST AMENDMENT

TUESDAY, MARCH 9, 1999

U.S. SENATE,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The committee met, pursuant to notice, at 10 a.m., in room SD-226, Dirksen Senate Office Building, Hon. Orrin G. Hatch (chairman of the committee) presiding.

Also present: Senators Grassley, Specter, Kyl, DeWine, and Feinstein.

OPENING STATEMENT OF HON. ORRIN G. HATCH, A U.S. SENATOR FROM THE STATE OF UTAH

The CHAIRMAN. Good morning. Today, the Judiciary Committee will hear testimony concerning the growing business of interstate shipments of alcohol. Unfortunately, along with that growing business, problems associated with that trade are also growing. While I certainly believe that interstate commerce should be encouraged, and I do not want small businesses stifled by unnecessary or overly burdensome and complex regulations, I do not subscribe to the notion that purveyors of alcohol are free to avoid State laws which are consistent with the power bestowed upon them by the 21st amendment.

All States, including the State of Utah, need to be sure that the liquor that is brought into their State is labeled properly and subject to certain quality control standards. States need to protect their citizens from consumer fraud and have a claim to the tax revenue generated by the sale of such goods. And of the utmost importance, States need to ensure that minors are not provided with unfettered access to alcohol. Unfortunately, indiscriminate direct sales of alcohol have opened a sophisticated generation of minors to the perils of alcohol abuse.

I can tell you that my own home State of Utah, which has some of the strictest controls in the Nation on the distribution of alcohol, is not immune from the dangers of direct sales. Take a look at this story which ran on KUTV in Salt Lake City last Tuesday. If we can take time, we will put this story on.

[Videotape shown.]

The CHAIRMAN. If that story doesn't bother you, it should. If a 13-year-old is capable of ordering beer and having it delivered merely by, "borrowing," a credit card and making a few clicks with their mouse, there is something wrong with the level of control that is being exercised over these sales. Of course, the Utah case is not

just an isolated example. Stings set up by authorities in New York and Maryland have also shown how easy it is for minors to obtain alcohol.

The 21st amendment was ratified in 1933. That amendment ceded to the States the right to regulate the importation and transportation of alcoholic beverages across their respective borders. By virtue of that grant of authority, each State created its own unique regulatory scheme to control the flow of alcohol. Some set up, "State stores," to effectuate control of the shipment into and dissemination of alcohol within their States. Others refrained from direct control of the product, but set up other systems designed to monitor the shipments and ensure compliance with their laws. But whatever the type of State system enacted, the purpose was much the same, and that is to protect its citizens and ensure that its laws were obeyed.

Although not perfect, the systems set up by the States worked reasonably well for many years. However, it is apparent that modern technology has opened the door for abuse and created the need for further governmental action to address those abuses. No longer must a State prosecute just an errant neighborhood retailer for selling to a minor. Now, the ones selling to minors and others, in violation of a State's regulatory laws, are a continent away.

A small winery can create its own web page and accept orders over the Internet. A large retailer can advertise nationally in the New York Times and accept orders over the phone. An ad can be placed in a magazine with a national circulation offering sales through an 800 number. Let me emphasize that there are many companies engaged in the direct interstate shipment of alcohol who do not violate State laws, and that needs to be emphasized. In fact, many of these concerns look beyond their own interests and make diligent efforts to disseminate information to others to ensure that State laws are understood and complied with by all within the interstate industry.

I should note that I am certainly sympathetic to the small wineries and the specialty micro-breweries who feel that the requirement that they operate through a three-tier system—that is, producer-wholesaler-retailer—which does not embrace them may, in effect, shut them out of the marketplace. They make the argument that if wholesalers do not carry their product, they have no other avenue to the consumer other than through direct sales. However, if there is a problem with the system, we need to fix the system, not break the laws.

Later today, I will introduce a bill entitled the Twenty-First Amendment Enforcement Act. Federal law already prohibits the interstate shipment of alcohol in violation of State law. Unfortunately, that general prohibition lacks any enforcement mechanism. The bill I am introducing simply provides that mechanism by permitting the attorney general of a State, who believes that his or her State laws regulating the importation and transportation of alcohol are being violated, to file an action in Federal court for an injunction to stop these illegal shipments. The bill is balanced to ensure due process and fairness to both the State bringing the action and the company or individual alleged to have violated the State's laws.

The bill, No. 1, permits the chief law enforcement officer of a State to seek an injunction in Federal court to prevent the violation of its laws regulating the importation or transportation of alcohol. No. 2, it allows for venue for the suit where the defendant resides and where the violations occur.

No. 3, it does not permit an injunction without notice to the opposing party. No. 4, it requires that any injunction be specific as to the parties, the conduct, and the rationale underlying that injunction.

No. 5, it allows for quick consideration of the application for an injunction and conserves court resources by avoiding redundant proceedings. No. 6, it mandates a bench trial. And, No. 7, it does not preclude other remedies allowed by law.

Now, some will make the argument that State courts are capable of handling this issue. Unfortunately, States have had mixed success in enforcing their laws through State court actions. Companies and individuals have raised jurisdictional, procedural and legal defenses that have stalled these efforts, and that continue to hamper effective law enforcement. It is, in part, because of those inconsistent rulings that Federal leadership is needed in this area.

Moreover, the scope and limitations of a State's ability to effectively enact laws under the 21st amendment are essentially Federal questions that need to be decided by a Federal court, and perhaps ultimately by the Supreme Court. Only through such rulings can both the States and companies seeking to conduct interstate shipments be assured of consistency in interpretation and enforcement of the laws.

Of course, the hearing today will help us understand the issues involved, and I am sure the individuals providing testimony will greatly enlighten us and give us guidance in passing effective legislation to deal with these problems. It is my hope that at the end of the day we can reach an agreement on how best to balance legitimate commercial interests with the constitutional rights of the States as ceded to them by the 21st amendment.

So with that, let me just say that Senator Leahy regrets that he cannot be here to help open this hearing. He is at an Appropriations hearing with the Attorney General, where certainly I would want him to be, and he asks that the hearing proceed so as not to inconvenience the witnesses who traveled here to testify this morning, and, of course, our Representatives who are here with us today who we appreciate taking time from their busy schedules to come over and be with us.

So we will begin today.

Senator FEINSTEIN. Mr. Chairman, may I enter a statement into the record, being the one who represents California, which has 90 percent of the winemaking business in America?

The CHAIRMAN. We will enter all statements in the record, certainly yours.

[The prepared statement of Senator Feinstein follows:]

PREPARED STATEMENT OF HON. DIANNE FEINSTEIN, A U.S. SENATOR FROM THE
STATE OF CALIFORNIA

I share the concerns of members of this committee regarding underage drinking. However, we must be careful to address this problem directly, and not by legislation

which purports to target underage drinking, but instead would do little to address that problem and much to harm legitimate businesses in the wine industry, stifle the growth of electronic commerce, and diminish consumer choice.

I am proud to say that California is the home of more than 800 wineries, which produce over 90 percent of our nation's wine. The vast majority of these wineries are small, family farms. The wine industry is a vital sector of California's economy. Winegrapes are grown in 45 of California's 58 counties. The industry accounts for 112,000 permanent jobs and another 40–50,000 seasonal jobs in my state, and generates an estimated \$10.9 billion in economic activity in California. This results in more than \$335 million annually in state and local tax revenues in California. More than 10 million citizens from across the country visit California's wineries each year.

I'd like to welcome two representatives of California's wine industry to the committee today. John DeLuca has been the President and Chief Executive Officer of the Wine Institute for more than 20 years. Before, that, he served for seven years as Deputy Mayor of San Francisco, to Mayor Joseph Alioto. In addition to his service to California's wine industry, John also serves as Co-Chairman of California's Advocating Responsible Education.

Michael Ballard is the owner of one of California's small, family wineries, Savannah-Chanel Vineyards in Saratoga, California, and a leader in the high-tech industry in California. It's a pleasure to welcome both of you to the committee today.

Nationally, there are over 1,600 wineries in the U.S. Indeed, wine is America's third-largest horticultural export. Most of these wineries produce several different varieties—cabernet, chardonnay, etc. Sheer arithmetic tells you that a retail store cannot possibly have even the shelf space to offer more than a mere sample of this multitude of American wines.

Direct shipment of wine, therefore, is vital to the hundreds of small wineries who cannot fit on the shelf of the local store. By the same token, consumers and wine connoisseurs who appreciate hard-to-find wines also rely on direct shipment of wine, whether over the phone, by mail or through the Internet.

Indeed, the Internet presents a tremendous opportunity for small wineries to grow their business and for wine consumers to dramatically increase the wine selection to which they have ready access. Congress should be working to promote and encourage electronic commerce, not taking steps which could stifle and chill its growth.

At the same time, the growth of electronic commerce presents an economic threat to those who profit from the existing commercial structure. In many states, alcohol sales are controlled through a very limited number of wholesalers and distributors, who, of course, take a profit on every wine sale made through them, through the so-called "three tier system." Direct shipments threaten their business, and many winery owners believe that it is these middlemen who are behind this legislation, and who are funding organizations who promote its passage. I also note that a coalition supporting this legislation contains national alcohol wholesalers and retailer organizations.

While there is a risk that youths can use the Internet to obtain alcohol, I am not convinced that the magnitude of the danger is sufficient to justify stifling small wineries and electronic commerce. Virtually all the examples of youths using the Internet to obtain alcohol involve youths who were *prompted* to do so, usually by a local news organization. I have seen precious few examples of youths on their own initiative deciding to obtain their alcohol by ordering it over the Internet, waiting days or weeks for shipment, and managing to be home without their parents at just the crucial time when it arrives. Indeed, it seems quite unlikely that youths will be ordering thirty dollar bottles of wine over the Internet in sufficient scale to present a national problem.

In contrast, an operation by Virginia's Alcoholic Beverage Control found *37 percent of retailers sold alcohol illegally to minors*—in half the cases even after checking IDs. This would seem to be where the *real* problem is.

Indeed, it is important to take real-world experience into account. Congressman Mike Thompson, who I am pleased to have here today along with my other Golden State colleagues George Radanovich and Juanita Millender-McDonald, will testify in greater detail about this, but I hope he will not mind if I preview this testimony by mentioning that California allowed direct shipments of wine in-state for more than 30 years, and California's Alcoholic Beverage Control Department has stated that, quote, "the sale-to-minor issue is overblown," end quote, and that, with more than 10,000 complaints investigated annually, they have received but *one* complaint about minors obtaining alcohol by direct shipment—the minor son of a Kentucky package store owner who ordered beer from California, and whose *mother* signed for the package when it was delivered.

One justification offered for this legislation was a Utah court decision that Utah could not enforce its alcoholic beverage control laws against an out-of-state beer-of-the-month club, which shipped directly into Utah. However, this decision turns out to have been wrong, at least according to the Utah Court of Appeals. In a decision announced *after* this hearing was noticed, just last Thursday, the Utah Court of Appeals reversed the lower court's decision, and reinstated the state's case. This obviously raises questions about the necessity for federal legislation on the subject.

Others argue that federal legislation is needed to enforce state tax laws. However, the annual sales of Dell Computers, which relies entirely upon shipment, are greater than those of the entire California wine industry, which relies primarily upon retail sales. And yet I don't hear anybody offering federal legislation for states to use federal courts to enforce their tax laws against interstate computer shipments.

Indeed, the entire subject of laws governing the taxation of electronic commerce is slated to be studied by the Advisory Commission on Electronic Commerce, which was established under the Internet Tax Freedom Act which the Congress passed—by an overwhelming majority—just last year. Prudence would dictate that we give the commission the opportunity to study and report on this issue before singling out one industry for special treatment.

There also is concern that states could use this legislation to enforce in federal court state laws whose intent is to discriminate against out-of-state commerce. In *Bacchus Imports v. Dias*, the Supreme Court struck down a Hawaii alcohol tax for just this reason, holding that the 21st Amendment did not justify discriminating against interstate commerce to provide a commercial advantage to local business. I would like to *ask unanimous consent that a letter from the noted constitutional scholar, Professor Jesse Choper, former Dean of Boalt Hall School of Law, raising this concern, be placed in the record.*

Professor Choper states in his letter that this bill:

goes far beyond simply providing a remedy for a violation of Webb-Kenyon. Instead it makes fundamental changes in current law and in doing so affects serious constitutional and public policy issues * * * Most significantly, it would run counter to the spirit of Bacchus and remove the protection that the Commerce Clause grants the alcoholic beverage industry, along with all others, from state erection of barriers to free trade.

So I think it is important that we proceed cautiously, Mr. Chairman, and not enhance the economic interests of some industry sectors against small family farms, while chilling electronic commerce.

Senator KYL. Mr. Chairman, I would like to do the same, and also just note the fact that while the Internet is just exploding new opportunities for commerce, including those of the wine industry and many others, the problem you identify is very similar to the problem we identified last year with Internet gambling.

The same kind of click-on technology that you displayed in that TV story was enough for all 50 State attorneys general to come to the Congress and actually ask us to pass a Federal law creating the same kind of injunctive, or similar injunctive relief that you have in your legislation to permit them to stop that kind of illegal activity. And I will certainly be looking forward to working with you on this legislation to achieve the same kind of objective. Incidentally, we are going to be reintroducing that Internet gambling bill next week.

The CHAIRMAN. Well, thank you, Senator, and we will move ahead on that basis.

At this point, I would like to enter into the record a statement submitted by Senator DeWine.

[The prepared statement of Senator DeWine follows:]

PREPARED STATEMENT OF HON. MIKE DEWINE, A U.S. SENATOR FROM THE STATE OF OHIO

I would like to commend Chairman Hatch for holding this hearing today on interstate alcohol sales. This is a very important topic, and it will become increasingly

important in the future, as the Internet becomes a conduit for more and more alcohol sales. Today's hearing will be a good opportunity to explore some of the issues raised by this popular form of interstate commerce.

I am especially concerned about one particular aspect of this industry—sales of alcohol to minors. Often minors are able to order alcohol from out-of-state suppliers, without providing proof of age, and have alcohol delivered right to their doorsteps. This practice is a threat to the safety and welfare of our children, and we need to find a way to eliminate it. I look forward to working with the other members of this Committee to address this very important issue.

The CHAIRMAN. The first panel today is comprised of four distinguished Representatives from the House.

Congressman Robert Ehrlich is a third-term Congressman from the Second District of Maryland. He serves on the Budget and Banking Committees in the House. Congressman Ehrlich is as concerned as I am with the ability of States to be able to enforce their laws regulating the importation and shipment of alcohol. And in the 105th Congress, Congressman Ehrlich sponsored a measure similar to the one I have now introduced in the Senate.

Congresswoman Juanita Millender-McDonald is now in her second term from California's 37th District in the U.S. House of Representatives. As I recall, you serve on the Committee on Transportation and Infrastructure and the Committee on Small Business, where you are the ranking member of the Subcommittee on Tax, Finance, and Exports.

Congressman George Radanovich is now in his third term from California's 19th District. He serves on the House Budget and Resources Committees. Before coming to Congress, his public service included elective office as a county supervisor, as well as being a member and chairing the Mariposa County Planning Commission.

However, Congressman Radanovich is first and foremost a farmer. In fact, Congressman Radanovich is the first full-time winemaker to serve in Congress. The Radanovich Winery produces some 4,000 cases annually and, as I understand, pretty high-quality wine, at that.

Representative RADANOVICH. Thank you.

The CHAIRMAN. Of course, how would I know? [Laughter.]

I wouldn't.

Finally, on the first panel we have with us first-term Congressman Mike Thompson, from the First District of California, which is one of the premier wine-growing regions of this country. We are really honored to have you with us as well. In the House, Congressman Thompson serves on the Agriculture and Armed Services Committees. He is a decorated Vietnam veteran, and I might add that Congressman Thompson is also a former small vineyard owner.

So I think we have a pretty balanced panel here and I am really looking forward to hearing what you have to say. We would like you to keep your remarks short, if you can, because we have a rather long hearing. We will start with you, Representative Ehrlich, and then we will go on right across the table.

STATEMENT OF HON. ROBERT L. EHRLICH, JR., A U.S. REPRESENTATIVE IN CONGRESS FROM THE STATE OF MARYLAND

Representative EHRLICH. Thank you, Mr. Chairman. In the interest of time, I have a statement I would like to submit for the record.

The CHAIRMAN. Without objection, we will put all statements of all witnesses in the record as though fully delivered. And, of course, we hope you can summarize.

Representative EHRLICH. Thank you. It is great to be here with you in this great committee, as well as with my friends here. Congresswoman Millender-McDonald has been a leader on this issue and I really appreciate her cosponsorship of the bill that you are sponsoring on the Senate side and I am sponsoring on the House side.

I welcome Congressman Thompson to the debate. Congressman Radanovich is one of my best friends in the Congress, and we have had many, many discussions on this issue and he has worked with me in a very cooperative manner and I appreciate that from the bottom of my heart. And I am sure he will say nice things about me today, too, I hope.

Representative RADANOVICH. Yes, sir.

Representative EHRLICH. Mr. Chairman, real briefly, this issue was originally brought to me by a group of State comptrollers with respect to the tax issue, which I know you are very familiar with. The problem concerns the direct shipments that bypass the three-tier system set up in this country since Prohibition.

Under present law, as the chairman eloquently stated, States do not have an adequate remedy. They are simply unable to enforce their State statutes in the Federal court. They are unable to go to Federal court to secure the type of remedy they need. As a result, the States lose a legitimate source of tax revenue.

Second, and of equal importance, is the clip you ran today. It is interesting, Mr. Chairman. Last year, Parkville High School, in Baltimore County—I attended a rally where one of the students at Parkville went online and did the same thing as you just saw in the clip you ran from Utah TV. Yesterday, in Maryland, in fact, we had testimony along similar lines in the Maryland General Assembly. Mr. Chairman, the law is the law and it is pretty clear.

Because of my friendship with Congressman Radanovich and because of the access issue, I have attempted over the last year-and-a-half to work with him and various groups involved in the industry to remedy what I see as a legitimate problem, the problem you alluded to in your statement, the problem of market access. I will continue to do that.

We have made great strides with respect to an 800 number and we are going to hear more about, an Internet solution. The WSWA, the wholesalers, and all groups involved in the stream of commerce have been quite cooperative with George and myself over the past year-and-a-half in trying to come to a resolution of that collateral and legitimate issue that certainly impacts the political viability of our bills. So I will let Mr. Radanovich talk more about that issue.

I thank you for the time today. This is an important issue. This is happening everyday in our towns and cities across this country,

and I appreciate the opportunity this committee is giving me and all of our cosponsors in trying to get the bill passed, the same bill that we submitted in the 105th Congress, and signed into law in the 106th Congress.

I thank you very much.

The CHAIRMAN. Thank you, Congressman Ehrlich.

[The prepared statement of Representative Ehrlich follows:]

PREPARED STATEMENT OF HON. ROBERT L. EHRLICH, JR.

Good morning, Mr. Chairman and members of the Committee. Thank you for the opportunity to speak in support of legislation that will help all states interested in preventing underage access to alcohol and in enforcing their laws regarding the shipment of wine, beer, and liquor within their borders.

Alcohol products have a unique place in American history; they are specifically identified in the U.S. Constitution in the form of the Twenty-First Amendment. Section 2 of the Twenty-First Amendment states specifically: "The transportation or importation into any State, Territory, or possession of the United States for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited." This Amendment and related federal laws regulating the interstate shipment of alcohol beverages result from a bygone era of "bootlegging" and prohibition. A key-statute, the *Webb-Kenyon Act*, was enacted in 1935 (for the second time) and prohibits the interstate shipment of alcohol beverages in violation of applicable state law. The Twenty-First Amendment and the *Webb-Kenyon Act* clearly give states the right to pass laws restricting or prohibiting the importation of alcohol beverages.

Unfortunately, recent interpretations of federal law do not protect states nor provide states an adequate judicial remedy in the enforcement of their laws. Furthermore, the Bureau of Alcohol, Tobacco, and Firearms (BATF), the federal agency charged with protecting against illegal alcohol shipments, has cited statutory ambiguity and to date has failed to aid states in the enforcement of these laws.

State laws vary widely with respect to interstate shipment of alcohol beverages. Approximately twenty states prohibit direct shipment. In some of these states (Florida, Kentucky and Georgia), it is a felony for anyone other than a licensed distributor to import alcohol beverages. In approximately twenty other states, direct shipments of alcohol are limited, under controlled conditions. The remaining states allow direct shipments of limited quantities of alcohol provided the states involved have reciprocal laws in effect.

Regardless of any particular law regulating shipment of alcohol into a state, and adequate enforcement mechanism must be made available to all states. This mechanism would allow states to address two common elements of state law: the assessment of taxes on the manufacture, shipment, and sale of alcohol; and the public interest in prohibiting underage drinking.

Unfortunately, what began as occasional sales of light alcohol beverages over the Internet has become a billion-dollar-a-year market in illegal liquor, wine, and beer sales that affects many states. Illegal interstate shipping of alcohol not only violates a state's ability to regulate incoming alcohol beverages, it also deprives states of excise and sales tax revenue. It is estimated that revenue lost due to illegal shipments is between \$200 and \$600 million a year.

Further, unlike the checks and balances in the current excise tax collection system, made possible by requiring all liquor to be shipped through licensed parties, any effort to tax a shipment that takes place outside the licensed three-tier system—distributor, wholesaler, and retailer—results in a "trust me" situation. The shipper simply tells the state what taxes he owes, leaving the state with no independent way to verify that amount.

The rapid development and popularity of the Internet and mail-order catalogs have given consumers easier access to a wide variety of beers and wines. At a time when many of us are concerned about the rise in drinking, smoking, and drug use among teenagers, illegal shippers are asking us to treat a shipment of beer or wine like the purchase of an L.L. Bean sweater or a book from "Amazon.com." Further, some will have us believe that state laws are to be disregarded or ignored.

We are here today to simply provide a forum for states who have not been able to enforce their laws prohibiting the direct shipment of alcohol beverages. For example, on October 24, 1997, the U.S. Court of Appeals for the 11th Circuit upheld the Northern District of Florida's decision to dismiss Florida's attempt to enjoin four out-of-state direct shippers, holding that neither the 21st Amendment nor the *Webb-Kenyon Act* supplied a federal right of action for failure to comply with state liquor

laws. *Florida Department of Business Regulation v. Zachy's Wine and Liquor, Inc. et al.*

States, with no other recourse, are doing their best to combat these illegal sales. In the last two years, seven state legislatures have passed laws making illegal direct shipments punishable as a felony. Five more states expect to toughen their laws this year. Efforts to stop illegal shipping, however, will remain severely hampered until state attorneys general receive the necessary support from Congress.

The practice of illegal direct shipping has generated much press across the country, fueled in part by the debate during the 105th Congress over my bill, HR 1063. Industry groups have shown good faith in resolving the issue of market access for small wineries by creating both a telecommunication and Internet solution to product location and sales. Some, however, will continue to avoid state tax and regulatory laws. Accordingly, I plan to introduce this legislation again, and I am encouraged to know that you, Mr. Chairman, share my interest in this issue and intend to introduce similar legislation.

With your permission, Mr. Chairman, I would like to show you a short news segment from KUTV, a television station located in your state of Utah.

Additionally, I would like to enter into the record a series of newscasts which capture 29 deliveries to minors in 21 states, including California and Utah. Most states have laws against such shipments, but these efforts carry little weight unless states gain access to the federal courts. I will leave the tape with the committee.

In conclusion, I want to emphasize that this issue is not about restricting or regulating the Internet, nor is it about interfering with legitimate, legal shipments of alcohol. It is about enforcing current law, protecting state's rights, and restoring peace of mind to parents of today's high-tech teens. In my view, adult consumers in Maryland and elsewhere should be able to take advantage of the convenience of ordering of wine, liquor, and beer over the Internet. The delivery of any alcohol beverages, however, must be made in compliance with state law. If not, the states must be given an enforcement mechanism to protect themselves against such illegal interstate shipments.

The CHAIRMAN. Representative Millender-McDonald.

STATEMENT OF HON. JUANITA MILLENDER-McDONALD, A U.S. REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA

Representative MILLENDER-McDONALD. Good morning, Chairman Hatch, and to all of the other members of this committee, especially our very own Senator Dianne Feinstein. I would like to thank you, Mr. Chairman, for holding this hearing and commend you for bringing this very important subject before this committee.

The issue of Internet alcohol sales to minors is an important issue worthy of discussion on its face. One would say such a direct delivery would never happen, as we are restricted from selling alcoholic beverages to minors. But direct shipment of alcohol is impacting our most vulnerable constituents, our children, who are surfing the Internet and getting direct access to alcohol.

Currently, an estimated 10 million of our Nation's children have access to the Internet, a 444-percent increase from 1995. As the new millennium approaches, with more computers in the classroom and more children using the Internet at progressively younger ages, teenagers and adolescents will have significantly more access to beer and wine sold over the Internet made more available to them.

The 21st amendment to the Constitution grants States jurisdiction over the shipment and delivery of alcoholic beverages, and the direct shipment of alcohol ordered through the Internet is illegal in more than 30 States. Alcoholic beverages are held to a regulatory system that distinguishes them from other products, such as food or clothing. Yet, everyday alcoholic beverages are delivered to consumers who have ordered them through the Internet, telephone, or

a catalog from direct shippers who operate outside of regular shipping companies.

These packages are shipped not only in violation of the laws in more than 30 States, but also through a system that circumvents the Nation's tax structure. Because there is no way to determine the age or identity of the consumer ordering over the Internet, anyone, regardless of age, with access to a major credit card can order these products and have them delivered to his or her home, as we saw in your clip. This opens the door to what I call cyber booze for minors, the direct shipment of alcoholic beverages to adolescents who often do not understand the dangers involved in consuming excessive alcoholic beverages.

According to the Centers for Disease Control, 80.4 percent of the Nation's high school students have had at least one drink in their lifetime. 51.6 percent have had at least one drink in a 30-day period, and 32.6 percent qualify as a binge drinker, having had 5 or more drinks on at least one occasion during a 30-day period.

A recent survey of 4,390 high school seniors and dropouts found that within the preceding year approximately 80 percent reported either getting drunk, binge drinking, or drinking and driving. More than half say drinking has caused them to feel sick, miss school or work, get arrested, or have a car accident. In addition, an estimated 88 percent of college students, including those between the ages of 17 and 20, have used alcohol or engaged in binge drinking.

Despite the 21 minimum drinking age and laws prohibiting underage drinkers from driving to another State to pursue alcohol, this is not enough to curb the disturbing trend I have just mentioned. The direct shipment of alcohol through the Internet, telephone, or catalog creates a new means of underage drinkers to avoid all law enforcement barriers. America's children and teenagers need our help in preventing the harmful and often destructive use of alcohol when they are at such young ages.

Stopping the purchase over the Internet and delivery of alcoholic beverages to their homes is a powerful step in this effort to prevent teenagers from driving under the influence, missing school and work, experiencing health problems, getting arrested, or becoming another DUI fatality.

Mr. Chairman, I thank you so much for bringing this very important issue to this committee and for my having the opportunity to testify in its regard.

The CHAIRMAN. Thank you so much.

[The prepared statement of Hon. Millender-McDonald follows:]

PREPARED STATEMENT OF HON. JUANITA MILLENDER-MCDONALD

Good morning Chairman Hatch, Senator Biden, Senator Feinstein, and Members of the Judiciary Committee. I would like to thank you Mr. Chairman for holding this hearing and commend you for bringing this very important subject before the Committee. This issue of Internet alcohol sales to minors is an important issue worthy of discussion on its face. One would say such a direct delivery would never happen as we are restricted to selling alcoholic beverages to minors. But direct shipment of alcohol is impacting our most vulnerable constituents—our children, who are surfing the Internet and getting direct access to alcohol.

This hearing comes at a time when American families need it most. Currently, an estimated 10 million of our nation's children have access to the Internet—a 444 percent increase from 1995. As the new millennium approaches with more computers in the classrooms and more children using the Internet at progressively younger

ages, teenagers and adolescents will have significantly more access to beer and wine sold over the Internet than ever before.

The 21st Amendment to the Constitution grants States jurisdiction over the shipment and delivery of alcoholic beverages and the direct shipment of alcohol ordered through the Internet is illegal in more than 30 states. Since Prohibition, Congress has recognized the unique nature of alcoholic beverages and the ramifications for the abuse of this product. Thus, alcoholic beverages are held to a regulatory system that distinguishes them from other products, such as food or clothing directly to consumers. Yet, every day packages filled with beer, wine, liquor or other vinous or malted products are delivered to consumers who have ordered them through the Internet, telephone or mail order catalog from direct shippers, who operate outside of regular shipping companies. These packages are shipped not only in violation of the laws of more than 30 states, but also through a system that circumvents the nation's tax structure. Because there is no way to determine the age or identity of the consumer ordering over the Internet, anyone, regardless of age, with access to a major credit card can order these products and have them delivered to his or her home. This opens the door to what I call "cyberbooze for minors", the direct shipment of alcoholic beverages to adolescents, who often do not understand the dangers involved in consuming excessive alcoholic beverages.

According to the Center for Disease Control, 80.4 percent of the nation's high school students have had at least one drink in their lifetime; 51.6 percent have had at least one drink in a 30-day period; and 32.6 percent qualify as a binge drinker, having had five or more drinks on at least one occasion during a 30-day period.

A recent survey focusing on the alcohol-related problems experienced by 4,390 high school seniors and dropouts found that within the preceding year, approximately 80 percent reported either getting "drunk," binge drinking, or drinking and driving. More than half said that drinking had caused them to feel sick, miss school or work, get arrested, or have a car accident.

This problem does not end when students matriculate from high school to college. In fact, the access to alcohol by underage drinkers increases once they arrive on college campuses, where the Internet serves a stronger role in their education. An estimated 88 percent of college students, including those freshmen and sophomores between the ages of 17 and 20, have used alcohol or engaged in binge drinking. In 1994, 67.5 percent of college students had used alcohol within the past 30 days. By comparison, 61.7 percent of young people *not* in college reported monthly alcohol use in 1994.

Despite the fact that every state has set 21 as the minimum drinking age to prohibit teenagers from purchasing alcoholic beverages, this is not enough to curb the disturbing trend I have just mentioned. With additional laws prohibiting underage drinkers from driving to another state to purchase alcohol, the direct shipment of alcohol through the Internet, telephone or catalog creates a new means for underage drinkers to avoid all law enforcement barriers and have it delivered right to their home.

You may recall the story that aired on Friday, December 12, 1997, by an NBC affiliate in which an underage youth in New York ordered alcohol from a direct shipper in my state of California via the Internet and accepted delivery from a commercial freight carrier. Since then several television stations including KEYT, an ABC affiliate in Santa Barbara, California and WSPA, a CBS affiliate in Spartanburg, South Carolina, have aired stories on the problems associated with the direct shipment of alcoholic beverages. Recently, WUSA, another CBS affiliate in our nation's capitol aired a story shedding light on this growing problem.

Alcohol is the number one drug of choice by minors and alcohol-related accidents are the biggest killers of our nation's teenagers. If we fail to implement a stricter system for limiting the accessibility of alcohol to our nation's youth, we will ultimately reverse all of the progress we have made over the past decade in highway safety and alcohol awareness. Further, we will allow yet another venue for the illegal distribution of alcoholic beverages to minors accelerate the binge drinking, driving under the influence, missing school and work, causing both long and short-term health problems, getting arrested or becoming another DUI fatality.

Currently, law enforcement officers bust vendors who sell alcohol to minors, as well as those underage persons who are caught purchasing alcohol. However, we currently have no means by which to police the Internet or regulate the direct shipment of alcohol. Direct shippers operate outside of the licensed distribution system. The licensed beverage distribution system is an essential part of the alcohol control process and contributes billions in federal and state taxes each year. Direct shipments circumvent these laws and rob states of tax revenues. Florida, Tennessee, Kentucky, Georgia and North Carolina have recently upgraded their laws to make "direct shipment" a felony. At least 26 other states have sent "cease and desist" let-

ters to wineries and retailers urging them to stop illegal direct shipments of alcohol. With direct shipments there is no regulatory system to guard against underage access or to collect alcohol beverage taxes.

Over the past decade, the proliferation of micro-breweries and small wineries, and the aggressive marketing techniques used by them via the Internet, have resulted in a dramatic increase in the number of direct shipments of alcoholic beverages to homes across this country. What started many years ago as a cottage industry to sell rare wines and micro brewed beer to connoisseurs has burgeoned into a billion dollar business.

Mr. Chairman, what was once considered a "boutique" issue is finding its way into the mainstream, which is raising the eyebrows and concerns of many American families. In fact, a recent poll conducted by *Americans for Responsible Alcohol Access* found that 69 percent of Americans oppose the direct shipment of alcohol to minors; 85 percent agree that the sale of alcoholic beverages over the Internet would give minors easier access to alcohol and could result in more abuse; and 70 percent of Americans don't trust delivery to ensure that the recipient of alcoholic beverages via common carrier is at least 21 years of age.

These facts demonstrate the need to enact legislation that prohibits the direct shipment of alcoholic beverages and related products to our nation's children. I am sure that my colleague from Maryland, Congressman Ehrlich, will agree with me as I urge you to join us in the fight to eliminate this problem. The enactment of legislation in this area will provide states the ability to better enforce the laws that prohibit the sale of alcoholic beverages to minors as well as properly collect sales and excise taxes. More important, it will help us keep our children safe from the scourge of underage drinking.

As a mother, grandmother, and former teacher, protecting our nation's children and working to produce a generation of educated, capable, responsible adults is one of my top priorities in Congress. America's children and teenagers need our help in preventing the harmful and often destructive use of alcohol when they are at such young ages. Stopping the purchase over the Internet and delivery of alcoholic beverages to their homes is a powerful step in this effort.

Mr. Chairman, thank you for the opportunity to testify before this distinguished Committee and address this critical issue. As you know, I have introduced legislation in the past to close the door to cyberbooze and will re-introduce legislation in the 106th Congress. I look forward to working with you and my colleagues in the House in a bipartisan effort to regulate the sale and direct shipment of alcohol to minors.

Thank you.

The CHAIRMAN. Representative Radanovich.

STATEMENT OF HON. GEORGE RADANOVICH, A U.S. REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA

Representative RADANOVICH. Thank you, Mr. Hatch, and thank you for the introduction and the opportunity to be here. I am somewhat encouraged by the fact that another member of your committee has the name "DeWine," so I feel that there is some good representation up on the committee. [Laughter.]

But I also want to ask that my full fellow Congressman, Doc Hastings, comments that he sent over with me would also be submitted into the record.

The CHAIRMAN. Without objection, we will put them in the record.

[The letter of Mr. Hastings follows:]

CONGRESS OF THE UNITED STATES,
HOUSE OF REPRESENTATIVES,
March 8, 1999.

The Hon. ORRIN G. HATCH,
Committee on the Judiciary,
Dirksen Office Building, Washington, DC.

DEAR MR. CHAIRMAN: I represent Washington State's 4th Congressional District, which includes the tremendously productive agricultural area of the Cascade Moun-

tains. Within my district are the Yakima Valley and much of the Columbia Valley Viticultural Areas, recognized by the federal government as distinct, high quality wine grape growing regions.

There are more than 15,000 acres of vineyards in my district, with more being planted each season. There are over 50 wineries in the district, including the state's largest and oldest wineries as well as some of the youngest and smallest.

In addition to producing some of the finest vintages in the world, these wineries also serve as a tourism magnet for eastern Washington. Because of the unique experiences visitors enjoy at our wineries, they generate many repeat requests for wines once they return to their home states. While Washington has "reciprocal" legislation that allows our wines to be shipped to consumers in twelve other states, it is impossible for consumers who live in non-reciprocal states to obtain Washington state wines not distributed through conventional outlets in their local markets. The conventional distribution outlets typically favor high volume producers. Most wineries in my district are relatively small—producing less than 10,000 cases per year—and therefore do not have distribution in many states. Washington State wineries need an opportunity to respond to their customers who are ready, willing, but unfortunately unable to buy these quality wines other than traveling great distances to the wineries themselves.

The bill being considered by the Senate Judiciary Committee, to enforce the Webb-Kenyon Act more aggressively, will do serious damage to the state by state effort to open avenues for consumers to purchase hard-to-find wines such as those produced in my district. I urge the Committee to reject this legislation.

Sincerely,

DOC HASTINGS,
Member of Congress.

Representative RADANOVICH. Thank you, sir, and I do appreciate being here with my Senator from California and also the members of this committee, and especially my good friend, Bob Ehrlich.

Mr. Chairman, in 1982 I established a small vineyard and winery in the Sierra foothills community of Mariposa, my hometown. The Radanovich Winery produces about 4,000 cases annually, and we are located at the boundary of Yosemite National Park, which receives about 3.4 million visitors throughout the world every year. We have the opportunity to present our wines to these tourists, who in many cases don't want to carry wine home with them and ask that we send it to them, or wish to purchase wines. They come from every State in the Union, and frankly all over the world. So this issue is near and dear to my heart.

Like most wineries, mine is small. Of the 1,600 wineries in this country, only 50 are available in a typical retail marketplace. Sales of regional or limited availability wine, of which there are perhaps over 10,000 labels, have grown dramatically in recent years. Unfortunately, traditional distribution avenues are insufficient for the shipment and delivery of wines from these numerous small producers. Direct mail, the Internet, and other alternative forms of distribution have helped these small wineries stay afloat, while at the same time helping to satisfy the growing consumer demand for small or lesser wines.

And let me say right off the bat, too, I want to reiterate that as a member of the wine industry the last thing that we want is minors purchasing alcohol. That is not the intent or the purpose of being in business and making and growing and producing and selling wines.

And, second, the other issue is that in many cases the argument is brought forward in this that the wine industry is avoiding paying taxes within the States that they are selling wines. And that is not the issue here. The wine industry is perfectly willing to pay a tax in any sales, anywhere across the country. However, small

wineries are at a disadvantage in what my friend, Bob, had mentioned in the three-tier system that was created after Prohibition. It is an antiquated system that shuts out small wineries from being able to sell their fine wines and good products all across the country.

And I think that the real issue is the fear that the national wholesalers have in increased demand—or it is about national wholesalers concerned about increased competition brought on by new Internet technology and the desire for market access for small wineries. This is the concern that I think the wineries have in this country, is that we have access under the Commerce Clause, due access, as would anybody else. And I would hope that during the discussions on these bills that access by small wineries in States would not be shut out.

Again, I reiterate that the advent of Internet technology could bring problems in the future, but California has been operating under mail order, direct mail, for many, many years, and it has not been a problem ordering wine through distribution channels such as UPS or anybody else.

I would like to draw attention to the progress the States have been experiencing in reciprocal agreements in Louisiana and New Hampshire, where they are allowed under their State laws the ability to ship wine into those States, pay the taxes, and guarantee that those wines do not go to minors by the willingness of transportation companies to obtain adult signatures and even adult proof of I.D. when it is delivered at the door.

These are issues that should be decided by the State. I think each State ought to be given the opportunity to regulate commerce without limiting access by small wineries. They are proving to do it and they need the encouragement from the Federal Government to make sure that those agreements are, in fact, implemented within their own States.

So I look forward to working with this issue, and hope that we might, out of all of this thing, solve the access for small wineries because it is critical to—as Mrs. Feinstein pointed out, 90 percent of the wine production in the United States is in our State of California and it is very important to small business there.

Thank you very much.

[The prepared statement of Representative Radanovich follows:]

PREPARED STATEMENT OF HON. GEORGE RADANOVICH

I am a California farmer. In 1982, I established a small vineyard and winery in the Sierra foothill community of Mariposa, my hometown. The Radanovich Winery, which produces Sauvignon blanc, Chardonnay, Merlot, Zinfandel and Cabernet Sauvignon, has grown to over 4,000 cases annually.

Like most wineries, mine is small. Of the 1,600 wineries in this country, only 50 are available in a typical retail marketplace. More specifically, about 20 wineries produce 90 percent of all the wine produced. Despite this, sales of regional or limited availability wine—of which there are perhaps over ten thousand labels—have grown. Unfortunately, traditional distribution avenues are insufficient for the shipment and delivery of wines from these numerous small producers. Direct mail, the Internet and other alternative forms of distribution have helped these small wineries stay afloat, while at the same time helping to satisfy the growing consumer demand for smaller, lesser known wines produced in this country.

Grape growing is a very important agricultural crop, the largest crop in California and the sixth largest crop in the nation. Over 60 percent of the grape crop is used in the production of wine. The resulting wine industry in total annually contributes

over \$45 billion to the American economy; provides 556,000 jobs, accounting for \$12.8 billion in wages; and pays \$3.3 billion in state and local tax revenues. In addition, wine is our third largest horticultural export. Wine is commercially produced in 47 states.

Consumers in every state should be able to obtain access to a wide variety of wines, especially the wines of small producers who lack the distribution channels of the major wine producers in this nation. To meet these consumer needs, I point to the 12 states which have chosen to enact variations of a "reciprocal shipment" law, waiving local taxes and allowing consumers to directly order a limited number of cases of wine. I also direct your attention to recently passed "shipper permit" legislation in New Hampshire and Louisiana and to the special order system developed and implemented by the Pennsylvania state liquor monopoly. I am concerned that passage of the proposed legislation would have a chilling effect on efforts underway to craft creative state-by-state solutions such as these.

Legislation to allow states to bring to Federal court an action to enjoin shipment or transportation of liquor in violation of the laws of a particular state would have the unintended consequence of crippling small wineries in this country. The proposed legislation does much more than simply providing a remedy for a violation of the Webb-Kenyon statute which governs interstate shipments. I fear that it will authorize a state to erect discriminatory barriers to interstate commerce which will be used to favored in-state commercial interests to the detriment of out-of-state wine producers. The Commerce Clause protects against state imposed barriers to free trade. That protection should apply to wineries as well as all other businesses.

Further, existing remedies are available for violations of liquor laws. In the case of wine (as with harder liquors) there is an underlying federal permit which is required to operate a winery. That permit is subject to oversight by the Bureau of Alcohol, Tobacco and Firearms, and requires conformance to applicable laws. There have been successful compliance actions through this mechanism. An additional mechanism is not necessary.

Professor Jesse H. Choper, a distinguished scholar in the field of constitutional law from University of California has written the Committee to express his concerns about the possible consequences of Federal legislation in this arena and I ask that this letter be included in the record of this hearing. Professor Choper concludes that the proposed legislation would violate the Commerce Clause protection against barriers to free trade among the states, by allowing states, rather than the Congress, to establish those barriers.

I am also concerned that the thrust of this legislation is to allow states to use the Federal courts to obtain direct jurisdiction over small businesses located in other states in a manner which invites abuse of the court system and a trampling of the rights of out-of-state citizens in order to satisfy the demands of politically powerful local interests. Allowing the federal courts to be used as enforcement machinery for state actions seems to me a huge expansion of federalism and a very dangerous precedent.

Proponents of this legislation claim it is necessary to curb the delivery of alcohol product to underage purchasers. I believe that there are few more important causes than to stem the tide of underage drinking in this country. A Health and Human Services survey reflects that more than half of 18-20 year olds were drinking alcohol in the past month and an astonishing quarter of that age group have engaged in binge drinking during the same period. However, I am convinced that direct shipment of wine, beer or spirits does not significantly contribute to the problem. The two states with the highest consumption of wines—California and New York—have long permitted intrastate shipments ordered by phone or mail. Surely, if such mechanisms were inherently open to abuse the authorities in those states would have discovered that by now. But they have not. Manuel Espinoza, Chief Deputy Director of the California Alcoholic Beverage Control agency has written to Congressman Thompson and myself that as a result of remote sales of alcohol in California, a practice which has been legal for almost fifty years, the state has experienced no enforcement problems or impediments in its ability to enforce laws related to sales to minors. California has only received one complaint about the delivery of alcohol to underage recipients via interstate mail orders. That complaint originated from a privately organized "sting" and investigation ascertained that the actual delivery, though left at the door, was accepted by the minor's mother. I have included Mr. Espinoza's letter as an attachment to my remarks.

Another concern raised by proponents is the avoidance of state excise taxes by interstate shippers. There is no indication that taxes avoided by shippers constitute a significant loss of revenue to any state. It is estimated that interstate direct shipments consist primarily of ultra premium wine and never constitute more than one-half of one percent of a state's total wine volume. For the entire country, a tax loss

of that magnitude would be \$2 million annually. For the State of Maryland, even if it was to allow direct shipment of wine, annual tax losses at full volume would be less than \$20,000 per year. For New York only \$50,000. Other states: Missouri \$13,000, Arizona \$40,000, Iowa \$20,000, Ohio \$30,000 and Michigan \$40,000.

To address even this minuscule problem, forty-three members of California's Congressional delegation have written to the Advisory Commission on Electronic Commerce requesting that the Commission address this problem when it examines means to ensure the fair imposition of consumption, sales and use taxes arising from remote sales of all products, a far more significant revenue problem estimated to involve many billions of dollars in lost revenue. Legislation which preempts the Advisory Commission on Electronic Commerce regarding wine will have the affect of setting a precedent in regulation of the Internet before the Commission has done its' work. We are moving into an arena that all of us have not had the opportunity to think through, and our narrow attempts with wine may end up with far-reaching impacts on the sale of anything through the Internet.

Mr. Chairman, I am not convinced there is an urgent national problem which needs to be solved by allowing virtually unprecedented use of federal courts to solve state problems which can be addressed by state legislative and judicial means. States can make it a crime for an person under 21 to attempt to purchase alcohol. What fool in such a state would dare to leave an evidentiary trail of credit card and delivery records?

Rather than the proposed legislation, alternatives include legislation which would encourage the development of open markets so that consumers can have access to the products which they wish to purchase.

I close by quoting for you a letter by Florida Attorney General Robert Butterworth urging the veto of a bill making direct interstate shipment of wine to a Florida consumer a felony: "[The bill] is the perfect tool for the vested interests who seek additional control over the marketplace, at the expense of competition and consumer choice."

The federal government should not empower states to engage in anticompetitive actions favoring their in-state businesses. The federal government should not use the power of the courts to suppress competition. The federal government should not expand its reach into the private purchases of consumers, or the activities of the small businesses which make up the largest part of the wine business.

Thank you for the opportunity to address this distinguished Committee.

STATE OF CALIFORNIA,
DEPARTMENT OF ALCOHOLIC BEVERAGES CONTROL,
Sacramento, CA, March 3, 1999.

The Hon. MIKE THOMPSON,
The Hon. GEORGE RADANOVICH,
*U.S. House of Representatives,
Cannon Building, Washington, DC.*

DEAR REPRESENTATIVES: This is in reply to your letter of March 1, 1999, requesting information about the Department's experience with direct shipments of wine or other alcoholic beverages to California consumers via the Internet, telephone or mail. We have responded to your questions in the same order as they are presented in your letter.

Question 1. Have direct shipments of wine or other alcohol beverages to California consumers resulted in an enforcement problem for your department?

Answer. No. California has permitted direct wine shipments to consumers since 1963. From 1963 to 1995 California law permitted an adult resident to receive a case of wine per month from a source outside of California but within the United States. The statute established a no cost permit process administered by the Department. In addition to requiring the name and address of the sender as well as the California recipient, the permit process required that the shipment be transported into California via common carrier (no guarantee a paper trail) and an affirmation under penalty of perjury that the person requesting permission to receive delivery was an adult. The statute in question, Section 23661.2 of the California Business and Professions Code, was repealed in 1995 and replaced with the current wine reciprocity statute.

During those thirty-five years the Department authorized thousands of those permits. At no time was a complaint received indicating the wine was used for illegal purposes, i.e., re-sale by a retailer or purchase and consumption by an underage person.

The Legislature has not extended the shipping privilege to beer or distilled spirits. Consequently, our experience relates only to wine products.

Question 2. Do remote sales of wine or other alcohol beverages in California jeopardize the department's ability to enforce laws relating to sales to minors?

Answer. While we have no data indicating just how widespread mail order alcohol sales are in California, we have none the less experienced no enforcement problems or impediments to our ability to enforce laws relating to sales to minors as a result of this practice.

Question 3. What experience if any has the department had with intrastate and interstate remote sales of wine or other alcohol beverages to minors via the Internet telephone or mail?

Answer. While the subject of interstate sales of alcoholic beverages has been the subject of considerable debate throughout the country including California, we have to date witnessed no measurable adverse effects on public welfare or safety that could be attributable to interstate mail order alcohol sales.

Intrastate sales of alcoholic beverages from California retailers to California consumers has been authorized by statute for almost fifty years.

The number of complaints received by the Department involving purchases by underage persons via this method have been minimal when compared to all other complaints involving minors and alcohol. Of the more than ten thousand complaint investigations conducted by the Department each year, we estimate that less than one half of one percent have involved illegal sales to minors via home delivery.

Question 4. Have there been any complaints about the delivery of wine or other alcohol beverages to minors which have been investigated by your department? How many complaints? What was the outcome of the investigation(s)?

Answer. To date we have received one complaint about the delivery of alcohol to minors via interstate mail order. The complaint was from a package store owner in Kentucky whose underage son placed an order for beer with a California retailer and received delivery in Kentucky. The son placed the order using the father's credit card with the father's permission.

After conducting an investigation, it was ascertained that the son's mother accepted delivery of the package that had been left at the door by the parcel service who transported the shipment.

The Department took no disciplinary action against the California retail licensee.

We trust this has been responsive to your request. If you have any questions, please feel free to call on us.

Sincerely,

MANUEL R. ESPINOZA,
Chief Deputy Director.

March 4, 1999.

The Hon. ORRIN G. HATCH, Chairman,
Senate Judiciary Committee, U.S. Senate, Washington, DC.

DEAR SENATOR HATCH: I write about Senator Hatch's Bill, currently before the Judiciary Committee, that has been said to "add enforcement" to the Webb-Kenyon Act passed by Congress in 1913. I am a Professor specializing in Constitutional Law (and the former Dean) at the School of Law of the University of California at Berkeley (Boalt Hall) I attach a copy of my curriculum vitae.

I believe it is most important to underline that the Bill goes far beyond simply providing a remedy for a violation of Webb-Kenyon. Instead, it makes fundamental changes in current law and in doing so affects serious constitutional and public policy issues. Webb-Kenyon prohibits the importation of alcoholic beverages into a state in violation of that state's laws. It is generally understood that Congress' intent in passing the statute in 1913 was to give federal sanction to a state's decision to "go dry," an authority that had been denied to the states by the Supreme Court in *Leisy v. Hardin*, 135 U.S. 100 (1890).

Webb-Kenyon does *not* authorize a state to erect discriminatory barriers to interstate commerce. Indeed, in the absence of an express federal enactment, any attempt by a state to do so—by conferring different rights on in-state and out-of-state producers of alcoholic beverages—would violate the core principle underlying the Commerce Clause of the U.S. Constitution that forbids state discrimination against interstate commerce. Only Congress can so regulate trade between the states.

Nor does the 21st Amendment, which confers special powers on the states regarding alcoholic beverages, affect that conclusion. In *Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263 (1984), the Supreme court held that the 21st Amendment did *not* permit

state regulations of the local sale or use of liquor to discriminate against interstate commerce. To do so, the Court reasoned, would be inconsistent with a central tenet of the Commerce Clause: forbidding economic protectionism.

I believe that the Bill, rather than simply creating a federal remedy for a violation of Webb-Kenyon in its current form, would dramatically expand the powers of the states to regulate alcoholic beverages. Most significantly, it would run counter to the spirit of *Bacchus* and remove the protection that the Commerce Clause grants the alcoholic beverage industry, along with all others, from state erection of barriers to free trade.

I would be happy to provide any further information you may find helpful.
Sincerely,

JESSE CHOPER.

The CHAIRMAN. I don't want to get on the wrong side of Senator Feinstein is all I can say.

Senator FEINSTEIN. That is a good spirit, Mr. Chairman.

The CHAIRMAN. A good spirit.
Congressman Thompson.

STATEMENT OF HON. MIKE THOMPSON, A U.S. REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA

Representative THOMPSON. Thank you, Mr. Chairman and Senators. It is a pleasure to be before you this morning and I appreciate the opportunity to be here. I represent the north coast and the northern portion of California. In my district, we have about 350 wineries. I think it is the largest concentration anywhere, in any region of the United States. And I represent the premier wine-growing region—or one of the premier wine-growing regions of the United States—

Representative RADANOVICH. Watch it. [Laughter.]

Representative THOMPSON [continuing]. Which would be Napa, Sonoma, Lake and Mendocino counties. And I just want to emphasize the importance of the industry. This industry brings about tremendous economic benefit not only to my district, but to the entire United States. The industry is directly responsible for over 200,000 jobs, and they pay about \$3.2 billion in wages and \$1.6 billion in State and local taxes. And they contribute \$12.4 billion to the gross domestic product. If you take into account normal multipliers, this increases markedly.

Notwithstanding those impressive numbers, it is important to note, as has already been said today, that the majority of the wineries are small wineries, small, family-owned mom-and-pop-type wineries. And there are less than 100 wineries of the 1,800 across the Nation that produce 95 percent of the wine. So as was pointed out, most of the wine in our country is produced by the larger wineries. The small wineries produce a very small part. Yet, they contribute a tremendous amount to our economy and to our society.

But through some of the problems in this three-tiered system that has been referenced today, specifically the consolidation of distributors, these small wineries are at a very distinct disadvantage in being able to get the product that they produce to consumers across these United States that want to buy this product.

I have one vintner in my district who told me this week that he loses, they figure, \$32,000 per month on tourist-generated orders. These are people who come to California, visit the winery, and say this is great wine, will you send a case to my home. And they can't;

they can't do that, nor can the consumer do that. So they lose \$32,000 per month, and for a small business that is a tremendous amount of money.

I also want to point out that winery owners and vintners are responsible citizens. They don't want wine or any other alcoholic beverage to be sold or to be distributed to minors, nor do they want to avoid paying their fair share of taxes. And I want to suggest that there are, in fact, ample safeguards either in place or the opportunity to put ample safeguards in place that would make it impossible to either avoid taxes or to sell to minors or to sell within dry jurisdictions. I think any examples to the contrary are orchestrated.

Even in the video we saw today, we saw a young woman, with adult supervision, accessing her computer and using someone else's credit card. So not only in a situation like this is the minor in violation of State liquor laws, but also in violation of credit card laws as well.

Manuel Espinoza is deputy director of the California Department of Alcoholic Beverage Control, and in a letter that he sent to Mr. Radanovich and myself—and I would like, Mr. Chairman, to ask that this be entered into the record.

The CHAIRMAN. Without objection, we will do that.

[The letter referred to is attached to the prepared statement of Representative Radanovich.]

Representative THOMPSON. He stated that he does not believe that this is, in fact, a problem. Last year, when I was in the State legislature, I held hearings on this very issue and Mr. Espinoza came forward and stated the same thing, and he stated it based on 20 years of experience in California. In California, for the last 20 years we have been able to sell alcoholic beverages direct within our State jurisdiction and there has been no problem.

And I would like to read from his statement to that committee. He said, "I do believe the sale to minor issue is overblown, and I say that because we have got experience here in California with a piece of legislation that was on the books for at least 20 years. It would allow a person to receive a case of wine a month from any part or from any State, regardless of the source. And it was a very simple permit process. There was no charge. The consumer who wanted to purchase or wanted to receive a case of wine a month could merely send in a form. They would name the shipper, they would describe the contents of the shipment, and it would have the name and address of the person that was going to receive the shipment. We would review the form and sign it and send it back, and the form was permission for the shipper to bring it in. Our experience with that—you know, like I said, for the last 20 years there was never a problem."

I believe, Mr. Chairman, that passage of this legislation, absent any Federal allowance for direct marketing or for entry and access into the direct market, would, in fact, set back our efforts that Mr. Radanovich had outlined earlier in regard to working on this issue in a State-by-State manner.

I thank you very much for the time to present.

[The prepared statement of Representative Thompson follows:]

PREPARED STATEMENT OF HON. MIKE THOMPSON

Mr. Chairman, Members of the Committee, thank you for allowing me the opportunity to discuss the important matter of direct interstate shipments of wine and the issue of underage access to alcohol.

I represent the north coast of California from the top of the San Francisco Bay to the Oregon border, a district which includes America's premier winegrowing region: the Napa Valley, Sonoma, Mendocino and Lake Counties. I represent over 350 wineries and can safely say that all of them would like to be able to service their customers, all want to pay their fair share of taxes, and none wants minors to purchase their product.

This is an important industry to our national economy. It directly creates 207,000 jobs, accounting for \$3.2 billion in wages. In 1997, the industry directly added \$12.4 billion to the gross domestic product and paid \$1.6 billion in taxes to state and local economies. The total net contribution is larger when economic multipliers are used to calculate the indirect effects of industry activity. When direct and indirect figures are totaled, the industry provides 556,000 jobs that pay \$12.8 billion in wages, generate \$45.6 billion to the U.S. economy, and pay \$3.3 billion in state and local taxes.

Many of America's wineries are small, mom-and-pop businesses that make between a few hundred to a few thousand cases of wine per year. The economic lifeblood of the typical family winery combines the selling of wine to tourists and limited off-site wine sales. Like most small businesses, the winery hopes to be able to compete on a level playing field and to sell wine to customers who request it.

In many states, however, the only means to sell wine is through a distributor and many wineries depend upon distributors to get their product to the market. Unfortunately, for the majority of wineries, that option is unavailable and direct shipping is the only viable means to fill customer orders.

The reason is that the distributorship industry has experienced considerable consolidation over the past decade. There are fewer wine distributors and fewer people to adequately market the 7,000-10,000 American wines currently for sale. In addition, many distributors have no financial incentive to represent the small, family-owned and operated wineries.

And it's these businesses, the wineries which need to satisfy tourism-generated demand for small production wines, that suffer the most. Since these wineries can't get their product to customers using the normal distribution network, their only alternative is to sell to the consumer by direct mail or the Internet.

Such sales are a considerable source of revenue for these small businesses. States enacting anti-direct shipping laws restricting this market can significantly affect a winery's business. One Sonoma winery estimates it loses \$32,000 a month in revenues because it is not permitted to fill orders requested by out of state tourists and wine consumers.

Opponents of direct shipping raise two patently false arguments that must be dismissed. Some claim that wineries are unwilling to live up to their tax obligations and that wineries want to ship to dry counties and to minors. Please know that nothing could be further from the truth.

Despite the rhetoric from direct shipping opponents, winery owners are responsible citizens and generous members of our communities. American wineries all want to pay their fair share of taxes and no winery in any state wants to send wine into dry counties or supply minors with wine.

Despite a very few orchestrated incidents, there is no evidence to support the claim that minors are purchasing wine over the Internet or through the mail. As a California state Senator, I conducted a 1997 committee hearing specifically on the subject of direct shipping. At that hearing, California Alcoholic Beverage Control Deputy Director Manuel Mendoza testified as follows:

I do believe the sale-to-minor issue is overblown, and I say that because we've got experience here in California with a piece of legislation that was on the books for at least 20 years * * *

* * * * *

*Our experience with that * * * for at least 20 years there was never a problem that was brought to our attention with regard to sales to minors or the importation of a product that was harmful.*

* * * * *

** * * we've got studies that show that 87 percent of our high school seniors have reported that they consume alcohol. About 67 percent of those say that they can buy it. So as to the issue of minors purchasing these products*

and having it shipped in, I don't think that's going to happen in California because the kids, unfortunately, can find ways to buy it here far, far to easy.

In his recent letter to Mr. Radanovich and me, Mr. Espinoza reiterated the fact that the Department of Alcoholic Beverage Control in California has not experienced an enforcement problem or impediments to its ability to enforce laws relating to direct shipping sales to minors. He said that there are "no measurable adverse effects on public welfare or safety that could be attributable to interstate mail order alcohol sales."

Moreover, shipping companies such as DHL Worldwide Express have implemented effective safeguards to prevent the delivery of alcohol to minors and intoxicated persons:

DHL's protocol requires every recipient's ID to be visually checked;

The ID information is logged on a DHL tracking document;

Every package containing wine must be labeled on the outside as containing alcohol, delivery to minors prohibited; identification required.

Over the past 20 years, at least 15 states including California have adopted legislation allowing consumers to purchase a limited amount of wine from their homes. These are balanced statutes which place a cap on the quantity of wine sold to an individual addressee and which prohibit wine sales to minors.

As such, I question the reasons some states are using to enact anti-direct shipping laws—laws which in my view are unreasonable barriers to competition erected to favor local liquor industries and distributors. In fact, the U.S. Supreme Court has said:

State laws that constitute mere economic protectionism are therefore not entitled to the same deference as laws enacted to combat the perceived evils of an unrestricted traffic in liquor.

(*Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263 [1984].)

There is no legal justification for states to be granted access to federal court. The legislative proposal before you would dramatically expand the powers of the states to regulate alcoholic beverages and would run counter to the Supreme Court's decision that the 21st Amendment does not permit states to discriminate against interstate commerce.

Furthermore, the proposal is unnecessary and unduly burdensome since there is already a remedy at law to address this problem. The Bureau of Alcohol, Tobacco and Firearms can currently revoke a winery's basic permit to operate if they violate state law restrictions on sales to minors.

Finally, this proposal will hamper efforts by the interested parties to resolve this issue at the state level.

America's family wineries simply wish to be able to respond to requests from adult customers wanting to purchase premium wine. I strongly urge this Committee to carefully consider the legitimate needs of consumers and the companies that sell to those customers. Any legislation should be balanced to ensure that both consumers and wineries are able to transact a legal business in a reasonable manner and on grounds no more stringent than those that apply to in-state manufacturers and distributors.

Mr. Chairman, again, thank you for the opportunity to present our views. I am pleased to respond to any question you might have.

The CHAIRMAN. Well, I want to thank each of you for coming and for taking time from what I know are busy schedules to come over here and help this committee to at least look at this in the best possible way we can, and we will try to do that, taking into consideration everybody's needs. I just want to thank you for coming. We appreciate it.

Representative MILLENDER-MCDONALD. Thank you, Mr. Chairman.

Representative THOMPSON. Thank you, Mr. Chairman.

The CHAIRMAN. Leading off the second panel today is Utah Assistant General Wayne Klein. Mr. Klein is currently leading the battle in the Utah Office of Attorney General to prosecute companies and individuals who are alleged to be illegally shipping alcohol into that State. Although an important case he is prosecuting was

initially dismissed on procedural and constitutional grounds, he recently persuaded the Utah Court of Appeals to reinstate that case and allow him to bring the charges before a jury. However, as I believe he will testify, further appeals are expected. Prior to his current position, Mr. Klein was the Idaho Securities Bureau Chief and an adjunct professor at Boise State University. We are happy to have you here, Wayne.

Our second witness on panel two is Prof. Stephen Diamond, from the University of Miami School of Law. Professor Diamond specializes in American legal history and teaches courses in that subject, as well as in State and local government law, tort law, property law, and most importantly for our purposes, liquor law.

Now, how a person who has devoted his life to a study of liquor law ever managed to pass the bar is beyond me. [Laughter.]

Professor Diamond is a member of the Committee on Beverage Alcohol of the American Bar Association, and is also a member of the International Wine Lawyers Association. He received his B.A. from Swarthmore College, a certificate in social anthropology from Cambridge University, and an A.M., a Ph.D. in history and a J.D. from Harvard University. Prior to his current position at the University of Miami, Professor Diamond was a professor of law on the faculty at the Cardozo School of Law of Yeshiva University. So we are pleased to have you here, Mr. Diamond.

I am very pleased to have with us today Brendan Brogan. At 18 years of age, Brendan is already quite an accomplished young man. He is the first youth member of Mothers Against Drunk Driving's National Board of Directors. He was selected for that position after serving in 1998 as a New Jersey delegate to MADD's National Youth Summit to Prevent Underage Drinking in Washington. Brendan is also a member of a MADD Youth in Action Team, a community group dedicated to changing a societal environment which condones underage drinking. He is also president of a DEA, Drug Enforcement Administration-sponsored Boy Scout explorer post, a group whose purpose is to organize and enjoy high adventure in a drug-free environment. Brendan became an Eagle Scout at age 13, one of the youngest ever to receive that honor. So we are proud to have you here, Brendan.

The fourth member of the panel is John DeLuca, president of the Wine Institute. The Wine Institute is the public policy advocacy association of California wineries. It brings together the resources of 450 wineries and affiliated businesses to support legislative and regulatory advocacy, international market development, media relations, scientific research, and education programs that benefit the California wine industry. It is great to have you here, Mr. DeLuca.

Finally, filling out the panel is Mike Ballard, the President of Savannah-Chanel Vineyards, located in California's Santa Cruz Mountains. Established by a French immigrant in 1892, Savannah-Chanel Vineyards still makes wines from some of the original plantings.

So we are honored to have all of you here. Each of you brings a special expertise to this committee today and we will look forward to hearing each of your testimonies. Now, we are going to limit you to 5 minutes each. We hope that you will abide by that and then we will have some questions for you.

Mr. Klein.

PANEL CONSISTING OF WAYNE KLEIN, ASSISTANT ATTORNEY GENERAL, STATE OF UTAH, SALT LAKE CITY, UT; STEPHEN DIAMOND, PROFESSOR OF LAW, UNIVERSITY OF MIAMI SCHOOL OF LAW, CORAL GABLES, FL; BRENDAN BROGAN, NATIONAL BOARD MEMBER, MOTHERS AGAINST DRUNK DRIVING, RIDGEWOOD, NJ; JOHN A. DeLUCA, PRESIDENT AND CHIEF EXECUTIVE OFFICER, WINE INSTITUTE, SAN FRANCISCO, CA; AND MICHAEL BALLARD, PRESIDENT, SAVANNAH-CHANEL VINEYARDS, SARATOGA, CA

STATEMENT OF WAYNE KLEIN

Mr. KLEIN. Thank you, Mr. Chairman, members of the committee. As assistant attorney general for the State of Utah, one of my responsibilities is white collar crime, including a case that I am prosecuting against an Illinois-based company, Beer Across America, which was shipping alcohol into Utah in violation of Utah criminal laws.

I appreciate the opportunity to appear in support of legislation that would empower State enforcement officials to use the Federal courts in limited instances to halt illegal shipments of alcohol when the State enforcers otherwise would be unable to prevent the shipments. I confess to being somewhat surprised that events are necessitating new legislation and this hearing. States have always been permitted to exercise their police powers in ways that would protect their citizens.

Beyond the significant police powers granted to States by the 10th amendment, alcohol long has held a special status. The 21st amendment endowed the States with constitutionally-based authority to determine the conditions under which alcohol is sold in a State. The constitutional amendment process that repealed Prohibition guaranteed this control to the States. The Webb-Kenyon Act has long served as a legislative reaffirmation of this special status. My surprise derives from the depth and boldness by which alcohol marketers are contesting this special status.

Beer Across America was warned that its shipments of alcohol to Utah were illegal. It responded by promising to halt any further shipments. Six months later, Utah investigators were seizing over 100 cases per month. These invoices from seized shipments demonstrate not only the defiant continuation of sales, but that in many cases customers were encouraged to list an out-of-State address for billing purposes, in the hopes that regulators would not find out that the alcohol was destined for Utah.

The problem is not just beer. An estimated 5 million cases of wine are shipped to consumers illegally every year. And it is not just adults who are buying the alcohol. You saw the video piece about a 13-year-old Utah girl being able to order beer through the Internet. In our prosecution, we had a minor who purchased and was sent alcohol. A study cited in my written remarks indicates that up to 10 percent of alcohol being acquired by minors comes via delivery services. And of alcohol being sent to consumers, an estimated 59 percent is left out on porches or in car ports rather than being physically delivered to an adult.

I spent much of my earlier career bringing civil and criminal enforcement actions against those committing securities fraud. I have filed suit and obtained literally hundreds of injunctions against fraud promoters located in other States. Just last summer, I obtained two felony convictions against a New York brokerage firm for fraudulently soliciting a Utah resident. In all of those cases, no one ever challenged the State's authority to obtain a civil injunction or a criminal conviction against an out-of-State defendant. No one claimed the State could not prosecute a crook engaged in interstate fraud via the telephone or mail. Everyone recognized it was beyond dispute that a New York firm had to comply with Utah law if it wanted to sell securities to Utah residents.

It is paradoxical that the States with no special constitutional authority over investment transactions seem to have more authority over securities violators than shippers of alcohol. This result is truly unfortunate. There are very good reasons for States to decide to control the sale of alcohol in their States. These reasons range from preventing sales to minors, to quality control, to public safety.

I am happy to report some good news. Last Thursday, the Utah Court of Appeals reversed the trial court's 1997 decision to dismiss our criminal charges against Beer Across America. That criminal trial now can proceed. It is a good first step, but it is still a long way from solving the national problem or from eliminating barriers to civil cases. Many States like Florida have been subject to a legal catch-22. The State courts may think they lack subject matter jurisdiction or personal jurisdiction over the out-of-State defendants. But the Federal courts, which may more easily assert jurisdiction, have denied the States a remedy because the Webb-Kenyon Act provides no Federal cause of action.

We need legislation to solve this legal catch-22. The States need some artificial barriers removed, barriers that are being used to hide illegal activities of hundreds of companies shipping alcohol directly to consumers. I respectfully recommend this committee seriously consider the following three-point plan for giving the States more power to control their borders.

First, Congress should move immediately to pass amendments to the Webb-Kenyon Act that will empower the States to use Federal courts to halt illegal shipments. This authority must be sufficient to grant effective relief to the States in, A, stopping the violations; B, punishing the perpetrators; and, C, deterring future wrongdoing. Venue and service of process limitations must not make the Federal court remedy illusory. Venue needs to be where the violation occurred. If a company ships its products into a State, it should be answerable in the location from whence its revenue was derived.

Second, Congress should use the occasion to reaffirm the principles behind the 10th and 21st amendments that alcohol distributors must comply with the laws of each State in which they want to sell their products.

And, third, the committee should consider legislation in this bill or another requiring that alcohol being shipped across State lines, whether or not in compliance with the laws of the receiving State, be clearly labeled as alcohol, identify the sending company, and require an adult signature before delivery. Packages of alcohol should

not be left on doorsteps. Minors must be foreclosed from taking advantage of any new alcohol sources.

Mr. Chairman, members of the committee, doing business in a State is a privilege. That privilege is fairly conditioned on compliance with the laws of that State. Alcohol more than any other product should demand adherence to this fundamental principle.

Thank you for the opportunity to express my views and I am happy to answer any questions. Thank you.

The CHAIRMAN. Thank you.

[The prepared statement of Mr. Klein follows:]

PREPARED STATEMENT OF WAYNE KLEIN

MR. CHAIRMAN AND MEMBERS OF THE COMMITTEE: My name is R. Wayne Klein. I am an Assistant Attorney General for the State of Utah. I am a prosecutor with responsibility for cases involving white collar crime, including a criminal case against an Illinois company that was selling and then shipping into Utah alcohol in a manner that violated Utah criminal laws. The Attorney General's office works closely with the Utah Department of Alcoholic Beverage Control and the Utah Criminal Investigation Bureau in enforcing Utah's alcohol control laws.

INTRODUCTION AND OVERVIEW

I am pleased to express strong support for amending the Webb-Kenyon Act in a way that empowers state enforcement officials to halt deliberate and blatant violations of state alcohol control laws. States need to be allowed to prevent out-of-state alcohol vendors from continuing to ship liquor in to the states in violation of state laws. An unfortunately high number of alcohol producers and shippers are defying state laws and challenging their authority to control the sale of liquor within their borders.

Heretofore unchallenged notions that the Tenth Amendment and the Twenty-First Amendments vested the states with authority to control the sale and transportation of liquor within the states' borders are now under broad and determined attacks. What is unfortunate is that these violators are masquerading as legitimate businesses.

If alcohol producers wish to be able to ship their products directly to consumers in other states, the producers must change the laws. Permitting the continuation of a massive, coordinated effort by these companies to defy state laws promotes neither the rule of law nor the sanctity of states rights.

THE DIRECT SHIPPING INDUSTRY IS DEFYING STATE AND FEDERAL LAWS

In 1997 the Joint Committee of the States, a committee of state alcohol regulators, conducted a survey of direct shipping of alcohol in the United States. The survey identified 154 companies engaged in mail order and direct shipment of alcohol at that time. Many other companies have entered the market since then.

This activity is in stark contrast with the laws of those states. Every state either prohibits or tightly regulates direct shipments of alcohol to consumers, in varying degrees.¹ Twelve states are *so-called* reciprocal states, permitting shipments of wine only (but not beer or distilled spirits) into their jurisdictions, but only from other reciprocal states. About nineteen jurisdictions (including the District of Columbia) permit some limited importation by *consumers*. In many cases, the consumer must obtain a permit *before* placing the order. It should be noted that the availability of limited importation for a consumer does not necessarily mean the shipper also is exempt from the law's requirements. Some twenty states allow no direct shipments. In at least five of these states direct shipment is expressly made a felony.

These alcohol marketers are not located only in "reciprocal" states. They are not limiting sales only to consumers in other reciprocal states. They are shipping directly to consumers in every state. The direct sales are in blatant violation of state alcohol control laws. Why?

¹The Wine Institute maintains a state by state breakdown of each state's laws on direct shipping of alcohol. See www.wineinstitute.org/shipwine/analysis/state-analysis.htm. See also DeConti, *New Legislation Increases Prohibition on Direct Selling*, "The Bar" (ABA Committee on Beverage Alcohol Practice), Vol III, No. 3 (Jan. 1998).

The reasons for selling and shipping alcohol in violation of state laws are explained only by greed and opportunism. We can rule out ignorance of the law as the reason for their conduct. Sales of alcohol are regulated by the home jurisdiction as well as by the federal Bureau of Alcohol, Tobacco and Firearms (BATF) at least to some degree. The existence of state laws and law enforcement efforts against direct shippers is well known within this industry.² Indeed, when Utah criminally charged Illinois-based Beer Across America with illegally shipping beer to customers in Utah, it was only after investigators had warned the company and its lawyer that the sales were illegal—yet the sales continued.

In any other legitimate industry, businesses first would ensure that laws were changed to permit activity before engaging in massive marketing and sales of their products. Not so here. There may be several explanations. It may be that alcohol marketers are (a) hoping not to get caught (and the large number of sellers certainly assists in the anonymity), (b) hoping to get the laws overturned (laws that have withstood challenges for sixty years), or (c) seeking sympathy from the public and the media, wishing that public pressure will result in changes in the law (after the violative conduct, rather than before).

Regardless of the motivation, it must be emphasized that this industry was born—and is thriving—in manifest disregard of the law.

ARE STATE ALCOHOL CONTROL LAWS STILL VALID?

There are high stakes in this battle. The existence of the alcohol direct selling industry is a frontal challenge to the entire concept of states exercising their police powers. It is a defiance of states' rights and their ability to control alcohol sales within their states.

By what authority do the states enact laws controlling the sale of alcohol within their borders?

The Tenth Amendment to the Constitution provides: "The powers not delegated to the United States by the Constitution nor prohibited to it by the States, are reserved to the States respectively, or to the people."

The Twenty-First Amendment repealed prohibition. The State of Utah cast the deciding vote for the repeal, in large part because state powers were preserved. The operative language of the 21st Amendment reads: "The transportation or importation into any State, Territory, or possession of the United States for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited." Under this Constitutional provision, alcohol is given a special status. States have the constitutionally protected ability to determine the conditions under which alcohol is sold or shipped into their states.

Congress has reaffirmed this special reservation of powers to the states. The Webb-Kenyon Act³ expressly prohibits the "shipment or transportation" of alcohol "in violation of any law of [a] State, Territory, or District * * *." Again, the rights of the individual states to control the sale of alcohol within its borders has been recognized and preserved.

It should not be surprising that lawmakers in most states have made violations of the alcoholic beverage control laws a predicate offense for racketeering laws. Utah has done so.⁴ In fact, Utah's charges against Beer Across America included one count alleging a violation of state racketeering laws.⁵

WHY DOES ALCOHOL HAVE SPECIAL STATUS?

The sale—or even transportation—of alcohol is accorded special status under the constitution, federal law, and state law because of the unique nature of alcohol. Control over the sale of the alcohol, its transportation, and its use reflect public policy determinations that limitations on the sale of alcohol serve the public interest. Examples are many:

- *Sales to minors* Restricting alcohol sales to minors is one of the most fundamental justifications for state regulation of alcohol. It is discussed in the next section.

²In addition to the Wine Institute web page, WFF Distributing in Healdsburg California publishes an annual *Retail Wine Shipping Guide* which clearly and succinctly provides state-by-state information on whether direct shipping is allowed and, if so, under what conditions.

³27 U.S.C. § 122. The Webb-Kenyon Act and its predecessor the Wilson Act date back to 1890. This demonstrates long standing Congressional recognition of state authority in this area.

⁴Utah Code Ann. § 76-10-1602 (4)(www) (1998).

⁵*State v. Amoroso, Beer Across America*, Case No's. 97 1002970 FS and 97 1002971 FS, First Amended Criminal Information, Utah Third District Court (Apr. 21, 1997) reversed Case No. 971712-CA (Utah Ct. App. Mar. 4, 1999).

- *Restrictions on locations, types of sales* States may decide to prohibit the sales of alcohol on certain days of the week or after certain hours at night.⁶ Establishments that sell liquor might be restricted to locations away from schools and churches.⁷ There may be prohibitions against selling to intoxicated or interdicted personnel.⁸ Concerns about restrictions on the availability of certain products are largely unfounded.⁹
- *Control consumption* Requiring alcohol to be sold at state liquor stores may reduce the amount of consumption. This reflects a valid policy choice of the state.¹⁰ If lawmakers choose to limit beer sales to products having a low alcoholic content, it may be endeavoring to reduce some of the ill effects of consumption.¹¹
- *Public safety* Alcohol is the largest single cause of automobile fatalities. Control by the state can ameliorate this travesty. “Because of Utah’s stringent laws, only 20.6 percent of all Utah traffic fatalities in 1997 were related to alcohol, compared to 38.6 nationwide.¹²
- *Product quality* State alcohol regulators have responsibility to ensure the purity of the products being sold for consumption. The State has a great interest in preventing the sale of any adulterated alcohol products.¹³
- 32A–12–219 (1998) (adulteration); Utah Code Ann. § 32A–13–109 (1998) (inspections).
- *Labeling* The labels and packaging for alcohol products must be approved prior to use. This prevents untruthful and misleading statements and reduces the likelihood that labeling and packaging will overtly entice underage consumers.¹⁴
- *Taxation* Alcohol is taxed at a heavy rate. This is intended both as a source of revenue¹⁵ and as a disincentive to high consumption. If sales taxes or alcohol-specific taxes are not paid to the state treasury, all taxpayers suffer and the policies behind such taxes are unmet. In Utah’s criminal case against Beer Across America, the company collected sales taxes from Utah residents and claimed to be paying it to another state. We were unable to verify whether the amounts collected were remitted to another state. If not, the company fraudulently collected—and converted to its own use—increased amounts from its customers. Even if taxes were paid to another state, Utah residents still are obligated to pay Utah use taxes for the purchases. In such cases, citizens paid taxes twice. If the vendor is not licensed to collect sales taxes, how can a state know whether taxes have been collected or remitted. Businesses that are obeying the law and pay the required fees and taxes should be commended.
- *Licensing* The licensing of producers and vendors of alcohol gives the state a means of preventing unqualified or undesirable persons from participating in this business.¹⁶ Persons with criminal records or with ties to illicit organizations can be excluded. Insurance coverage may be required of the licensee.¹⁷ The licensing process also can require that licensees be knowledgeable in the law. The threat of revoking a license is an incentive for the holder to insist on compliance with the law by his firm. Licensing also gives states the ability to impose pro-consumer requirements such as a mandate for all licensees to undergo server training to prevent sales to minors or to the already intoxicated.

⁶Utah Code Ann. § 32A–3–106 (10) (1998). And, in some cases, on election day. *Id.*

⁷Utah Code Ann. § 32A–2–101 (3) (1998).

⁸Utah Code Ann. § 32A–3–106 (9) (1998).

⁹While state policies may restrict the availability of certain products, this problem is largely a myth. The beers shipped to Utah consumers by Beer Across America were all available in state liquor stores and at a price lower than charged by Beer Across America. Most state alcohol regulators make a great effort to provide a wide variety of products at state stores.

¹⁰Utah’s alcoholic beverage laws are explicit on this point. “This title is an exercise of the police powers of the state for the protection of the public health, peace, safety, welfare, and morals and regulates the sale, service, storage, manufacture, distribution, and consumption of alcoholic products.” Utah Code Ann. § 32A–1–103 (1998).

¹¹Utah Code Ann. § 32A–1–105 (4) (1998).

¹²Editorial Opinion, *Don’t Contaminate Liquor Laws*, Deseret News, Feb. 1, 1999.

¹³Utah Code Ann.

¹⁴See Utah Administrative Code, (DABC Rule) R81–1–3 (3), R81–1–17(3)(a) (1998).

¹⁵This revenue is far below the well-known societal costs of dealing with the effects of alcohol consumption as reflected by increased rates of domestic abuse, workplace absenteeism, and health care costs.

¹⁶Utah Code Ann. § 32A–4–103 (1) (1998).

¹⁷Utah Code Ann. § 32A–4–102 (1) (1998).

SALES OF ALCOHOL TO MINORS

One of the strongest—and most universally accepted—justifications for controlling the sale of alcohol is to prevent consumption by minors. The reasons for this paternalism are beyond cavil.

Nationally, 26 percent of 8th graders, 40 percent of 10th graders, and 51 percent of 12th graders report drinking alcohol in the prior month.¹⁸ Although rates are lower in Utah, there are nevertheless 22,000 underage binge drinkers in the state of Utah.¹⁹

Across the country, about 84 percent of all college students drink,²⁰ and about 44 percent are binge drinkers.²¹ College students under 21 binge drink at rates equal to or greater than those of legal drinking age.²² Rates of college drinking are lower in Utah. In 1994, 80 percent of Utah college students reported that they did *not* drink.²³ Binge drinking, although not as prevalent in Utah as elsewhere, is still a major problem. A survey conducted by the Utah Alcohol Policy Commission indicates that 12 percent of first-year (underage) Utah college students binge drink. When statistics from Brigham Young University (a church-sponsored institution) are factored out, the number jumps to 18 percent.²⁴

What is clear is that governmental control policies, such as raising the drinking age and increasing taxation of alcohol, have been shown to reduce alcohol consumption and alcohol-related problems among young adults.²⁵

Firms engaged in direct shipping of alcohol are making it significantly easier for minors to gain access to alcohol—and in some ways that may not be anticipated. Unlike the traditional sales transaction involving alcohol, direct shipping eliminates the face-to-face contact between the buyer and seller. Whether the traditional seller is a state liquor store or a private storefront, a cashier is present to verify the age of the buyer. Not so with direct sales. There is no means of determining the true identity of the buyer. While the telephone order takers or the Internet order forms may ask the buyer whether he or she is over 21, no steps are taken to verify this crucial piece of information. If a minor is willing to violate the law by purchasing and consuming alcohol we are deluded if we think the youth will be dissuaded from doing so by having to lie about his or her age.

Last week, a Salt Lake City television station ran a story about a 13 year old girl who ordered alcohol over the Internet using her brother's credit card. This is outrageous. No one should condone business practices that permit this result. Our pending criminal case involving Beer Across America also included one criminal charge of a sale to a minor who was shipped beer by the company.

One might think that delivery to minors can be prevented by requiring package delivery companies to require an adult signature for the alcohol being delivered. In fact, the Beer Across America home page states: "An adult signature is required at time of delivery. Please make sure that someone will be present to sign for the package during regular business hours."²⁶ In reality, this does not occur. Direct shipping companies rarely disclose on the package that the contents are alcohol—perhaps out of a fear that the package will be seized by law enforcement officials. As a result, the packages do not identify the contents, do not give the full name of the seller (ordinarily using the initials of the company and its address), and do not say that an adult signature is required.

Indeed, the package delivery companies do not want to have to obtain an adult signature for their deliveries. The delivery companies simply do not want to have to make multiple trips to a home hoping to find an adult present. The alarming

¹⁸ *Youth Drinking: Risk Factors and Consequences*, Alcohol Alert, No. 37, July 1997.

¹⁹ Anne Wilson, *Study Links Ads, Teen Drinking*, Salt Lake Tribune, Sep. 11, 1996 at C1.

²⁰ Henry Weschler et al, *Too Many Colleges are Still in Denial About Alcohol Abuse*, The Chronicle of Higher Education, Apr. 14, 1995.

²¹ Henry Weschler et al, *Health and Behavioral Consequences of Binge Drinking in College: A National Survey of Students at 140 Campuses*, JAMA, Dec. 7, 1994.

²² Ralph W. Hingson, *College-Age Drinking Problems*, Public Health Reports, Jan/Feb, 1998, at 52; Donna E. Shalala, *Message from Secretary of Health and Human Services*, Alcohol Alert, July 1995.

²³ Joan O'Brian, *More Students Aren't Drinking to Their Health*, Salt Lake Tribune, May 24, 1994, at D1.

²⁴ Dan Egan, *Study: Binge Drinking Low at Utah Colleges*, Salt Lake Tribune, Nov. 7, 1997 at B1.

²⁵ Barbara L. Braun et al, *Civic Participation by 18- to 20-Year-Olds as a Predictor of Support for Alcohol Control Policies: The Communities Mobilizing for Change Project*, Contemporary Drug Problems, Mar. 1, 1997.

²⁶ See www.beeramerica.com for the home page of this company. The order form with this language is found under the "Join Our Club" button. It also is found at: www.actonet.com/cgi-bin/BAA/display?TEMPLATE=register.template

truth is that most alcohol sent to homes via delivery companies are left on porches, in bushes, and behind fences—often with a note on the door. Our criminal investigation of Beer Across America revealed that of 558 cases of alcohol delivered to Utah residents during a three month period, 330 were left where someone else—including minors—could get access to it. This means that 59 percent of the alcohol sent into my state by direct shippers is left out for anyone to pick up. Presumably the same is true everywhere. No signature is required. No adult must accept control of the package. It is a perfect situation for a minor who knows about the delivery. If he steals the package, no one may ever know he has the alcohol.

The draft of a study in progress has revealed that: "Underage youth use home deliveries as a source of alcohol. Ten percent of 12th graders and 7 percent of 18- to 20-year-olds in 15 midwestern communities reported that they obtained alcohol through delivery services in the last year."²⁷

THE WORLD HAS NOT CHANGED

Advocates for this new industry argue that the world is different now; that we cannot apply prohibition-era laws to Internet-era transactions. This seductive argument is not only wrong, but pernicious.

While alcohol now can be ordered over the Internet, this new phenomenon is not much different than the way business was conducted by toll-free telephone or mail order. While a new method of advertising and ordering has been devised, it does not signal any fundamental change in the nature of alcohol regulation such that the laws should be scrapped. More importantly, it must be emphasized that while orders can be placed over the Internet, the products are not shipped via the Internet. Unlike some products that can be purchased and delivered over the Internet—such as music, software, or pornography—this product still is delivered the old fashioned way. Whether a product has been ordered over the Internet has no effect on the final activity: alcohol is delivered into a state by UPS, FedEx, or other delivery companies in violation of the laws of that state. I see nothing in the creation or popularity of the Internet to undermine the state policies that led to regulation of alcohol.

Last summer I took guilty pleas from a New York securities brokerage firm for two felony counts of securities fraud and sales by an unlicensed securities broker. The unlicensed broker had called into Utah pitching stocks to buy and doing so under a false name. In that case there were no challenges to our authority to require the out-of-state seller to be licensed. No one doubted that the New York broker had to comply with Utah law when selling securities to Utah residents over the telephone. No one said that Utah lacked jurisdiction to prosecute the violators. And, the same licensing requirements apply also to the conduct of business by insurance agents, lawyers, physicians, and the dozens of professions regulated by states.

It is illogical and bad public policy to permit a state to prosecute violators of securities, insurance, or other professional licensing laws, but not violators of the alcohol control laws.

The legal arguments being made by defenders of this industry are troubling. If one accepts that it is within a state's police powers to determine that certain products are contraband, or at least regulated, then the state should have the ability to enforce compliance with those laws. If states cannot enforce their alcohol compliance laws, does this portend challenges to their ability to enforce securities or insurance laws—not to mention laws against child pornography or the illicit drug trade?

A company should not be allowed, with impunity, to sit in one state and ship a contraband product to a buyer in another state. If a state is to have power to declare activities illegal, it is untenable to deny it the ability to enforce those laws. The only change occasioned by the Internet is to increase the availability of alcohol without changing the laws regulating its sale and use.

ILLEGAL CONDUCT IN UTAH

Utah does not attempt to control what its residents do in other states. However, Utah must be able to control its borders when contraband products are destined for delivery into the state.

During October and November 1996, state investigators intercepted 244 cases of beer²⁸ shipped to Utah residents by Beer Across America. We discovered that sales had been ongoing since at least 1992. This problem is not a recent phenomenon. Considering that Utah has less than one percent of the U.S. population, by extrapo-

²⁷ Fletcher, L.A., Willenbring, M.L., Wagenaar, A.C., *Alcohol Home Delivery Service: A Source of Alcohol for Underage Drinkers*, Journal of Studies in Alcohol, in print.

²⁸ Each case had twelve bottles.

lation the number of shipments into Utah during those two months means that over 146,000 bottles of beer are being shipped by this one company every month to citizens all over the country. And this is only one of the hundreds of companies engaged in this business. As noted below, one estimate is that five million cases of wine are sold and shipped illegally each year. This is a massive disregard for the rule of law.

It is instructive to note that all of the shipments into Utah by Beer Across America occurred six months after the company was informed that it was a violation to ship the product into Utah. These sales—and the resulting violations—were deliberate. Even more egregious, in 33 of these cases, or 13.5 percent, the company urged the customers to list an out-of-state address for the sale, then an in-state address for delivery. A more manifest disregard of the law—by someone pretending to be legitimate—is hard to imagine.

THIS PROBLEM AFFECTS ALL PRODUCERS, NOT JUST OUT-OF-STATE SHIPPERS

If direct shipping is permitted in disregard of state laws, in-state producers are harmed. If out-of-state producers do not have to pay taxes, local producers are placed at a competitive disadvantage. If out-of-state shippers do not have to be licensed, inspected, or have quality testing of their products, local producers will be incurring costs higher than the out-of-state shippers. The natural result of elimination of restrictions on out-of-state producers is a push to eliminate restrictions on in-state producers.

Put another way, if regulation of in-state alcoholic producers, distributors, and vendors is to continue, the same restrictions must apply to out-of-state sellers. We cannot harm those who have complied with the law by giving preferential treatment to those who do not operate under the same constraints. If we did, it would drive all producers out of our state—and out of the reach of the police powers of the state. As indicated above, if out-of-state shippers are not forced to comply with the laws of the states in which their products are sold, state authority to regulate alcohol will cease. The effect of the 21st Amendment will cease. The Webb-Kenyon Act will be rendered meaningless.

POLICY CHOICES, NOT LEGAL QUESTIONS

Proponents of direct shipping make several superficially attractive arguments in support of their position. They argue that prohibitions on direct shipping are protecting state-sponsored monopolies. They decry restrictions on freedom of choice and the limited purchase opportunities. They accuse states of protecting large manufacturers or in-state distributors who are guarding their own turf. They even seek sympathy by pointing out that alcohol control laws are turning ordinary citizens into criminals.

It is important to see these for what they are: policy arguments, not legal arguments. Each of these arguments is an expression of an opinion about what public policy should be. Out of frustration at their inability to change public policy in other states they are flouting the law's requirements.

These arguments are being directed at the wrong targets. These policy choices should not be made to prosecutors or to courts. So long as the 21st Amendment is in effect, states will have constitutionally sanctioned authority to assert their police powers in a manner determined by the state legislature. Proponents of direct shipping should focus their attention on state legislatures. If they fail there, they can attempt a repeal of the 21st Amendment. Until that time, it is my sworn duty to enforce the laws legitimately passed by my legislature. And I serve notice at this time that the law will be enforced most aggressively against those who are deliberately violating the laws of my state.

ENFORCEMENT PROBLEMS

State enforcement of alcohol laws are complicated by several factors:

- The number of direct shippers violating the law (and the volume of shipments),
- The perennial shortage of enforcement resources,
- Statutes that have not been updated to reflect current marketing practices through mail order, Internet, and direct shipments,
- The difficulties of obtaining information from out-of-state violators,
- The reluctance of some in-state customers to report the violations or to cooperate with investigators,
- Problems establishing personal jurisdiction over defendants in another state,
- Difficulties inherent in prosecuting an out-of-state defendant, and

- The occasional reluctance of other states to extradite a defendant for criminal charges. It is particularly regrettable that some states are reluctant to extradite defendants, as a means of protecting their domestic alcohol industries. This is tantamount to aiding in the efforts of businesses that are violating the law.
- The lack of cooperation by delivery services which generally resist attempts by state investigators to gather information.

In Utah's Beer Across America case, we were thwarted at the trial court level because the judge accepted the argument that defendants did not direct their efforts at Utah and that enforcement of state laws would improperly impair how the company conducted business in Illinois. We appealed this ruling because the implications of his decision would have taken the heart out of the legal basis for prosecutors to proceed against out-of-state defendants in any number of different crimes.

I am happy to report that last Thursday, the Utah Court of Appeals issued its ruling in the Beer Across America case. The court reversed the trial court and reinstated the criminal charges. The appeals court made three significant rulings that apply to our criminal prosecution:

- First, the state has personal jurisdiction over a criminal defendant if that defendant is present in court. Civil concepts of minimum contacts are not applicable in criminal cases.
- Second, Beer Across America is subject to prosecution in Utah for conduct committed in Illinois because its conduct caused an unlawful result in Utah.
- Third, Utah's prosecution is valid under the 21st Amendment and does not run afoul of the Constitution's Commerce Clause.

This decision only clarifies Utah law and our criminal prosecutions. It is a good first step. However, attempts to enforce civil law and to remedy subject matter jurisdiction problems remain unsolved. Florida still is being thwarted in bringing a civil enforcement case. Legislation still is needed. We must also be mindful that further appeals of Utah's decision are possible. We cannot ask other states to continue to hold off on enforcement pending any further appeals in our case—especially since our case involves criminal proceedings, not civil ones.

Florida alcohol regulators attempted to enforce their laws in a civil enforcement action. State courts said they lacked personal jurisdiction over the defendants in Florida and could not proceed.²⁹ The state tried to solve this problem by using the Webb-Kenyon Act's proscriptions against violating state laws and suing in federal court—where personal jurisdiction was not a problem. The federal court ruled that, as currently written, the Webb-Kenyon Act does not give the states a cause of action to file suit in federal court.³⁰ Once again the direct shippers are flouting the law and finding ways to avoid accountability.

If the Webb-Kenyon Act or the 21st Amendment or state laws regulating the sale of alcohol are to remain viable, there must be a means for states to enforce those laws. If the states continue to lack an effective enforcement method, there will be even more massive disregard of constitutionally permitted restrictions and states rights. But, the answer is not to federalize the crime or to have federal agencies prosecute the violators. This is a state law problem where enforcement actions represent the implementation of legislative policy decisions regarding state police powers. We are not seeking a federalization of this problem. We do, however, seek federal assistance in solving unique problems facing the states.

State enforcers are making great efforts to solve this problem. It is getting larger by the day. More and more companies are thumbing their noses at state laws and state enforcement actions. We are asking Congress to remove the legal technicalities behind which some of these crooks are hiding. Enforcement must continue unless or until policy makers in the individual states alter their policies. What these shippers want is for the courts to overrule the policy decisions of the statehouses.

While direct shippers may have a pipe dream that the U.S. Supreme Court may soon eviscerate the powers of states and the validity of the 21st Amendment, they cannot be rewarded for that dream by getting free passes to violate the laws they now are challenging. They have chosen to flout the law instead of changing it. This is a law enforcement problem and it must be solved now.

²⁹ *State v. Sam's Wine and Liquors*, Case No. 97-3828 (Fla 1st DCA 1999). This is not a complete barrier to enforcement. It only means the state cannot act early to stop shipments and must wait until it has evidence of sufficient shipments for personal jurisdiction over the violators to attach.

³⁰ *Florida Dep't of Business Regulation v. Zachy's Wine and Liquor*, 125 F.3d 1399 (11th Cir. 1997) cert denied 18 S.Ct 1402, 140 L.Ed.2d 660 (1998).

RECOMMENDATIONS

We cannot emphasize enough the seriousness of our concern about the reprehensible conduct of these direct shippers who are deliberately violating state laws. They are seeking to be excluded from the ordinary obligations of businesses: paying taxes, submitting to quality control inspections of their products, and complying with statutory restrictions on their operations. Even worse, their conduct is directly contributing to the increased availability of alcohol to minors.

To help us in solving this problem, I offer the following recommendations:

Prompt passage of federal legislation with the following components:

- First, grant the states jurisdiction in federal courts to halt violations of state law by out-of-state violators.
- Second, give the states effective relief against violators. Ideally, the federal court action would halt the conduct, punish the violator, and deter further violations by defendant and other companies. At the least, legislation must enable states to halt the illegal conduct and empower the courts to impose contempt on recidivists.
- Third, make the federal court process effectual and efficient. Allow venue where the illegal shipments are received, in addition to general venue provisions. Permit nationwide service of process. Provide for bench trials, not jury trials. If the federal court actions will not permit the state to enforce the full panoply of state enforcement powers, make sure that the federal action is not the exclusive remedy for the states.

A Congressional reaffirmation of the powers of states to set their own alcohol control policies and a call to all liquor producers or distributors to comply with state laws. This can be done with the Senate Report to accompany this legislation or testimony before the Congress. At the same time, we would hope that state alcohol regulators will recognize the seriousness of this type of violation and use an injunction issued under this new statute as grounds to suspend or revoke the licenses of violators.

Consider adopting requirements that any alcohol shipped across state lines by commercial carriers clearly identify the shipper, describe the contents of the package as alcohol, and require an adult signature. Packages containing alcohol should not be permitted to be left on porches or in bushes—even if a state permits direct shipments.

CONCLUSION

I appreciate the opportunity to present our views on this very important issue. We commend you for taking steps to assist states in their efforts to halt this burgeoning illegal practice. We respect the rights of direct shippers to ship their products in conformance with the law and respect their rights to petition state lawmakers to adopt new state alcohol policies.

However, we categorically reject the current practice of violating the law and adopting a battle strategy of trying to overturn state control over this product—and in the process eviscerate both the 21st Amendment and the Webb-Kenyon Act.

The terms of engagement for this battle were aptly described in a newspaper article in California:

Cushioned from risk by the limited jurisdictions and enforcement abilities of other states, the absence of any meaningful punishment such as fines or loss of sales license, and by their wine shippers—who are the primary target of most enforcement—local wineries and other direct mail wine operations have joined an underground industry where each year an estimated five million cases of wine are sold and shipped illegally.

* * * * *

I would say it's like being an accessory to the crime, [industry consultant Sara] Schorske said.

* * * * *

The St. Helena winery owner who wished to remain anonymous estimates that selling his wines by direct mail brings in upwards of \$150,000 a year. He said that approximately five percent of his direct wines sales are to reciprocal states.³¹ And, while he said he has wondered lately if an unusually high volume of out-of-state

³¹This means that 95 percent of the sales and shipments are to non-reciprocal states—where the sales are illegal.

inquiries about his wines conceals a sting operation aimed at his business, he isn't going to stop. "I said let's look at this from a business point of view. This business means \$150,000 a year to us. We're not going to walk away from that," he said. "And I'm not a gambler either."³² (Footnote added).

The CHAIRMAN. Mr. Diamond, we will turn to you.

STATEMENT OF STEPHEN DIAMOND

Mr. DIAMOND. Mr. Chairman and Senators, I have submitted a longer statement which I would like to summarize now. I am here to suggest that Federal help may well be necessary to preserve relative State autonomy in alcoholic beverage regulation, and that such help conforms with the spirit of the 21st amendment and that the 21st amendment is not and should not be read as a dead letter.

My remarks will therefore focus on two topics. Are interstate sales more of a threat to State alcoholic beverage regulations now than they were in the past, and has the 21st amendment become so eviscerated that it no longer shields any significant State regulatory efforts and there is not deserving of congressional support?

Circumstances have changed drastically in recent years. Volumes of shipments have unquestionably grown. Shipments of wine have increasingly come directly from the suppliers, and thus are asymmetric, with a few States being significant net exporters, while the other States are larger importers. The most dramatic difference between contemporary interstate sales and that of earlier decades is the growth of industry advertising, which in the past was usually limited or prohibited. Cheaper out-of-State products could not then be so easily identified. Now, the Internet is available.

Ambivalence about marketing is revealed in the most sympathetic argument for interstate shipment, which is the story of a small winery whose product was tasted and admired by a tourist who was subsequently frustrated to discover that he or she could not purchase it back home. The demand was not stimulated by the seller, it is implied, but preexisted in the buyer. What was being sought was not price savings, including possible tax avoidance, but access to otherwise unavailable products.

Many States are sympathetic to such a story and have passed regulations to permit such shipments of wine, in particular. More States are considering them. There must, however, be a way to prevent shipment into a State on such a scale as to challenge the State's fiscal system and three-tier regulatory regime. Both monopoly and license States often derive significant revenues from mark-ups or excise taxes.

Moreover, wholesalers and retailers need to be assured of sufficient sales returns to compensate them for the many regulatory restraints under which they operate, and to make it unlikely that they become so economically pressed as to turn in desperation to what used to be termed the classic liquor evils—pushing sales to the underaged, the intoxicated, selling after hours, et cetera.

In spite of the recent decision in Utah, State court prosecutions are still problematic. Personal jurisdiction is uncertain, perhaps because judges are reluctant to permit criminal convictions in these matters. The proposed bill is less onerous in its consequences for shippers, since it only provides injunctive relief, and more efficient

³² Jeremy Jay, *Special Report: On Wings of Wine*, St. Helena Star, Jan. 12, 1995 at 1.

in administration, since the judgment, if granted, will automatically be enforceable in all Federal courts.

I believe the State systems are still functioning and deserve protection from out-of-State challenges to their integrity. This is not to say that they cannot be improved. They have in the past, and continue to adjust. Their variety is the price we pay for federalism, and the price that was specifically paid to achieve repeal of the 21st amendment and to provide for a range of alcoholic beverage regulatory regimes which fairly reflect the fact that even now, as Judge Posner has observed, there is no consensus within the United States on how the sale and use of alcoholic beverages should be regulated.

The 21st amendment has not been critically eroded by Supreme Court decisions. It is, of course, true that the broad reach of the amendment enunciated by Justice Brandeis in the 1930's is no longer accepted in its entirety. With regard to economic regulation, the Court has rejected protectionist State taxes, price affirmation, fair trade legislation, and State limitation of factual alcoholic beverage advertising. This does not lead to the conclusion that the 21st amendment has ceased to protect State regulations from the challenge that they violate the dormant Commerce Clause, nor that State regulations necessarily are preempted by Federal legislation enacted under the Commerce Clause.

In *324 Yorkshire v. Duffy*, the Court did suggest that mandatory price markups were valid. In *44 Liquor Mart*, Justice Stevens declared that the State could pursue its temperance aims by taxes or by establishing minimum prices. In *Rice v. Norman Williams*, Justice Stevens again concurring, observed that the State presumably could regulate the wine market by fixing retail prices itself. Such regulatory programs would be devastatingly undercut by uncontrolled interstate shipments.

The limits which have been placed by the Supreme Court upon State action with regard to alcoholic beverages should actually give Congress greater confidence if it acts to facilitate enforcement by States of their importation rules. The 21st amendment does not have any requirement that Congress implement its terms. Congress has, in the FAA, passed legislation in part to support State regulation. To do so again would comport with the spirit, history, and present role of the 21st amendment.

Thank you.

The CHAIRMAN. Thank you, Mr. Diamond.

[The prepared statement of Mr. Diamond follows:]

PREPARED STATEMENT OF STEPHEN DIAMOND

My name is Stephen Diamond. I am a Professor of Law at the University of Miami Law School where I have taught classes on the evolution of the Twenty-first Amendment and local, state and federal regulation of alcoholic beverage trade practices. I am also an Adjunct Professor of History there where I teach a course on the history of Prohibition and the early Repeal Regime.

I am not here to speak about the specific merits and demerits of the proposed bill, but to trace how the problem of interstate sales has arisen and to suggest that Federal help is probably necessary to achieve a solution.

I do think that federal intervention of some kind is desirable to preserve the realm of relative state autonomy in alcoholic beverage regulation and that such an intervention conforms with the spirit of the Twenty-first Amendment, and that the Twenty-first Amendment is not and should not be read as a dead letter.

My remarks will therefore focus on two topics:

1. Is there in practice a new set of circumstances with regard to interstate shipments that has emerged, for which the existing legal regime is inadequate to protect state authority to define its own importation and distribution regulations with regard to alcoholic beverages. The Supreme Court, on several occasions, even when finding particular state practices to be unconstitutional, has continued to describe importation and distribution as the “core” concerns of the Twenty-first Amendment.

2. Has the Twenty-first Amendment become so attenuated as a shield for state autonomy, so “eviscerated”, in Justice O’Connor’s lamenting phrase in dissent in *324 Yorkshire v. Duffy*, that it no longer protects any significant state regulatory efforts and therefore is not deserving of Congressional support?

To evaluate the present threat posed by interstate shipment is problematic. As with any underground activity, figures are hard to come by and often offered for at least suspect motives. We were told several years ago, at a meeting in Chicago of the National Conference of State Liquor Administrators, that the value of such shipments was already one billion dollars, a figure probably chosen to imply that efforts to frustrate and impede such trade would be as ineffectual as King Canute ordering back the tide or the Prohibition Bureau stamping out the bootlegger.

Conversely, when the State of Florida sued out-of-state shippers in both state and federal court, the defense suggested that the amount of shipments was greatly exaggerated—the state’s estimate of lost tax revenues was, I believe, based upon the one billion dollar figure—and that the violations, if that was how to describe them, were de minimus.

There have long been de minimus defenses—though controversial ones—to efforts to prohibit interstate shipments. It was on such grounds that the lower court, in the famous *Idlewild* case, based its conclusion that New York’s efforts to prohibit sales at the airport duty free store violated the commerce clause. The low volume of sales, although not referred to by Justice Stewart in his opinion for the majority of the Supreme Court, was in effect an answer to Justice Black, who, in dissent, was concerned that permitting such sales might endanger the profitability of New York State retail stores.

Interstate shipments by car, usually transported by the purchaser for importation into his own state, and usually in limited quantities, had been a topic of discussion at regional NCSLA meetings and a focus of intermittent enforcement efforts—in the states where they were not legal—since the early days of Repeal. The volumes involved only became a significant issue where large cities were located near the state border. State regulators were under pressure from colleagues in sister states; they were in effect mutually hostage to the consequences of price-cutting and tax-lowering wars.

The circumstances, or at least the potential circumstances, of interstate shipment of alcoholic beverages have changed drastically in recent years. Volume has unquestionably grown. Techniques of efficient transportation over long distances have improved. The shipments of wine have increasingly come directly from the suppliers, and thus are asymmetric with a few states, California, of course, in particular, being significant net exporters while other states are largely importers. The states are not mutually vulnerable, in the sense that New York and New Jersey were. What is really reciprocal about California and Illinois agreeing to permit shipments purchased by residents of each state of the wine produced in the other? It should be added, however, that if interstate shipments are not re-regulated and controlled, U.S. wine producers may find themselves in competition with foreign producers who are presently considering exporting to one state and undertaking nation-wide internet sales from that site.

The most dramatic difference between contemporary interstate sales and that of earlier decades is the growth of industry price advertising, limitations on which were recently prohibited as violations of the First Amendment in *44 Liquor Mart*. In the past, such advertising was usually prohibited. Cheaper out of state products could not be so easily identified.

This served to some extent to reduce the amount of interstate crossing to purchase cheaper goods in the neighboring state. The spirit of this older regime is still at least in part reflected in the fact that some states which have entered into reciprocal inter-state wine shipment agreements with California prohibit direct mail solicitation by the out-of-state wineries. What this means is the growing world of Internet marketing is unclear. The ambivalence about marketing is reflected in the most sympathetic argument for inter-state shipment outside of traditional channels which is the story of a small winery whose product was tasted and admired by a tourist to the winery region, who was subsequently frustrated to discover that he or she could not purchase more of the product in his or her own state, because wholesalers would not carry it. (We will leave unexplored the possibility that its un-

availability was because it was an item which the winery preferred to ship on allocation to those who ordered directly from it so that it might retain the full retail price for itself or whether it feared that entering the traditional distribution system might lock it into a wholesaler who would not support the brand). The demand was not stimulated by the seller, but pre-existed with the buyer. What was being sought was not price savings, including possible tax avoidance, but access to otherwise unavailable products. Many states are sympathetic to such a story and have passed regulations to permit such shipments, of wine in particular. While the type, amount, and circumstances under which importation is permitted vary, a general pattern emerges: opportunities are being offered to in-state consumers to purchase unavailable products. I am told that, presumably responding to such pressures, the Wine and Spirits Wholesalers Association is supporting a program in all license states in which a buyer may special order any wine through the system upon payment of the appropriate state taxes. I am also informed by a National Alcoholic Beverage Control Association official that all of the states that wholesale wine also permit special ordering, although the effort is not always successful either because the state, Utah, for example, is not on the marketing horizon of the winery, the winery dislikes dealing with government officials, or it refuses to give up some of the full retail price to the lower tiers of distribution.

To the extent that consumers simply want to purchase tax avoidance, the quest should not be facilitated, but indeed it should be frustrated. To the extent that what they seek is a choice, there will be pressure for states to respond positively, already indicated in a number of states which are attempting to permit some importation of limited quantities of specifically defined products for personal use. There must, however, be a way to prevent shipment into a state on such a scale as to challenge the state's fiscal system and three tier regulatory regime.

The recent history of interstate shipment regulation in Louisiana is instructive. The legislature which had provided for limited interstate imports from pre-registered out-of-state sellers has just narrowed the scope of its permission to wineries which do not use wholesalers for additional distribution—whose product is therefore unavailable, as a result either of supplier or wholesaler decisions. In addition, beer and distilled spirits can no longer be similarly imported, and the supplier must now provide monthly rather than annual reports. Regulators in Louisiana have always been concerned about the capacity to assure tax compliance even with those who registered for shipment in the state but whose records and product are out of state. State administrators have talked of performing compliance stings, at least to establish confidence levels in the reporting. So far as I know, this has not yet been implemented.

Before turning to a discussion of the Twenty-First Amendment, I would like briefly to address an issue often raised by supporters of such shipments; if a state is serious about prohibiting them, should it not pursue the buyers, the in-state residents? There has long been a belief in alcohol beverage regulation that it is more effective to regulate sellers, whose interest is profits, and who therefore can be constrained by a combination of incentives and fines, that to try to regulate buyers whose motives are much more complex and volatile, and who may respond with defiance. This traditional approach is buttressed by a concern in the state that its own citizens may have been stimulated by increased marketing efforts. When the importation was by a Maryland resident driving to Washington, D.C., for example, to purchase cheaper alcoholic beverages, the buyer was responsible and enforcement, if undertaken, focussed on him.

While no one knows with any precision the extent of such shipments now, and while efforts are being made in a number of states to provide local consumers access to unavailable products, there is a realistic fear on the part of states, as reflected in NCSLA and NABCA resolutions, that failure to limit or control shipments, for the purpose of tax avoidance, for instance, will serve as a very slippery slope to the destruction of state alcoholic beverage regulation. This could well be a race to the bottom in which states lower their taxes, and thus abandon temperance regulation through price, for example, to discourage out-of-state purchases. The threat to the state regulatory system is real. Both monopoly states and license states often derive significant revenues from markups or excise taxes. Moreover, in license states, and in monopoly states which use private wholesalers to distribute beer or wine, the wholesalers and retailers need to be assured of sufficient sales returns to compensate them for the many regulatory restraints under which they operate and to make it unlikely that they become so economically pressed as to turn in desperation to what used to be termed the classic "liquor evils": pushing sales to the underaged, the intoxicated, selling after hours, even purchasing bootlegged liquor.

In addition, it is not totally far-fetched to fear that the long-term result of unregulated and unrestricted interstate shipments would be the rise of a small number of

mega stores buying in large volume. These stores might well be the beneficiaries of state tax exemptions and subsidies. It is unlikely that consumer welfare in the long run would be maximized by this process.

This is the problem. Now what are the solutions? Some states have attempted to prosecute or otherwise deter those engaging in unauthorized interstate shipments. This has proven difficult. In Florida, the state court found insufficient contacts to satisfy personal jurisdiction requirements for civil and injunctive relief. In Utah, the trial court did likewise in a criminal prosecution and also held that the restriction unconstitutionally restrained interstate commerce. That decision was just overturned. But state court prosecutions are still problematic, personal jurisdiction is uncertain, perhaps because judges are reluctant to permit criminal convictions in these matters. The proposed bill is less onerous in its consequences for shippers, since it only provides injunctive relief, and more efficient in administration since a judgment if granted will automatically be enforceable in all federal courts.

The second question is whether the state regulatory system is worth protecting, or whether it is so old-fashioned and out of date and so stripped of power by Supreme Court decisions of the last several decades that it is incapable and undeserving of rescue. I believe the system is still viable, still functioning, and deserves protection from out-of-state challenges to its integrity. This is not to say that it cannot be improved. It is a very positive sign that the State of Washington, for instance, is undertaking a year-long re-evaluation of its three tier system regulations. Present laws are hardly perfect, but this is not a constitutional obligation. Their variety is the price we pay for federalism, and the price that was specifically paid to achieve repeal of the Eighteenth Amendment, and to provide for a variety of alcoholic beverage regulatory regimes which could fairly reflect the fact that even now, as Judge Posner has observed, there is no consensus within the United States on how the sale and use of alcoholic beverages should be regulated.

The Twenty-first Amendment was accepted by Congress with the addition of the famous paragraph 2. This paraphrases though does not follow the precise language of the Webb-Kenyon act and was intended to constitutionalize it. The state was to be permitted to regulate the importation of alcohol beverages without fear that Congress might repeal the act and therefore subject state regulation again to the restrictions of the dormant Commerce Clause. Congressional debate over the Twenty-first Amendment and debate in the state ratifying conventions point in several directions. While sometimes it was suggested simply that the amendment was to protect dry states from interstate shipments, it was often asserted, and held by the Supreme Court in the famous Brandeis opinions, that the purpose was to give the states the authority to fashion their own alcoholic beverage regimes including monopoly of the wholesale and retail functions and, in the case of license states, the creation of the customary three tier system. These were the alternatives discussed in the famous Fosdick and Scott report commissioned just before repeal by John D. Rockefeller.

Of the many lessons that were drawn from the failure of Prohibition, one of the most important, often repeated on the floor of Congress in the Twenty-first Amendment debates, was that the federal government ought not to attempt to regulate and enforce rules about alcoholic beverage sales and use. It was for this reason that paragraph 3 of the proposed amendment, which would have given Congress concurrent power to regulate saloons, was withdrawn. This division between state and federal authority had been suggested even earlier, during Prohibition, by Emory Buckner, the U.S. Attorney from New York, who had proposed a division of enforcement responsibility: local officials to close down speakeasies; federal officials to deal with producers of interstate supply. In effect, this formulation was adapted to the regulation of legalized alcoholic beverages.

States could remain dry, create monopoly systems, or regulate alcoholic beverages under what is called the license system which usually has meant the creation and support of a three-tier system in which supplier, wholesaler, and retailer usually are kept independent. The critical point is that the retailer is independent of supplier pressure and domination. The American system since Repeal has been to temper the pressures on retailers through the regulation of wholesalers, to give retailers the independence to pursue respectability and good standing in the neighborhood as well as profit, to limit sales venues to prevent over-competition, with resulting failures. The social consequences of aggressive competition in alcoholic beverages are seen to be deleterious. Those who lose because the market cannot support all the retailers, a circumstance which would be aggravated by direct mail shipping, do not necessarily fold up their tents and quietly disappear. While they struggle for survival, they may cut corners; state regulators have generally chosen to reduce the risks of this occurring.

Tied-house evil regulation constitutes a parallel form of anti-trust law, one which protects small retailers from discriminatory behavior on the part of those above them in the distribution chain.

The theory of Repeal was one of compromise and moderation. Moderation in consumption, moderation in the pursuit of profit, somewhat analogous to the philosophy behind public utilities, and moderation in lawmaking: no longer would the law demand that which would not be obeyed and could not be enforced.

Those who argue for free trade in wine ignore not just the Constitution, and the past history of this country but contemporary attitudes. Almost no one thinks the sale or use of alcoholic beverages should be unregulated. Alcoholic beverages provide a source of pleasure; abused, they create significant social dangers.

Alcoholic beverages need regulation and most of the regulation must be at the state and local level. That is the intent of the Twenty-first Amendment. Even if it had the authority, the BATF presently has neither the interest nor the resources to regulate alcoholic beverages effectively. The Supreme Court still defines the "core" state powers protected by the Twenty-first Amendment to be the importation and distribution of alcoholic beverages.

It has been suggested that the Twenty-first Amendment has been seriously eroded by Supreme Court decisions over the last several decades and no longer has enough force to justify a call for action by Congress to protect the states. This is not the case. It is of course true that the broad reach of the Twenty-first Amendment enunciated by Justice Brandeis in the 1930's is no longer accepted in its entirety. It was not accepted by everyone even at the time. Brandeis, for instance, declared that the Twenty-first Amendment was not limited by the Fourteenth Amendment, but no one argued for, or attempted to impose, a formal prohibition upon the sale of liquor to African-Americans, for instance. His support of retaliatory protectionist legislation, which he called protective, was criticized but was probably a factor in persuading states to abandon most overt protectionist legislation by around 1940.

The Supreme Court has declared that the Twenty-first Amendment does not shield state alcoholic beverage regulations from due process or equal protection challenges when regulations are attempting to limit sale of alcohol beverages to those identified by their families or public authorities as inebriates or to maintain a lower legal drinking age for young women than for young men.

With regard to economic regulation, the Court has rejected protectionist state regulations, specifically an effort by Hawaii to exempt at least some locally produced alcoholic beverages from state taxes imposed on all imported products. (In *Bacchus*.) In *Midcal*, the Court rejected as preempted by federal antitrust law, fair trade legislation, in which the state delegated authority to suppliers who could fix the price at which their product was to be sold to retailers. This was not actually much of a restraint. Some states had already voluntarily withdrawn such laws and the California ABC did not appeal an adverse lower court decision in *Midcal* and clearly had abandoned support of its own rules.

The Court has also prohibited price affirmations statutes—the same results can apparently still be imposed by contracting monopoly states—which required that a supplier affirm that the price being charged to its wholesalers was no higher than that charged to wholesalers in any other specified state. This was rejected on the ground of its extra-territorial impact. The Court asserted that extra-territorial legislation was prohibited by the Commerce Clause, but I believe that it is better explained, as Professor Regan of Michigan has argued, as a limitation implicit in the very conception of a federal system.

The Supreme Court has also rejected, at least in part, a tradition of state limitation of alcoholic beverage advertising, declaring that truthful factual advertising is protected by the First Amendment.

This does not lead to the conclusion that the Twenty-first Amendment has ceased to protect state regulations from the challenge that they violate the dormant commerce clause, nor even that state regulations necessarily are preempted by federal legislation enacted under the Commerce Clause.

In *324 Yorkshire v. Duffy*, in which the Court rejected a New York rule which permitted wholesalers to post prices in such a way as to determine retailers' profit margins, the Court did suggest that mandatory price mark-ups were valid. In *44 Liquor Mart*, in which a prohibition upon price advertising was struck down, Justice Stevens declared that the state could pursue its temperance aims by taxes or by establishing minimum prices. In *Rice v. Norman Williams*, upholding a primary source rule, Justice Stevens again, concurring, observed that "the State presumably could regulate the wine market by fixing retail prices itself. * * *" Such regulatory programs would be devastatingly undercut by uncontrolled interstate shipments. In *Midcal*, even as it found fair trade legislation to be pre-empted, the Court stated: "The Twenty-first Amendment grants the States virtually complete control over

whether to permit importation or sale of liquor and how to structure the liquor distribution system.”

As long ago as *Idlewild*, in which Justice Stewart insisted that the Twenty-first Amendment had to be read alongside of other Constitutional provisions, in a case where the state was found to have no authority to prohibit duty free sales of alcoholic beverages being shipped out of the country, Justice Stewart did assert that “a State is totally unconfined by traditional Commerce Clause limitations when it restricts the importation of intoxicants destined for use, distribution, or consumption within its borders.” It is worth remembering that the Twenty-first Amendment speaks of “transportation and importation” “for delivery or use.” Regulation of importation for use is protected by the Constitutional shield. The state is not to be left with authority only to regulate sale, and if direct mail shipments continue to grow, potentially only of drinking on licensed premises.

In spite of the Supreme Court opinions rejecting specific state laws or regulations, what has never been abandoned is the recognition that states have authority to establish the terms by which alcoholic beverages can be imported and distributed within their borders. Indeed, it is obvious that without control over importation, the state cannot effectively regulate distribution.

These decisions do not eviscerate the Twenty-first Amendment even though the Twenty-first Amendment is no longer as broad a shield from federal preemption as it once was. The core powers of regulating the conditions of importation and distribution are still largely unconstrained. States can impose primary source rules that frustrate gray market sales. The three-tier system and state monopoly still function as institutions to permit access to yet constrain and regulate the methods of sale of products which society does not believe should be available without regulation. The fears that were asserted by some contemporaries simultaneously with Justice Brandeis’s broad reading of the Twenty-first Amendment, that states might act to protect local industry and state regulation might be seized by private parties—a suspicion that of course can arise with regard to almost any legislation—are now significantly assuaged by the cases earlier described and by such lower court decisions as

- *Pete’s Brewing v. Whitehead*, rejecting a Missouri beer labeling statute. The limits which have been placed by the Supreme Court upon state action with regard to alcohol beverages should actually give Congress greater confidence if it acts to facilitate enforcement by states of their importation rules.

Even though the state might justify restrictions on importations simply by a formal reference to the Twenty-first Amendment, states are not making a formal claim alone. Uncontrolled importation from out of state without effective restrictions will threaten state tax revenues, the state fiscal system, and the three-tier system.

While the Twenty-first Amendment does not have any requirement that Congress implement its terms, Congress has already in the FAA chosen to pass legislation whose purpose at least in part was to support state regulation enacted under the Amendment’s protection. To do so again would comport with the spirit and history of the Twenty-first Amendment.

The CHAIRMAN. We will now turn to you, Brendan.

STATEMENT OF BRENDAN BROGAN

Mr. BROGAN. Good morning. My name is Brendan Brogan and I am an 18-year-old senior at Ridgewood High School in Ridgewood, NJ. I also serve on the National Board of Directors of Mothers Against Drunk Driving. MADD is an organization that represents over 3 million Americans, and exists to end the senseless violent crime of drunk driving, to secure basic rights, to meet the needs of victims of drunk driving, and to prevent underage drinking. MADD members and supporters are not just mothers. They include mothers, fathers, brothers, sisters, victims, nonvictims, and a growing number of youth just like me.

Although often viewed as an organization singularly focused on drunk driving, MADD since its inception has also been dedicated to preventing underage drinking in order to stop youth drinking and driving. MADD was instrumental in the passage of the Federal

minimum drinking age law in 1984, which resulted in raising the legal drinking age to 21 across the Nation.

MADD continues to advocate stringent enforcement of the 21 law because it has proven to be the single most effective measure in reducing alcohol-related traffic fatalities among people between the ages of 16 and 20. In fact, minimum drinking age laws are estimated to have saved more than 17,000 lives since 1975. Between 1985 and 1995, the proportion of drivers 16 to 20 years of age who are involved in fatal traffic crashes who were intoxicated dropped 47 percent, the largest decrease of any age group during this time period.

In addition, MADD was also a strong supporter of, and played an active role in the passage of zero tolerance Federal legislation in 1995 that required all States to lower the illegal blood alcohol limit for drivers under the age of 21 to .02. Zero tolerance is now the law of the land, and more young lives are now being saved as a result of this initiative. Many young people around the country testified in support of these laws because they were tired of going to class reunions at the funerals of their classmates who had died in alcohol-related crashes or as a result of alcohol-related incidents.

While tremendous progress has been made in reducing alcohol-related traffic fatalities among youth, alcohol continues to be the most frequently used and abused drug by high school seniors. Despite the fact that it is illegal to sell alcohol to underage youth and it is illegal for those under 21 to purchase alcohol, it remains readily available to youth and underage drinking still borders on epidemic proportion.

In 1997, 2,309 young people ages 15 to 20 died in alcohol-related traffic crashes. In the last 2 years, we have witnessed a growing number of tragic binge-drinking alcohol-related deaths of college students on campuses in Massachusetts and Louisiana. At the age of 14, I was almost one of those students.

My friends and I had been stockpiling alcohol for weeks, and on the night in question I sneaked out of my house and went to a school playground with an assortment of booze and a backpack. This was not the first time my friends and I had drunk, but I was now a high school freshman and I wanted to show my friends how I could really drink.

We all proceeded to get drunk, and later that night my drinking buddies dragged me back to my house and dumped me on my head through the window. I drifted in and out of consciousness and was aspirating my vomit when my friend, Dan, finally woke my father, who rushed me to the ER. When I arrived at the hospital, I was comatose and had a blood alcohol level of .20. I was lucky. I could easily have died of alcohol poisoning just like those college students did.

I am like a lot of high school students than and today who drink underage. At 14, I knew too well the problems associated with alcohol abuse and underage drinking. You see, many male members of my family for generations have died of alcoholism, and five out of six brothers, including my father, are recovering alcoholics. Underage drinking almost killed me, and the experience has brought me to where I am today.

Underage alcohol use contributes to numerous health and social problems, including risky behavior, such as under-the-influence driving without a seat belt or a motorcycle helmet or a bicycle helmet; traumatic injury and death due to motor vehicle crashes, falls, fires, and drowning; homicide and suicide; risk of overdose and death by alcohol poisoning; early onset of alcohol abuse and dependence, as previously stated; high-risk sexual behavior that may lead to unplanned pregnancies, HIV infection, or other sexually-transmitted diseases; other types of violence such as physical and sexual assault; and involvement in other criminal activities. Researchers estimate that alcohol use is involved in one to two-thirds of sexual assault and acquaintance or date rape cases among teens and college students.

Accessibility and availability of alcohol are the main contributing factors to underage drinking. Alcohol is easy to get, and most kids in my school and my community know where to get alcohol if they want it. Based on a study, nearly 90 percent of 10th graders and 75 percent of 8th graders think it is either fairly easy or very easy for them to get. These students ranked alcohol as a close second in perceived availability behind cigarettes. Almost two-thirds, or 6.9 million, junior and senior high school students who consumed alcohol in 1991 purchased their own directly. Studies confirm that anywhere from 30 to 70 percent of retail outlets illegally sell alcohol to minors. One sweep by a Louisiana Department of Alcohol and Tobacco Control in 1996 found that 57 out of 60, or 95 percent, illegally sold alcohol to underage youth.

I mentioned earlier that the 21 minimum drinking age law has been the single most effective measure in reducing traffic-related deaths in the 16- to 20-year-old age group. However, by making beer, wine and distilled spirits available to thousands of junior and senior high school and college students across the country through web sites and other direct access methods, these tools have virtually eliminated the 21 drinking age law.

Enforcing the minimum drinking age laws in bars, restaurants, package stores and other licensed beverage outlets is difficult, to say the least. Enforcing the law on the Internet and web sites is virtually impossible. Allowing home, apartment, or dorm room delivery of alcohol to those under the age of 21 is turning Federal Express and UPS drivers into bartenders.

Thank you, Senator.

The CHAIRMAN. Well, thank you, Brendan. That was a pretty dramatic story. We appreciate having you here and appreciate your willingness to share that with us.

[The prepared statement of Mr. Brogan follows:]

PREPARED STATEMENT OF BRENDAN BROGAN

Good morning. My name is Brendan Brogan. I am an 18-year-old senior at Ridgewood High School in Ridgewood, New Jersey. I also serve on the National Board of Directors of Mothers Against Drunk Driving (MADD). MADD, is an organization that represents over three million Americans and exists to end the senseless violent crime of drunk driving, to secure basic rights and meet the needs of the victims of drunk driving and to prevent underage drinking. MADD members and supporters are not just mothers. They include mothers, fathers, brothers, sisters, victims, non-victims and a growing number of youth just like me.

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In addition, MADD was a strong supporter of and played an active role in the passage of the "zero tolerance" federal legislation in 1995 that required all states to lower the illegal blood alcohol limit for drivers under the age of 21 to .02 or less. Zero tolerance is now the law of the land and more young lives are being saved as a result of this initiative. Many young people around the country testified in support of these laws because they were tired of going to class reunions at the funerals of their classmates who had died in alcohol-related crashes or as a result of other alcohol-related incidents.

While tremendous progress has been made in reducing the alcohol-related traffic fatalities among youth, alcohol continues to be the most frequently used and abused drug by high school seniors. Despite the fact that it is illegal to sell alcohol to underage youth and it is illegal for those under age 21 to purchase alcohol, it remains readily available to youth and underage drinking still borders on epidemic proportion. In 1997, 2,309 young people ages 15–20 died in alcohol-related traffic crashes. In the last two years we have witnessed a growing number of tragic binge drinking alcohol-related deaths of college students on campuses in Massachusetts and Louisiana, just to mention a few. At the age of 14, I was almost one of those students.

My friends and I had been stockpiling alcohol for weeks and on the night in question I sneaked out of my house and went to the school playground with an assortment of booze in a backpack. This was not the first time my friends and I drank but I was now a freshman in high school and I wanted to show my friends how I could really drink. We all proceeded to get drunk and later that night my "drinking buddies" dragged me back to my house and dumped me on my head through the window. I drifted in and out of consciousness and was aspirating on my vomit when my friend Dan finally awoke my father who rushed me to the ER. When I arrived at the hospital I was in a coma and had a blood alcohol level of .20. I was lucky. I could easily have died of alcohol poisoning just like those college students did. Unlike a lot of high school students then and today who drink underage, at age 14, I knew all too well the problems associated with alcohol abuse and underage drinking. You see, most of the male members of my family for generations had died of alcoholism and five out of six brothers, including my father are recovering alcoholics. Underage drinking almost killed me and that experience brought me to where I am today.

PROBLEMS ASSOCIATED WITH UNDERAGE DRINKING

Drunk driving deaths and injuries are only part of the problems associated with underage drinking. Studies reveal that people who start drinking at age 14 and younger are approximately four times as likely to become alcohol dependent as are those who begin drinking at age 20 or older. The results of a Harvard School of Public Health College Alcohol Study published in 1998 revealed the following: Two of five students were binge drinkers and one in five was a frequent binge drinker. Four of five residents of fraternities or sororities were binge drinkers. Student binge drinking is by far the single most serious public health problem confronting American colleges. Half of all college students surveyed who drank alcohol were binge drinkers. Of the students who drank, 20 percent drank on 10 or more occasions in the past 30 days, 42 percent binge drink when they drink and 52 percent drink just to get drunk. Thirty-six percent of those who drank admitted they drove after drinking. A 1996 survey by the American Medical Association found that 33 percent of 19 and 20 year olds consume at least four alcoholic beverages on an average night, and 20 percent have six or more drinks (AMA, 1996). While drinking among college students is viewed by many as a "rite of passage," this potentially deadly view also prevails at the high school level. The rate of drinking and binge drinking among high school and grade school students should serve as a wake-up call for parents, legislators and the public because a major determinant of college binge drinking is students who use alcohol in high school or at younger ages.

Although it is illegal for all secondary students to purchase alcoholic beverages, 81 percent of twelfth graders have tried them at least once, along with 71 percent

of tenth graders and 55 percent of eighth graders. (Johnson et al, 1996a) According to the 1995 Youth Risk Behavior Survey, 39 percent of twelfth graders and 30 percent of tenth graders reported they had consumed five or more drinks of alcohol on at least one occasion during the last 30 days. This figure was 33 percent for all high school students, 36 percent for male high school students, and 29 percent for female high school students (CDC, 1996). According to the Monitoring the Future Study, about 30 percent of the nation's twelfth graders, 24 percent of tenth graders, and 15 percent of eighth graders reported in 1995 that they had consumed five or more drinks of alcohol on at least one occasion in the last two weeks. In addition, about 33 percent of twelfth graders, 21 percent of tenth graders and 8 percent of eighth graders reported that they had been drunk during the last 30 days (Johnson et al, 1996b).

Underage alcohol use contributes to numerous health and social problems including:

- Risky behavior, such as driving under the influence and driving without using a seat belt, motorcycle helmet or bicycle helmet.
- Traumatic injury and death due to motor vehicle crashes, falls, fires, and drowning.
- Homicide and suicide.
- Risk of overdose and death by alcohol poisoning.
- Early onset of alcohol abuse and dependence as previously stated.
- High-risk sexual behavior that may lead to unplanned pregnancies, HIV infection or other sexually transmitted diseases.
- Other types of violence such as physical and sexual assault.
- Involvement in other criminal activities (NIAAA, 1997)

Researchers estimate that alcohol use is involved in one-third to two-thirds of sexual assault and acquaintance or date rape cases among teens and college students (OIG, 1992)

The federal and state governments spend billions of dollars each year in this country to address the problem of illicit drug use by young people. Sadly, however, they close their eyes and turn a deaf ear to the most dominant drug problem among young people—alcohol.

As I have testified to, the extent of the underage drinking problem is evident and the problems associated with underage alcohol consumption are well documented despite being swept under the social rug. One of the questions that is the focus of this committee hearing is why we have this problem if it is illegal to sell alcohol to youth and illegal for them to purchase it. The answer to the question is simple;

ACCESSIBILITY AND AVAILABILITY OF ALCOHOL TO YOUTH

Accessibility and availability of alcohol are the main contributing factors to underage drinking. Alcohol is easy to get. Most of the kids in my school and in my community know where they can get alcohol, if they want it. Based on a study, nearly 90 percent of tenth graders and 75 percent of eighth graders think alcohol is either "fairly easy" or "very easy" for them to get. These students ranked alcohol a close second in perceived availability behind cigarettes (Johnson et al 1996a). Almost two-thirds or 6.9 million junior and high school students, who consumed alcohol in 1991, purchased their own directly. Studies confirm that anywhere from 30 percent to 70 percent of retail outlets illegally sell alcohol to minors. One sweep by the Louisiana Department of Alcohol Tobacco Control in 1996 found that 57 out of 60 outlets or 95 percent sold alcohol illegally to underage youth.

In the past, teenagers have primarily had three sources of alcohol: bars and other licensed establishments that do not check IDs; using a fake ID to buy alcohol; and alcohol provided by adults. We are now confronted with a new source for youth access to alcohol and that is Internet and other direct access venues.

I mentioned earlier that the 21 minimum drinking age law has been the single most effective measure in reducing alcohol-related traffic deaths in the 16 to 20 year old age groups. However, by making beer, wine and distilled spirits available to thousands of junior and senior high school and college age students across the country through websites and other direct access methods, these tools have virtually eliminated the 21 minimum drinking age law. Enforcing the minimum drinking age law in bars, restaurants, package stores and other licensed beverage outlets is difficult to say the least. Enforcing the law on Internet web sites is virtually impossible. Allowing home or apartment or dorm room delivery of alcohol to those under the age of 21 is turning Federal Express and UPS drivers into bartenders.

A recent study of more than 300 World Wide Web sites finds that 25 major alcohol beverage companies are using the Web to advertise and promote their products through a variety of marketing techniques-such as sponsorship of music and sports, interactive games and contests, and chat and message boards that capitalize on the Web's strong attraction for young people. Overall, there are now hundreds of Web sites that promote alcohol, drinking and specific products. Nearly five million youth ages 2 to 17 used the Internet or an on-line service from school or home in 1996 and more than nine million college students use the Internet regularly (Center for Media Education, 1997a1b/c). Over the last two years, the number of Internet users under the age of 21 has skyrocketed.

My peers don't know about a society without the Internet. We've always had computers. Cyberspace is as much a part of our lives as is the television. In this very real dimension, there is currently no mechanism in that world to ensure that someone who purchases alcohol is of the legal drinking age. Enforcement of the 21 minimum drinking age law is critical to the effectiveness of this law and the local UPS driver should not have the responsibility for this enforcement. The key to enforcing laws against selling alcohol to minors is face to face confrontation between the seller and the buyer. You don't need to check an ID when the package is left at the doorstep.

Those who oppose restricting sales of alcohol over the Internet or by other direct shipment means argue that most young people under the age of 21 don't have a credit card and therefore cannot place an order. This is simply not the case in today's world. I have had a check/debit card since I was 16. In addition, as a high school senior I receive offers for credit cards in the mail almost every week. Later this year when I enroll in college, I assure you that during the first week of orientation the credit card companies will be out in full force offering free T-shirts in exchange for applying for their "college student" credit card.

We need to be finding solutions to the underage drinking epidemic and not creating new problems. We are spending millions of dollars a year on a taxpayer funded advertising campaign aimed at reducing illicit drug use among the youth of this country and not one dime of that money is being used to address the number one drug problem for youth and that is alcohol. Local and state agencies must be given the necessary tools to enforce the underage drinking laws and the federal government must lead in the fight to protect the future of all of us. The Internet is a fantastic key to the world. It should provide us unlimited information and knowledge. It should not however stock the bar for weekend underage parties.

We are repeatedly told that we as youth represent our nation's future. If that is true, the time is long overdue for the leaders in this country to invest in that future and get serious about the war on drugs. Alcohol may be a legal product for those over the age of 21 but by ignoring the fact that alcohol is the principal drug abuse problem for youth, you are fighting that war with one hand tied behind your back. My father is a Vietnam veteran and the only thing I know about that war is what I have learned from him, the history books and TV documentaries. What I have learned is that the so-called war on drugs we are waging will be another Vietnam unless our leaders recognize that the real enemy in the drug war is the accessibility and availability of alcohol to the youth of this country.

I want to thank the Chairman, Senator Hatch and the other members of the Committee for the opportunity to appear before you today. While my father was serving in Vietnam he bought a watch that was advertised as suitable for scuba diving or testifying before Congress. He gave me that watch a few months ago on my 18th birthday. Little did we know that the watch would be as advertised. I will be glad to answer any questions you may have.

The CHAIRMAN. Mr. DeLuca, we will turn to you now.

STATEMENT OF JOHN A. DeLUCA

Mr. DeLUCA. Thank you, Senator. First of all, I commend you personally for drawing attention to this very important issue. We make common cause with you. We perhaps, unfortunately, will not agree with the remedy that you propose, but certainly the effort. I want to thank the members of your committee, and especially our Senator, Senator Dianne Feinstein.

Having just heard Brendan and the others, I am going to depart from my prepared remarks and take a different course. But I would like to submit my prepared remarks which I think are appropriate.

The CHAIRMAN. Without objection, we will put them in the record.

Mr. DELUCA. I am the product of two worlds; culturally, European. My parents were Italian immigrants. I am a terrible statistic in this country. When I was 3 years old, I started drinking wine with my family, a little water. I didn't realize it at the time, but that was part of the several-thousand-year-old heritage that came with my ethnic and religious background. My children were raised the same way, as was my wife, Josephine, where it was introduced as part of our culture, as part of our meals.

I would offer to you that over the years I never felt that this was a forbidden fruit issue for me, I had to prove anything. There was no rite of passage. There was no need when I got to high school or college to prove anything. I feel great empathy for the comments that Brendan just remarked. Can you imagine what a terrible indictment of what is going on in this country that children, teenagers, young adults, feel that they have to prove their adulthood by blasting their brains by drinking to excess?

We have a lot to learn from other cultures. I spent several years in the Soviet Union with our Government. They had every control over distribution, advertising, cost, prices. And yet there, culturally, the issue of alcohol abuse and alcoholism was rampant. So, personally, as an individual, I believe we are talking about issues that go deeply to cultural trends.

On the other hand, I am a product of the United States. I have served in public policy positions and recognize that our industry, the wine industry, given the inheritance that we have in this society, cannot really progress unless it is a great example of social responsibility. In our State, when this issue first came to me, which was in 1985, and we talked of reciprocity and how would we adapt to wineries who didn't have access, I thought immediately in terms of trade agreements with our different States.

And so California, in 1986, passed the first reciprocity law which has now been engaged over the last 15 years, and let me read the States that are involved in reciprocity transactions—California, Colorado, Idaho, Illinois, Iowa, Minnesota, Missouri, New Mexico, Oregon, Washington, West Virginia, and Wisconsin. Lately, we have entered into very creative State-by-State crafting with Louisiana and with New Hampshire to address many of the issues that have been discussed today.

I think a very compelling argument can be made that we should support the model legislations and the draft legislations where you do have unsupervised shipments which occur in the States where it is illegal, but in the States where it is legal you have couriers who are trained. You have these stickers that I would like to enter into the record, where they are required on all wine shipments sent via Federal Express, where you must have a signature required and you must have identification when they are, in fact, delivered.

These safeguards also exist in our State, in California, and direct shipments, even though we are talking about interstate commerce, are presently in 30 States intrastate. So there is a longer history than just the present requirements that we have.

On the underage issue, it is a very serious question, but we have law enforcement agencies who are testifying in public that as far

as that issue is concerned, where it is supervised, where there are these safeguards, where you have couriers that are trained, where you have official requirements, that, in fact, is minimal, not that it doesn't exist, but it is minimal. It is not as serious as it is in the States where we don't have these safeguards.

So we are trying to craft State-by-State, creative solutions working with our wholesalers, with our retailers, who have been wonderful partners. We don't want to depart on that issue. However, the idea of a felony—and in 6 States this has now passed in the last few years—a felony that is enacted in a State for us sending directly to a consumer puts in basic, immediate jeopardy our permit, and that is—I want to conclude on that note. That has, in fact, led to a Federal remedy that doesn't require what you are proposing, and that is that the Bureau of Alcohol, Tobacco and Firearms which has jurisdiction over us has announced in a circular, 96-3, which was in February 1997, that, in fact, any case brought by the State that shows that there has been a violation of the State laws will cause that agency to immediately look into the issue, even to the point—and it is a death sentence for us—of suspending our basic permit.

So already at the Federal level, without any new laws that you are contemplating, there is a mechanism in place that can police this across the country because they have control over our basic permits. At the same time, Congress last year, as you recall, passed the Internet Tax Freedom Act and created the Electronic Commerce Tax Commission. We have legislators who have asked that this matter be looked into by that particular commission, including the issue of taxes, including the issue of revenues, including the issue of discrimination.

So my hope is that you will permit us, State by State, to work with wholesalers, retailers, as we respond to consumers—this is a very consumer-driven issue; without the consumers asking for it, we wouldn't be in this position that we are talking about; it is consumer-driven—that we work State by State to craft creative solutions. I fear that what you are proposing will have a chilling effect on our ability, and there will not be the incentive to keep working as we are in these different States.

Thank you very much.

The CHAIRMAN. Thank you, Mr. DeLuca.

[The prepared statement of Mr. DeLuca follows:]

PREPARED STATEMENT OF JOHN A. DE LUCA

MR. CHAIRMAN: I am John De Luca, President and Chief Executive Officer of the Wine Institute. Wine Institute is the association of over 450 California wineries which produce 80 percent of our nation's wine.

California's wineries and winegrape growers, along with their counterparts in other states, comprise a significant agricultural industry that continues in the proud tradition of family-owned farms. Wine's rich heritage is an asset to our economy, culture and cuisine which should be supported.

Our traditions, which began centuries ago in Europe, define us as agriculture, cuisine and tourism. As winemakers, we take great pride in the growth of our industry and with the fine quality of the wines which we are growing. These successes have been underscored by the astonishing growth of the premium wine industry over the past two decades, a time when nearly 1,000 new wineries have been founded across the country. With this success has also come media and critical acclaim for our wines. Yet today, small winery owners are cast as potential lawbreakers and even

felons for simply responding to the requests from consumers across the country who want our fine products.

I. OUR GOAL IS TO PRESERVE THE SYSTEM WHILE PROVIDING REFORM

Since the repeal of Prohibition, the wine industry has utilized the "three-tier" distribution system of producer to wholesaler to retailer mandated in many states to sell our wines. This is a system which served our industry well and we continue to value the partnerships we have developed with our colleagues over the years. When the number of wine producers was more limited, it was possible for wholesalers to handle the volume of brands and varietals offered for sale. However, the exponential growth in the number of wineries during the last two decades, coupled with the striking consolidation which has occurred within the wholesale tier, have created an environment which no longer allows for full service for all winegrowers and consumers.

In 1963 there were 10,900 distributors and 377 wineries. Today, there are less than 300 distributors and more than 1700 wineries. There are currently over 800 wineries in California alone, each of which produces approximately five different labels each year. That, in itself, is over 4,000 labels per year from California. There is simply no way that wholesalers and retailers in all cities and states can carry all of these wines.

Our attempts are directed at preserving the essentials of the system while providing necessary reforms. When reviewing wine industry statistics, it was found that the 50 largest wineries in the U.S. produce 90 percent of the wine. While the three-tier system is well suited to handle the wines made by these producers, it is not in a position to offer a similar distribution system for the more typical small, family-owned winery. Most wineries produce only a few thousand cases of wine each year (and some varietals in only a few hundred cases) and, therefore, simply do not have the quantities necessary to accommodate the needs of wholesalers.

The desire of consumers throughout the states for these specialty wines has only increased over the years. In the last 20 years, the attention of the media on the remarkable successes of the American wine industry has increased dramatically, with the proliferation of wine and food magazines, wine columns in local and national newspapers, and programs on television and radio. It is now commonplace for consumers in other states to learn about and want to purchase wines that are not available to them in their own states.

Our success has been further enhanced by the fact that the wine industry, in California and in many other states, has become a prime tourist attraction. Out-of-state visitors to our tasting rooms, as well as the tasting rooms in 46 other states, sample these small lots of wine, and want to purchase limited amounts to ship back to their homes, or else place phone orders for the wines upon their return home. Such basic transactions have now been elevated to the level of a felony in states such as Florida, Georgia, Indiana, Kentucky, North Carolina and Tennessee, primarily at the urging of the wholesalers in those states who fear losing possible market share. This year, 11 felony bills have been introduced in state capitals. Those who oppose direct shipments have a motto: "Ship the Wine, Do the Time."

II. SOME STATES HAVE FOUND WAYS TO ACCOMMODATE THEIR CONSUMERS

During the last ten years, 15 states have passed legislation which offer solutions allowing their citizens to have the wines they cannot readily find at home be shipped directly to them. These proposals were at first based on the concept of "reciprocity", which in effect created trade agreements between states allowing limited direct shipments between states enacting such legislation. Recently, Louisiana and New Hampshire enacted new, creative laws establishing a means of registering out-of-state shippers and collecting all tax revenues.

III. UNDERAGE ACCESS IS LIMITED

The opponents of direct shipments continue to raise the issue of underage access. Underage drinking is a serious problem. The Department of Health and Human Services reports that more than one-half of 18-20 year olds consume alcohol every month. However, minors are not purchasing any significant amounts of wine or alcohol by the relatively expensive and slow path of direct shipments, which leaves a clear trail of delivery records and credit card information.

In California, where direct shipment has long been legal, virtually no complaints of underage/illegal deliveries have been made. Artificially created "stings" that garner media attention can illustrate that it is possible for underage persons to obtain alcohol by direct shipment, even in instances when the wholesaler has handled the product and it is subsequently shipped directly from the retailer to consumer. Thirty

(30) states permit such intrastate shipments yet the wholesaler funded “Americans for Responsible Alcohol Access” does not emphasize the issue of underage access for this type of delivery.

The fact is, there is no evidence direct shipment to minors, whether from producer to consumer or retailer to consumer, is a serious problem. State enforcement authorities that have experience with direct shipments do not consider this to be a significant part of the underage drinking problem.

Common Carriers like Federal Express, DHL Worldwide, and United Parcel Service play a pivotal role in the delivery of wine to consumers via direct shipments with special handling taking place.

The wine industry has worked with these common carriers to develop programs that ensure such compliance, and the success rate of these programs has been excellent. In crafting legislation to permit direct shipments, we include language to require that all packages be marked: “Contains Alcohol, Adult Signature (Over 21) Required for Delivery.”

In these states, drivers have been trained as to how to handle packages that have these special delivery requirements. A good example of this is provided in the enclosed correspondence from Jon Olin, Senior Legal Counsel for DHL Airways, Inc. (See attachment #1) This letter was sent in response to a complaint by wine trade journalist Jerry Mead, who was upset that his 55 year old associate was made to show identification before she could sign and take possession of a wine delivery. (See attachment #2)

To further ensure our own Wine Institute members compliance with the shipping laws, we have agreed with Federal Express that any member identified by Federal Express as making an illegal shipment, or who is not marking packages as containing alcohol as outlined above, will be removed from our discount program and prohibited from shipping via Federal Express in the future.

Stings have almost exclusively been done in states where direct interstate shipment is not legal, and where drivers have not been trained on how to handle packages containing alcohol, as they have been in the legal shipping states. In addition, the packages involved in these deliveries have rarely borne the required warnings about special handling.

Common carriers have created a good system of checks upon their systems in the legal shipping states. If direct shipping opponents are truly concerned about deliveries to minors, they should in fact encourage the adoption of the direct shipping model we have passed in the 15 legal shipping states, and thereby ensure that all packages will be marked in such a way—and drivers trained in such a way—as to achieve a much greater system of protections than simply further criminalizing such shipments.

IV. MOST DIRECT SHIPMENTS ARE LEGAL

Opponents of direct shipments cite it as a billion dollar business—an exaggerated figure that cannot be substantiated. The entire market of direct shipments is estimated at less than \$600 million. Contrary to the impression fostered by wholesalers, virtually all of these sales are fully legal, made within the 30 states which permit intrastate shipments and 15 states which additionally permit limited quantities of wine to be shipped directly to their citizens. No direct shipment of wine is sold without full payment of both federal excise tax and state excise tax in the state where legally sold.

As an outgrowth of the Internet Tax Freedom Act, Congress created a commission to examine the means to ensure the fair imposition of consumption, sales and use taxes on business including those using the Internet in remote sales. A group of 35-plus Members from both the House and Senate has requested the Commission include an investigation of unreasonable state barriers which do not allow consumers access to out-of-state wine and remedies for states to collect excise and use taxes. This is where any legitimate revenue concerns should be addressed.

V. USING THE FEDERAL COURT SYSTEM TO REGULATE WINERIES IS NOT NECESSARY

The members of Wine Institute respect the need for states to be able to administer the laws which they have on the books, even as we work to create legislation that is responsive to consumer needs across the country. There already exists a federal remedy for states to enforce their alcohol laws. The Bureau of Alcohol, Tobacco and Firearms (ATF) has informed the states, in Industry Circular 96-3 dated February 11, 1997, that it has jurisdiction over any holder of a Federal Basic Permit (FBP)—a winery, distillery, wholesaler or importer—found to be in violation of a state’s laws. ATF, once notified by a state, will take action. ATF will administer punitive action up to and including suspension or revocation of a license if a FBP-hold-

er is in violation of a state's law. During the last two years, there has been one complaint to ATF which led to the loss of the violator's FBP—and the violator was a wholesaler.

States have other remedies available if they so choose, including pursuing citizens for illegal importation and criminalizing underage solicitation and purchase. And just last week, the Utah Court of Appeals ruled that Utah may prosecute companies that ship alcohol across state lines in violation of state law.

Passage of federal legislation in this area would harm efforts to craft creative state-by-state reforms. It would lock in the status quo and eliminate the incentive of the middle tier to work to find solutions.

VI. CONCLUSION

Our member wineries and I will continue to work with the various states to craft laws so that consumers in all states can have reasonable access to limited amounts of the wines which currently are not readily available to them. In the meantime, we recognize that in order to continue to do business, wineries must comply with the laws of the various states in order to retain their Federal Basic Permits.

There is no need for states to be granted access to the over-burdened federal court system as a second federal venue in which to pursue citizens and small wineries. American consumers want convenience, access and freedom to make their own purchases. America's winegrowers want to fulfill those desires. Local state-sanctioned distributors should not attempt to criminalize practices which in any other industry would be considered free enterprise.

Interstate commerce and burgeoning E-commerce should not be hindered by one segment of the industry, which raises false concerns in order to hamper competition and create barriers to trade. The three-tier system should be augmented on a state-by-state basis in order for consumers to have access to hard-to-find wines. Any federal legislation in this area should be balanced to allow this to happen.

On behalf of the members of Wine Institute, I thank the Committee for this opportunity to express our views.

Subject: **WineTrader/Jerry Mead**
Date: 9/18/98 5:02:30 PM Pacific Daylight Time
From: jclrn@US.DHL.COM (Jon Olin)
To: sjgwine@aol.com (Steve Gross)

Steve:

DHL's response to Mr. Mead:

DHL Worldwide Express has received a copy of your electronic publication dated September 17, 1998, entitled "Latest Shipping Stupidity," which questions DHL's policy to obtain proof of age of the recipient before making a delivery of alcoholic beverages.

After years of providing international transportation of alcoholic beverages, DHL recently commenced its domestic wine shipping service following months of painstaking and detailed analysis of state alcoholic beverage regulation, and after developing guidelines designed to ensure a reliable wine shipping service which is in strict compliance with state laws. DHL currently offers wine shipping services to 16 states and the District of Columbia, pursuant to direct and reciprocal privilege legislation in force in these jurisdictions.

Nevada law, as enforced by the Nevada Department of Taxation, requires delivery companies like DHL to obtain detailed records regarding all interstate deliveries of alcoholic beverages made in Nevada, and to retain those records for four years. DHL must be able to demonstrate during that retention period that such interstate deliveries of alcoholic beverages were made to individuals who are at least 21 years of age. Such a requirement obligates DHL to obtain and record a valid age identification number on the DHL delivery record, regardless of the age of the recipient and regardless of the fact that the recipient appears over twenty-one years of age. This is DHL's unwavering policy, and is intended to protect not only DHL, but our wine producing customers who value the precious rights afforded them, under few states' laws, to sell and ship their products directly to the wine consuming public, like you.

It is ironic that you should hasten to criticize DHL as a provider of responsible interstate wine shipping services, when the rights of consumers (like you) to receive shipments of alcoholic beverages are constantly jeopardized by companies which circumvent alcoholic beverage laws. We are aware that some delivery companies may leave shipments of wine without obtaining a delivery signature, however, it will remain DHL's policy to obtain delivery signatures and to require proof of age from a valid picture I.D., regardless of the age of the recipient. If you are troubled by this policy - though DHL does not countenance violating the law - we suggest you select someone other than DHL to carry your personal wine shipments.

If you have additional questions concerning DHL's alcohol beverage

shipping program, please contact DHL public relations at 650/802-4957.

 Jon E. Olin
 Senior Legal Counsel
 Assistant Secretary
 DHL Airways, Inc.
 333 Twin Dolphin Drive
 Redwood City, CA 94065-1496
 Telephone: (650) 802 4795
 Facsimile: (650) 802 4798
 Email: jolin@US.DHL.COM

THIS MESSAGE IS A PRIVILEGED AND CONFIDENTIAL COMMUNICATION OF COUNSEL

----- Headers -----
 Return-Path: <jolin@US.DHL.COM>
 Received: from ny-zb02.mx.aol.com (ny-zb02.mail.aol.com [172.31.41.2]) by air-zb05.mail.aol.com (v60.5) with SMTP; Fri, 18 Sep 1998 20:02:29 -0400
 Received: from gateway2.dhl.com (lhr246a.dhl.com [196.141.197.246])
 by ny-zb02.mx.aol.com (8.8.8.8.5/AOL-4.0.0)
 with ESMTP id UAA04043 for <sjgwine@aol.com>
 Fri, 18 Sep 1998 20:02:28 -0400 (EDT)
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 by uscmg2.us.dhl.com (8.8.7/8.8.5) with SMTP id QAA17286
 for <sjgwine@aol.com>. Fri, 18 Sep 1998 16:55:45 -0700 (PDT)
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 (DHLGMS 4.07-DSI-test) id AA27704; Fri, 18 Sep 98 17:00:18 -0700
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 Mime-Version: 1.0
 Content-Type: text/enriched; charset="us-ascii"
 Date: Fri, 18 Sep 1998 16:59:39 -0700
 To: Steve Gross <sjgwine@aol.com>
 From: Jon Olin <jolin@US.DHL.COM>
 Subject: WineTrader/Jerry Mead

Subj: **Fwd: LATEST SHIPPING STUPIDITY**
 Date: 9/17/98 11:50:18 AM Pacific Daylight Time
 From: benson@jbwine.com (Jeremy Benson)
 To: sjgwine@aol.com

Steve, FYI. I'm forwarding this from Jerry Mead, just received a minute ago (11:45).
 Jeremy

>XFrom_: WineTrader@aol.com Thu Sep 17 11:31:35 1998
 >>From: bin Thu Sep 17 11:31:35 1998
 >From: WineTrader@aol.com
 >Date: Thu, 17 Sep 1998 14:29:12 EDT
 >To: WineTrader@aol.com, OportoRAH@aol.com, Richard@amwoodwinery.com,
 > janebh@auswin.com, bart.etti@vcs.k12.ca.us, VBatchelor@aol.com,
 > benson@jbwine.com, danberger@rocketmail.com,
 > WINEBOUQUETBLOM@compuserve.com, JBreaw@Sebastiani.com,
 BSIPORT@aol.com,
 > StillmanB@aol.com, LuwWine@aol.com, Bumap@ibm.net, GBursick@aol.com,
 > JCalmeier@aol.com, patrickcambell@compuserve.com, nch@winemag.com,
 > bciffin@sen.state.nv.us, adlerfel@pacbell.net, BrewTomCA@aol.com,
 > Calgrapes@aol.com, jpdore@ix.netcom.com, RDoyle9326@aol.com,
 > jcdjr@draperin.com, reddy@pacific.net, PWFegan@aol.com,
 > UofTexas12@aol.com, FCPRMAVEN@aol.com, Goldhock@aol.com,
 > jgoodnight@youngsmkt.com, GollerJohn@aol.com, Dgwino@aol.com,
 > karylh@nywine.com, Tmb1986@aol.com, hausch@nevada.edu,
 > danlee@monmouth.com, johnhinman@beveragelaw.com, lhodo@goldrush.com,
 > WB6TCA@aol.com, ThomasLee1@aol.com, VINONERO@aol.com
 >Cc: macwine@mcn.org, cmara@computer.net, EdMascian@aol.com,
 geyserp@sonic.net,
 > rads@midusa.net, SeanNDori@aol.com, EtienneM@aol.com,
 > CalWineMan@aol.com, LMirascou@netgate.net, one49er@earthlink.net,
 > EZMoods@ainet.com, mospeak@flash.net, Lmurfisurf@aol.com,
 > AcomEntr@aol.com, wyn@coalitionf.org, Wendyberg@aol.com,
 > Wlperdue@aol.com, Winemaker@aol.com, predwine@mindspring.com,
 > dougrichards@earthlink.net, WrdBeatnk@aol.com, lggywine@aol.com,
 > linda_schneider@hotmail.com, woodangl@ccia.com, DJS20301@aol.com,
 > MStepanovich@csutak.edu, ssteves@airmail.net, TwoTaps@aol.com,
 > stane_terlep@eunet.si, Wrtish@aol.com, Vined@foodsci.purdue.edu,
 > gr8wine@primenet.com, John690561@aol.com, LFTBNK@aol.com,
 > SANDISCAT@aol.com, WWIleox424@aol.com, jackie@wines.com,
 > jernwils@home.com, Walter1ww@aol.com, MARKWONE@aol.com,
 > PSMcCown@aol.com
 >Subject: LATEST SHIPPING STUPIDITY
 >X-Mailer: AOL 4.0 for Windows 95 sub 214
 >
 >DHL has just replaced another shipper as our least favorite. Just received a
 >shipment (a regular happening at a wine scribe's residence) of several
 >bottles
 >of wine via DHL. We're used to some carriers insisting on a signature, even
 >though no one except old people (over 50) live in this house. But DHL takes
 >the prize for lack of common sense. My white-haired 55 year old associate ran
 >downstairs to answer the door for the DHL driver...only to be told that she
 >would have to go back upstairs and get a picture i.d. Now my sweetie is a
 >cutie, and perhaps doesn't look her full 50-plus years, but there is no
 >flipping way anyone, anywhere, is going to think she's an under-21. The DHL
 >driver's response was the infamous, "It's company policy."

>We assume whoever thought up this policy at DHL is about as smart as this
>stupid policy...and when we tried to call DHL public relations for
>comment...got put into the voicemail of some guy on vacation until Oct.
>12... and the person he referred to in an emergency wasn't in. Did I say I
atlc

>hate voicemail?!

>

>The Wine Curmudgeon

>

----- Headers -----
Return-Path: <benson@jwvine.com>
Received: from rly-zb03.mx.aol.com (rly-zb03.mail.aol.com [172.31.41.3]) by air-zb03.mail.aol.com (v50.5) with SMTP; Thu, 17 Sep 1998 14:50:16 -0400
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by rly-zb03.mx.aol.com (8.8.8.8/AOL-4.0.0)
with ESMTP id OAA05130 for <sjgwine@aol.com>;
Thu, 17 Sep 1998 14:50:03 -0400 (EDT)
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by dafy.napanet.net (8.8.8.8) with SMTP id LAA00074
for <sjgwine@aol.com>; Thu, 17 Sep 1998 11:49:47 -0700
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X-Sender: benson@pop.napanet.net
X-Mailer: QUALCOMM Windows Eudora Pro Version 4.0
Date: Thu, 17 Sep 1998 11:47:39 -0700
To: sjgwine@aol.com
From: Jeremy Benson <benson@jwvine.com>
Subject: Fwd: LATEST SHIPPING STUPIDITY
Mime-Version: 1.0
Content-Type: text/plain; charset="us-ascii"

The CHAIRMAN. Mr. Ballard, we will turn to you now.

STATEMENT OF MICHAEL BALLARD

Mr. BALLARD. Mr. Chairman, my name is Michael Ballard. I am proud to be a 1978 graduate of the University of Utah, and am particularly honored by the opportunity to testify before your committee.

My family owns a small California winery in the Santa Cruz Mountains, 1,400 feet above Silicon Valley. Prior to the purchase of the winery, I spent 18 years in Silicon Valley developing various Internet technologies. The small companies I helped to build developed many of the data and telecommunications technologies that led to and today serve as the primary means by which you and most other individuals gain access to the Internet.

The Internet has made consumer access to products and services, and producer access to the broader marketplace, vastly more efficient. As a result, the Internet has shaken many established distribution models across all industries. Wholesalers, who are the distributors or middlemen, have taken notice, and that is why we are here.

The annual U.S. production of wine in this country exceeds 200 million cases. Only 6 percent of all U.S. wineries produce 95 percent of that total. Our product, like that of many smaller wineries, is unique and specialized. Handcrafted from grapes grown on 90-year-old vines, our wines are inherently one of a kind, available only in small quantities. Consumers from all 50 United States seek us out with a desire to purchase our particular product. Our customers are frequently visitors to our property who seek out the product after returning to their home States.

Savannah-Chanel Vineyards adheres to all State and Federal laws in order to retain its Federal basic permit, as issued by the ATF. Where direct shipment to a consumer is prohibited by a given State or county, we obey. Today, in 35 United States, that precludes our customers from receiving our wines.

Prohibiting direct transactions between producers and consumers only results in paralyzing competition and consumer choice. At the heart of the American free enterprise system is the encouragement of small business and affording an even, competitive playing field. It is no secret that the three-tier distribution system is largely unchanged in the last 65 years and provides little value, except to the top 100 wineries.

Some of the objections to direct interstate shipping are based on concern for State collection and the need to control underage delivery. Producers will gladly collect State taxes in accordance with local tax authorities for the freedom to ship legally. In partnership with the major shippers, delivery certification services have been instituted, and development of additional carrier certification programs will continue to guarantee delivery to legalaged individuals.

Federal legislation in this area should represent a balanced approach of controlling undesirable commerce while enabling negotiations on a State-by-State basis to continue in a manner that permits wineries and their customers to conduct business. There are already several effective enforcement techniques that States can utilize. States can prosecute the citizen making the importation

vis-a-vis use tax violations. States can criminalize underage purchases. Dry-area purchases and importation can be criminalized. States can criminalize failure to pay taxes on products imported at a citizen's request. States can regulate the carriers and require them to enforce underage delivery laws.

And as John has said, there already exists a Federal remedy. The Bureau of Alcohol, Tobacco and Firearms has informed the States that it has jurisdiction over any holder of a Federal basic permit. ATF, once notified by the State, will take action, including suspension or revocation of the license, if a Federal basic permit holder is in violation of State law. That, ladies and gentlemen, is the death penalty for any winery owner.

But more importantly, let's open up legal mechanisms. This will allow the best control of any associated risk and greatly reduce violations. Administrators in 15 States which today allow access can testify to the success of these legal mechanisms. Quite frankly, if States can defer to the Federal court system to resolve these matters, our ability to successfully work out intelligent reforms will be severely and unfairly handicapped.

Help us to establish a fair, competitive marketplace for our products by directing the States to look inside their own sandbox for the solution. Protection of the distributors' monopoly position is not a viable solution to this problem. Passage of the bill as written will have a chilling effect on the effort to craft State-by-State solutions to allow consumer access to hard-to-find wines. Fifteen States, including two where the State completely controls sales, have already acted to provide such access. Legal, controlled market access is a well-known, proven solution that must be an alternative option to the closed system imposed by mandated three-tier distribution.

Thank you for your time and consideration of these matters.

The CHAIRMAN. Well, thank you, Mr. Ballard.

I appreciate the testimony of all of you. I am concerned about this issue because I am the last who wants to overregulate or pick on people, but it is a serious issue.

I notice in Congressmen Radanovich and Thompson's statements, or at least I heard this, that they have alleged that Prof. Jesse Choper, from the University of California at Berkeley, has concluded that, "The proposed legislation would violate the Commerce Clause protection against barriers to free trade among the States by allowing States rather than Congress to establish those barriers."

Now, we have a single-page letter from Professor Choper basically saying that. In this particular letter he first asserts that neither Webb-Kenyon nor the 21st amendment authorizes a State to erect discriminatory barriers to interstate commerce. Now, I certainly would not argue that they do. But tell me, Mr. Diamond, if you would, where in the draft bill does it provide that we are conferring upon the States the authority to enact such barriers.

Mr. DIAMOND. Well, I am a little uncertain as to what his objection is. The 21st amendment was clearly, and still is clearly understood to mean that traditional Commerce Clause limitations upon State activity—that is, allegations that the State action violates the dormant Commerce Clause—do not apply. It is true, as I mentioned, that the Supreme Court has said that overt protectionist ac-

tivity, as they found took place in Hawaii where the State imposed a tax on all alcoholic beverages except two produced only in Hawaii, was unconstitutional. But I don't see what the problem is.

The CHAIRMAN. Well, the bill merely allows a State to seek Federal injunctions and forcing compliance with its existing alcohol control laws. That certainly doesn't seem to erect a discriminatory barrier to interstate commerce.

Mr. DIAMOND. No, sir.

The CHAIRMAN. OK; well, he next asserts that the bill, "would dramatically expand the powers of the State to regulate alcoholic beverages." Yet, as I view it, the most powerful example of the State ability to regulate alcoholic beverages is to bring criminal actions in State court. Now, how can a lesser power to civilly enjoin practices which would allow prosecution under its criminal laws be a dramatic expansion of State regulatory power?

Mr. DIAMOND. I agree with you once again. I don't see that.

The CHAIRMAN. He cites the *Bacchus* case for the proposition that the States may not discriminate against interstate commerce. But he fails to mention that the Supreme Court also held in that case that State laws designed to combat the, "perceived evils of an unrestricted traffic in liquor," are entitled to greater deference by the courts.

Now, isn't any regulation of the State which would tend to discriminate against interstate commerce subject to the same challenge in a Federal civil injunctive action as it would be if used in a State proceeding?

Mr. DIAMOND. Well, the only thing that was objected to in *Bacchus* was overt facial discrimination.

The CHAIRMAN. Right.

Mr. DIAMOND. The fact is that everyone understands that a State regulatory system is one that interferes with free trade in the abstract, and as Justice Rehnquist has often said, either because it is trying to cope with preexisting distortions in free trade or because, as is obviously the case with alcoholic beverages, it is pursuing other social good. Again, I don't see what the problem is.

The CHAIRMAN. I don't either.

Mr. Klein, the recent Utah Court of Appeals decision in your case reinstated the criminal action Utah could bring, or instituted against Beer Across America. So in the absence of any further appeals, you can now proceed to trial.

Mr. KLEIN. Yes; we expect the case will be remanded to the trial court and that a hearing date will be set for a preliminary hearing and then trial.

The CHAIRMAN. Well, just one thing. Is the Utah opinion binding on any other State?

Mr. KLEIN. No, it is not, because it reflects an interpretation of Utah law.

The CHAIRMAN. My time is expiring, but I would like to ask you, Mr. DeLuca, a question or two. You point to the legislation that I will introduce as unnecessary, in part you allege because the ATF, the Alcohol, Tobacco and Firearms agency, is on the case and can revoke permits when shipments of alcohol in violation of State laws have occurred.

Now, leaving aside the question of whether the ATF has the resources to effectively police permit holders, is it not true that ATF jurisdiction is limited to wineries and that there is no Federal permit process for retailers and microbreweries who engage in interstate sale of alcohol?

Mr. DELUCA. The Federal basic permit applies to wineries, applies to wholesalers, to importers. They do not have the Federal permit jurisdiction over retailers and brewers. I am obviously addressing the issue in terms of the fact that the wineries are the ones that I represent.

The CHAIRMAN. That could be hurt here.

Mr. DELUCA. At the same time, there has been a case brought to the ATF. As I understand it, they investigated and they did bring action, and in this case it happened to be with a wholesaler. We are talking about a very big part of this issue, the wholesaler community and the wine community. But I do acknowledge what you have just said that the basic permit jurisdiction of ATF extends to us, but it does not extend to retailers and brewers.

The CHAIRMAN. Well, I am just going to ask one other question of you before I turn to Senator Feinstein because your testimony is particularly important here, of course, as is all the other testimony. I want to give you every opportunity.

You have stated in your testimony that, "minors are not purchasing any significant amounts of wine or alcohol by the relatively expensive and slow path of direct shipments." Of course, the first question that comes to mind is what is a, "significant amount of wine or alcohol." Some would argue that even one sale to a minor, potentially devastating to that minor should he or she drink and drive or imbibe to unconsciousness, is more than enough. We have Brendan's testimony about what he faced when he overindulged in alcoholic beverages.

But more importantly, how does the industry know minors are not purchasing, "significant amounts?" Certainly, a successful sale to a minor is not going to be reported by the minor.

Mr. DELUCA. May I answer it in two parts?

The CHAIRMAN. Sure.

Mr. DELUCA. First, the context that you are discussing is obviously very important, and the whole issue of what do you do about underage drinking and binge drinking is clearly of paramount importance to us. Our code of advertising, how we promote, how we educate, our emphasis on wine with food—I mean, these are addressed across larger issues than the narrow one that we are focusing on now. And as I said, we make common cause with the whole issue of how to address this with regard to underage drinking.

With regard to the Internet or direct sales and direct shipments, I think common sense prevails here. Most of the wineries are like Mr. Ballard's, hard-to-find wines, wines that are expensive, wines that are touted in magazines by journalists across the country. We have witnessed an extraordinary renaissance in tourism, people who can't find their products at home. If they were able to find it at home, they would buy it there; can't, so they write directly to the winery.

These wines are expensive. Those that are not expensive can easily be found throughout the distribution system that we have

today, through your normal wholesale-retailers. But we are talking about products that are either library editions or literally you cannot find in your own local market. I have been there at wineries when tourists have said, why aren't you interested in my business? I like your wine. Why isn't it back at home? And they find out that it isn't we who don't want to give it to them; it is just not available in their own commerce.

You need to have credit cards. Look at the trail that you leave if you are thinking of breaking the law. You can easily find on the Internet the order or the credit card that is being used. It is time-consuming, versus going down and finding it right there at your corner liquor store. So, in truth, that is one part of the answer.

The other one is we do have experience in California of almost 50 years intrastate. We are a big State, cover a lot of territory. We have been doing this for a long, long time, and the people who are policing this, as Congressman Radanovich and Congressman Thompson pointed out, have said in public testimony that it is a minor issue. It is serious for the people involved, but when you are looking at the totality of the underage issue, it is minor.

So focus on underage drinking; we are right there with you. On that point, we are with you. The moment you start talking about underage abuses through direct shipments, you are talking about a relatively smaller issue. But this is not to negate the question and the sympathy that is obviously there for us on the question of underage drinking.

The CHAIRMAN. Well, thank you.

Senator FEINSTEIN, we will turn to you.

Senator FEINSTEIN. Thank you very much, Mr. Chairman.

First of all, Brendan, congratulations to you and to the organization you represent. I am a big fan and supporter of MADD, and it is the first time I have seen a young person testify, and I just want you to know you did it very well and you made a very strong point.

Mr. Chairman, I have known the California Wine Institute well. I have known John DeLuca now for over 30 years, and know that he speaks the absolute truth. What has happened in California is you now have 800 wineries. They are in 45 of the 58 counties, and what has developed is a real competition in the sense of developing wines that are very specialized. If you have 800 wineries, you don't have room on shelves for 800 different products. So these wineries increasingly have the Internet as, some of them, their only source of sales. Ten million people a year visit these wineries, go through wine-tastings. They make purchases, et cetera.

I have been very proud of this industry because as it has grown, I think Congressmen Thompson and Radanovich said they employ 200,000 people on a regular basis. My figures are 112,000 people on a regular basis, and 50,000 parttimers. It has become a huge industry, but it has an increasingly boutique kind of nature—specialized wines, if you like an okie wine, if you like a fruity wine, even differences in chardonnays, and particularly in the varietal wines. It is, I believe, today the best wine produced in the world. And the smallness of the wineries, a part of what is driving this—they are very concerned that your legislation would have a real chilling effect on what they are doing.

I guess what I would like to say, rather than ask questions, is what Brendan pointed out is right. I don't know that he got what he drank when he went out—I suspect it was something that was bought at the corner store. And even in Virginia, our statistics indicate that enforcement along these lines is where the greatest weak point is; also, very much aware of the fact that there is a kind of three-tier approach here, and a lot of the support for the legislation comes from the very people that don't want to see the growth in Internet-type sales of this product, the wholesalers, for example. So I think there is a fine balance here.

I am a cosponsor with Senator Kyl on his legislation on Internet gambling, and I must tell you that I see some shades of difference there. So I would just hope that you would work with the Wine Institute. I am here to vouch for them as one of the most responsible representatives of an industry that I know of, and we are just extraordinarily proud of what has been developing in California.

The CHAIRMAN. Well, thank you, Senator Feinstein. I have a high regard for every Senator on this committee, but certainly Senator Feinstein fights very strongly for her State. You seem to know an awful lot about wine. I know absolutely nothing, to be honest with you.

Mr. DELUCA. Come visit us.

The CHAIRMAN. I am afraid to. [Laughter.]

A poor Mormon boy like myself, I would be in real trouble, I will tell you.

But I do want to be fair to you. We want to solve a problem without hurting your industry. It is a legitimate industry, and most people I know take a great deal of pain to understand their wines and enjoy them very much. So we will be happy to have your suggestions. We will be happy to listen.

We file these bills so that we can get comments, but if we can prevent deaths like Brendan almost suffered—and your testimony is very dramatic here today. I mean, I feel like what a wonderful young man you are to have gone through those things and now, having become an Eagle Scout at age 13 and now working with Mothers Against Drunk Driving and being used as somebody who can articulate some of their positions. I really think it is wonderful.

So we will keep an open mind, and we would like you to look at this and see if there is some better way of solving these problems because we think the problem is more pervasive, Mr. DeLuca, than you do. We have some indications that it is; we will put it that way. And, naturally, we want to protect as much as we can our young people from these type of—

Mr. DELUCA. Senator, will you permit me an auxiliary remark?

The CHAIRMAN. Sure.

Mr. DELUCA. Mothers Against Drunk Driving was started in Sacramento, CA, by Candy Leightner.

The CHAIRMAN. Right.

Mr. DELUCA. And in the early days when she was getting started, she came to see me and enlisted our support. And we were one of the earliest supporters of Mothers Against Drunk Driving. In fact, I held a wine-tasting at one of the events to try to promote interest in the subject matter as a way of showing that there was no ideological or theoretical or any practical reason for us not to

support that effort. It is an extraordinarily important development, how they have been able to impact the laws across the country.

And as I said, we will make common cause with anyone who wants to address the issue societally, and that is where we part company with you, is only on the specifics of your bill, but not in terms of the thrust of what you are talking about.

The CHAIRMAN. Well, let's talk in terms of how we do this. I want to be fair to people, certainly to your industry. There are a lot of decent, wonderful, honorable people in your industry. And, of course, it is a tremendous part of the commerce of not only California, but many of the other States as well.

I think that what we will do is we will keep an open mind and file the bill, and then you look at it and see how we can improve it or what we can do to resolve these problems. I will be happy to listen. I will be happy to do whatever we can to resolve them in a manner that really is fair to everybody concerned. But we are concerned about our young people in this society and there is no doubt in my mind that they are using credit cards to acquire alcoholic beverages of all kinds.

And we don't mean to center on the wine industry here today. They are getting beer and they are getting, harder substances, alcoholic beverages, that they really shouldn't be getting under these laws, and they shouldn't be abusing. So help us to know how to do it, and I will be happy to keep an open door to you and we will see what we can do to get this done the right way.

Mr. DELUCA. Thank you, Senator.

The CHAIRMAN. All right.

Senator FEINSTEIN. Mr. Chairman, may I make a small suggestion? The key may well rest in tightening verification in some way of the age of the purchaser through the Internet. Now, I don't know how that can be done, but it seems to me to be the logical safeguard there and I would just add that.

Mr. Chairman, may I ask that certain articles be entered into the record?

The CHAIRMAN. Without objection.

[The articles referred to follow:]

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REVIEW & OUTLOOK

Booze Busters

Anyone thinking the reservoir of creativity in this land is running a little low hasn't tried ordering a case of hearty zinfandel across state lines. There's just nothing like protectionism to energize the bureaucratic brain in the service of special interests and political gain. Turning vintners into felons is their latest triumph.

Smaller vineyards have often sold a percentage of their wines over the phone the way J. Crew ships sweaters. Even states with restrictions on direct wine shipments (which skip wholesalers, distributors and retail liquor outlets), didn't actively enforce them. That's no longer true. The way things are going, Saudi Arabia is only a few steps ahead. Kentucky, Georgia and Florida have all passed laws making direct shipping of even a single bottle of Chardonnay a third-degree felony punishable with fines up to \$2,000 and jail time (public whipping is not yet an option).

Microbrewers are also under siege. Just now, the *State of Utah v. Beer Across America Inc.*, is before a judge in Salt Lake City. Some of the club's beer ended up shipped to a thirsty customer in Utah, which happens to be in America though we are left wondering: Didn't the 21st Amendment repeal prohibition?

That's part of the story. In the 21st Amendment's comma-cluttered language many a state regulator has found happy refuge. "The transportation or importation into any State, Territory, or possession of the United States for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited." In 1933, of course, liquor meant booze, the American wine industry was in its infancy, and the greater purpose of the amendment was to keep alcohol out of the control of a single entity like the Mafia. It set up a three-tier system of producers, distributors and retailers. Over the years, they've come to be represented by a very powerful liquor lobby, which is leading the attack on the smaller vintners, afraid of losing turf to pinot noir.

Did the amendment intend to carve out an exception to the Constitution's commerce clause, the essential lubri-

cant of interstate trade? Courts are increasingly rejecting that argument, ruling that the 21st Amendment is trumped by the commerce clause in typical confrontations, a view recently taken by a Tallahassee judge.

None of this mattered much anyway until jug-wine enthusiasts became increasingly sophisticated connoisseurs of wine and practiced users of the Internet and mail order catalogues. Of course nothing changes in the world of regulators keen to officiate over the whole range of human experience. Wholesalers have very successfully raised harrowing visions of minors receiving crates of mail-order merlot. No doubt that's what teens do. They make credit card purchases of rare vintages from obscure wineries thousands of miles away and then wait for three days so they can go binge with their pals.

There is a reason for the mail-order wine business. Oregon, for example, now has more than 116 vineyards; California around 900, typically producing five to eight different kinds of wine. Distributors have no room on their trucks for most of them and neither does your local liquor store. Measured in terms of sku, or cost per shop-keeping unit, the profit per item just isn't enough for the bother when you've got vats of Blue Nun to move.

Already the crackdown has done great harm to smaller vintners. Matanzas Creek Winery in Sonoma County, for instance, estimates it is turning away around \$3,000 a month in direct sales from consumers who had visited the winery and now hoped to place orders. Virtual Vineyards, an Internet provider, has wearily installed software blockers that identify callers from felony states.

Louisiana just came up with an adult compromise that permits direct shipping of a limited quantity of wine per year, arranges for child proof labels and the payment of taxes. But elsewhere, the trend for increased policing seems well under way with Maine just repealing a reciprocity law. As of now, nearly half the states prohibit any direct shipping of wine to consumers. What's next? Green cards for workers who use the interstate highways?

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DOW JONES

Today's debate: MAIL-ORDER ALCOHOL

Wine by mail? Why not?

OUR VIEW Laws that prohibit selling alcohol by Internet, mail and phone stifle competition, cut consumer choices.

Remember that delightful small-winery chardonnay you discovered on a California vacation? Intrigued by an offer of far-off microbrews by mail? Sorry, but a cabal of local interests is working to make sure you can't get any delivered to your home.

From clothing to computers, from books to begonias, consumers increasingly are using the mail, phone and Internet to order all kinds of goods. It's a \$630 billion business, up almost 40% in five years. But entrenched alcohol wholesalers are applying their clout with legislatures and their alliance with state tax collectors to stop mail-order sales of boutique wines and beers.

Using alcohol's unique legal status as a both a sword and a shield, they're pushing to make such competition a felony — a form of economic protectionism that clothiers, electronics stores and nurseries can only dream of. So far they've succeeded in Kentucky, Georgia and Florida. Lesser punishments apply in 20 other states, but felony laws are being pushed in 14 states.

The Constitution says the states can't interfere with interstate commerce. But the 21st Amendment, ending Prohibition 64 years ago, created an exception for "intoxicating liquors." At the time, it was political-

ly necessary. Some states wished to continue to bar alcohol; others wanted the right to regulate sales tightly or to permit local option by county or municipality. Repeal might not have been ratified without it.

The result is a network of state-licensed distributors (in some cases, the state itself) controlling what wines, beers and spirits are available on retail shelves — and keeping all others out. It's also an easy way of collecting excise taxes on alcohol, so state tax departments eagerly front for the industry when it seeks to block newcomers that want to sell direct to consumers.

Defenders of the status quo also throw up dust about underage purchases, but not many teen-age drinkers are likely to be lured by the premium prices charged by the mail-order industry. Anecdotes of teen buyers have been exposed as state- or industry-engineered stings.

Small-volume California wineries that can't hope to crack the distribution cartels in far-off states say they'd be happy to remit state taxes if they were just allowed to respond legally to orders like any other business. Louisiana has even set up a system for wineries to register for a \$100 annual fee, pay state taxes and ship up to 60 bottles a year to residents who are over 21.

It's an experiment others might follow. Instead of protecting the profits of a few politically connected wholesalers, states should be exploring ways to expand the choices available to consumers.

Stop these bootleggers

OPPOSING VIEW States control alcohol distribution for many good reasons, including protecting kids.

By Douglas W. Metz

Americans can choose among more brands, flavors and sizes of wine, spirits and beer than for any other consumer item. Internet technology has broadened consumer choice and marketing opportunities even further, which is good for the alcohol beverage industry and the adult consumer.

These choices, however, must be balanced against a conflicting public demand for strict control of the distribution and sale of these popular products. States therefore license, closely regulate and heavily tax alcohol beverage distributors and sellers. Many deny licenses to felons, tax evaders and those who regularly sell to minors.

Is the public better served by proposals that amount to allowing anyone with a United Parcel Service account to sell licensed beverages? Unquestionably not. It is unwise to dismantle a system of easily traced responsibility, which is the basis of alcohol beverage control. With direct shipping to consumers, states cannot control sales to minors or "dry" areas and cannot detect, much less catch, tax scofflaws.

These shippers do not limit themselves

to expensive wines. The current controversy began when an underage Kentucky youth ordered easily available wine, beer and spirits from an out-of-state retailer. This white-collar bootlegging is a billion-dollar business that is untaxed, unregulated and growing.

In response, several states have made illegal direct shipping a felony. In Congress, Rep. Robert Ehrlich, R-Md., has introduced a bill which would give states access to U.S. courts to pursue offenders.

Louisiana, unfortunately, recently adopted a naive and ineffective law which trusts these bootleggers to obtain permits, limit sales to five cases per person per year, and pay taxes. Other states with similar requirements report widespread violations.

Legal ways are in place today on the Internet that allow consumers to legally order beverage alcohol. Direct-shipping wineries and retailers have refused in most cases to use them. They also reject sincere distribution offers from licensed wholesalers.

This rebuff was an economic decision. Rather than work within state laws, they chose to gain a price advantage by avoiding tax payments, regulation and license fees.

Let's not put young people, billions of dollars of tax revenue and orderly regulation at risk in the name of "choice."

Douglas W. Metz is managing director of Wine and Spirits Wholesalers of America.

The CHAIRMAN. I will enter some statements in the record, a statement from Jack Lynch, who is with the University of Baltimore School of Law; Simon Siegl, the president of the American Vintners Association; a letter from Jesse Choper, who is from the University of California School of Law; and then one—let's see; this one is from Jeremy Benson, executive director of Free the Grapes, an organization to ensure consumer access to fine wine.

[The statements referred to are located in the appendix.]

The CHAIRMAN. Now, let me just also note for the record that Professor Choper has, in response to my inquiry, informed us that he has been retained by the American Vintners Association. Now, this, of course, was not made clear in his letter to the committee. And in all honesty, I really don't, I have respect for Mr. Choper, but I don't see his point. Constitutionally, I think he is way off base. In fact, I don't think; I know he is way off base.

And I think what we have got to do here is make sure that we always get the very best constitutional authorities and the best constitutional opinions that we can. Mr. Diamond, I certainly agree with you in your interpretations here today, and in your statement of the law for the record.

But be that as it may, this has been an effective hearing for me. I have listened very carefully and I certainly want to be fair to the wine industry, and really to all of the alcoholic beverage industries. But I also want to be fair to our children and our young people in this society, who really should not have access to these things. As you know, the Internet has opened up all kinds of difficulties for us, and we have got to approach these difficulties in intelligent ways and we intend to do so. To the end, I want to thank each of you for appearing today because I think you have been very helpful to us. Thanks so much. It is great to see you.

With that, we will recess until further notice.

[Whereupon, at 11:28 a.m., the committee was adjourned.]

A P P E N D I X

QUESTIONS AND ANSWERS

RESPONSES OF WAYNE KLEIN TO QUESTIONS FROM SENATOR HATCH

Question 1. Many small wineries have argued that the current three-tier system shuts them out and their efforts to introduce their product into potentially lucrative markets are being stifled. They also claim that the costs of participation in the system would be passed on to the consumer making their products less affordable, and thus less marketable. These are certainly valid concerns. But to what extent do such economic factors justify contravention of State laws regulating the sale of alcohol as are appropriate under the Twenty-First Amendment?

Answer. The profit motives of alcohol marketers do not justify violating state laws. Similarly, desires by alcohol producers to collect the full markup between the cost of production and retail prices also do not warrant changing longstanding laws regulating the sale of alcohol.

Policy Choices/Enforcement. It is important to separate two distinct concepts implicit in this question; the arguments about what governmental policy should exist and the question of enforcement of valid laws that are on the books.

If changes were made to state laws, the availability of alcohol to consumers in various states might expand (including the availability of alcohol to minors). The costs of that alcohol to consumers might be reduced.¹ If it is the policy goal of government to reduce the costs and to increase the availability of alcohol to citizens, laws will need to be changed to accomplish this goal. However, this just begs the question of what the governmental policy should be and who should set the policy regarding alcohol access—the federal government or state governments.

The Twenty-First Amendment specifically conditioned repeal of Prohibition on granting to the states the ability to control the sale and distribution of alcohol within a state's borders. Pursuant to the authority of the Twenty-First Amendment and the Tenth Amendment, the states have exercised their police powers over the sale of alcohol. In the exercise of these police powers states have chosen to impose high taxes on alcohol, restrict the availability of alcohol, and limit the manner of sales. Every state has restrictions of these types.

To change these policy decisions requires that existing police powers be taken from the states. To do so requires a constitutional amendment to strip these powers from the states. If that is done, Congress then would obtain the power to dictate to the states that they could not restrict or control the sale or transport of alcohol in the states and could not impose special taxes on its sale.

Unless policy authority is taken from the states, then state laws regulating or controlling the sale of alcohol are valid. So long as those valid laws exist, enforcement officials are permitted—indeed, obligated—to enforce those laws.

In sum, the complaints asserted by wineries go to policy decisions of state legislatures, not to law enforcers. The arguments for change should be addressed either to state lawmakers or in support of a constitutional change. The language of S. 577, by contrast, specifically avoids having the federal government express a policy preference in this area. The bill is narrowly targeted at removing artificial barriers to effects by state officials to enforce valid state laws.

Costs, Availability of Alcohol. The current distribution system for alcohol does not necessarily increase the retail costs for alcohol or reduce the availability of products

¹As noted below, if distribution costs were lowered for alcohol producers, such as wineries, it is by no means certain that the savings would be passed on to consumers.

to consumers, beyond what would exist in a commercial setting. In some control states, including Utah, the state is not only the wholesalers, but also the retailer. Thus, Utah is a two-tier state, not a three-tier state. This enables the states to reduce the costs of a multiple-tier system. As a consequence, even if state law were usurped, a commercial distribution and retail system might very well result in retail prices higher than found in the state system. There are no assurances of lower prices.

Wine clubs or other distribution systems currently being offered to consumers do not necessarily represent a lower cost structure. A wine club becomes a distribution tier. Whether the sales are made through retailers or through a wine club, that level of distribution will incur costs and markups in price. Distribution systems such as this do not necessarily reduce costs as compared to the current systems. Wine club prices generally equal or exceed the shelf prices at Utah state liquor stores—before the wine club adds its separate shipping fee.

The assertions of increased costs under the state systems or the claims of limited availability may well be a “red herring.” Regulators suspect that even if alcohol producers could sell their product to consumers at a lower price, they would not do so. The small wineries or other producers who market and ship directly to consumers are *not* selling to those consumers at below market prices. Any savings from elimination of different levels of distribution are not passed on to consumers. The money saved is retained as extra profits. The wineries relish the possibility of collecting a retail price for their products rather than a wholesale price. Faced with the prospect of collecting a much larger margin on sales than through other distribution methods, the wineries are charging full retail price, plus shipping, and keeping the higher margin of profits. If the goal of shippers were to make their products more available to consumers and at a lower price than through the retail system, direct sales would be significantly cheaper than the prices at which the same products are sold at retail. However, this is not what is occurring.

The availability of alcohol also may not be improved by alternative systems. The Utah Department of Alcohol Beverage Control (DABC) has a policy permitting consumers to make special orders. Any product desired by a consumer will be ordered for that consumer on request.² In these instances, the prices offered to consumers is almost always less than the retail price and shipping costs consumers pay through wine or beer clubs. In such cases, the price is lower and the demand is consumer driven, not supply driven.

Utah requires no fees whatsoever for a winery to be set up with the Utah DABC as a vendor/supplier. The DABC does apply a fixed markup and tax structure to any product supplied for resale. This is what many mail order suppliers want to keep for themselves.

Another point to be remembered with alcohol availability is that not all products are readily available for purchase. Some California wineries already are selling all their output to consumers in California and to consumers located in reciprocal states. They simply do not have excess capacity to sell to buyers in other states, whether or not those states are willing to permit the product to be sold. For consumers in other states, the product simply is unavailable. This unavailability should not be the cause of criticism of state regulators or the state-control system.

Question 2. It has been argued that States can address all their concerns by simply enacting legislation permitting direct shipments with certain restrictions. Such legislation would require licensing by the State and would result in effective State control and ensure the receipt of appropriate tax revenue for those direct sales. Would the enactment of State laws permitting direct shipment of alcohol solve all the state problems and vitiate the need for federal legislation on this area?

Answer. No. This approach is neither good public policy nor an effective solution.

False Premise. This question presupposes a false premise. Yes, states could address the concerns of wineries and alcohol producers—if the states felt that the approach suggested by alcohol producers was good policy for the state. The false premise exists because it assumes that the states have adopted their various regulatory systems out of ignorance or incompetence rather than as a deliberate policy choice. Indeed, when states have adopted the industry-recommended approach, the results have been unsatisfactory.

²The state will special order other products only where the consumer is willing to purchase the entire amount of any minimum amount of a special order. If, for example, a winery is willing to sell its product only in cases of six bottles, the consumer must be willing to purchase the entire order. The winery must be willing to sell its product to the state liquor store. In some cases, such as the Stony Hill Winery, the producer sells products only at retail. There is no wholesale price. After the state's markup, the final price to consumers is very high because the winery is unwilling to provide the product at wholesale.

It is my understanding that all states do have procedures to permit out-of-state companies to sell alcohol in the state. The complaint seems to be that the procedures available are not the ones preferred by alcohol marketers. However, these are the procedures that are being followed by in-state companies and by out-of-state companies that have chosen to comply with the law.

It would be unwise for the states to adopt a policy of not requiring out-of-state companies to comply with laws applicable to in-state producers. To do so would penalize those companies that are located in the state, encouraging them to move their operations to another state. It certainly would not be fair to exempt out-of-state producers from compliance with state laws, but still impose taxes and restrictions on in-state companies. No advantage should be given to out-of-state companies that disadvantages in-state companies or those who are willing to comply with the law. If some California wineries satisfy the requirements to sell in a particular state—and demonstrate that compliance is feasible—why should other wineries not be expected to do the same?

Compliance with the law is possible. While there may be costs involved in complying with state laws, it can be done. I commend the many companies that do comply with state laws. There are commercial enterprises and technological advances that facilitate this process. The Internet, for example can be an affective and efficient means of understanding and complying with the laws of each state, instead of being used as a means of facilitating violations of the law.

The pernicious notion that states can (they really mean “should”) address producers’ concerns about difficulties in selling their products in certain states by changing their laws to no longer restrict those products is akin to having promoters of gambling or prostitution—which are legal in some areas—insist that other states change their laws to facilitate the export of these products to all states.

When States do Permit Direct Shipments, Alcohol Sellers Still are Not Complying with the Laws. Evidence that the states’ concerns are not alleviated by the passage of legislation permitting direct shipments is shown by the experience of states that do permit direct shipments. It is my understanding that at the National Alcohol Beverage Control Association (NABCA) *Symposium on Alcohol Beverage Law*, held in March, 1999, a representative of the New Hampshire State Liquor Commission reported that the New Hampshire law permitting direct sales to retailers and consumers has been met with very limited use. Since the law went into effect on July 1, 1998, only 14 permits have been purchased. Taxes of \$373 have been collected, reflecting very low levels of retail sales. This indicates that alcohol sellers are not utilizing the straight-forward compliance procedures provided by the law. The vast majority of direct sellers continue to sell alcohol to New Hampshire residents without taking the effort or paying the licensing fees to comply with the law.

While the state of New Hampshire created a mechanism for relatively simple compliance, the mechanism is not being used. The suspicion is that alcohol shippers do not want to submit to any regulatory oversight or are unwilling to pay any taxes or licensing fees.

The much-anticipated experience of Louisiana, the other state permitting direct sales by companies that register with the state, has been similar. A permit is required in order to ship alcohol directly to purchasers. A fee of \$150 is charged to manufacturers and \$1,500 to out-of-state retailers such as wine or beer clubs, or retail marketers. To date, the state has collected a mere \$7,000 in licensing fees—fewer than 50 out-of-state vendors. Again, this indicates that enacting legislation to permit direct shipments (with certain restrictions) is not a successful approach since few shippers are willing to comply the law.

RESPONSES OF WAYNE KLEIN TO QUESTIONS FROM SENATOR GRASSLEY

Question 1. Several of you have indicated that the ATF has regulations on alcohol sales. Has the ATF issued regulations or guidance on this issue of the direct selling of alcohol across state lines?

Answer. Yes. On February 11, 1997, the Bureau of Alcohol, Tobacco and Firearms (BATF) issued Industry circular 96-3, which noted that compliance with the Webb-Kenyon Act is a condition for the maintenance of the federal basic permit issued by the agency. Without a basic permit, a company is not eligible to engage in the distribution or sale of alcohol beverages. However, RATF is prohibited by law from regulating brewers or retailers, so 96-3 is of limited application. The BATF can take no action against brewers or against wine or beer clubs (as retailers).

Industry Circular 96-3, however, states that BATF will respond to a request for state assistance only where a written determination has been made by the state regulatory agency or Attorney General that the conduct at issue violates state law, and

where the *BATF* has independently determined that the conduct has some “pronounced impact” on the state regulatory or enforcement scheme.

A copy of Industry Circular 96-3 is attached. *BATF* has taken no enforcement action relating to direct shipping against any holders of permits since the issuance of the circular. State regulators report that *BATF* devotes little of its resources to alcohol (one estimate is less than 10 percent). Instead, *BATF* focuses on collecting fees and is reluctant to bring enforcement actions. At the 1999 NABCA Symposium, a *BATF* official stated that the Department of Treasury (of which *BATF* is a unit) has not taken a position on direct shipping in the past. It recognizes the issues of violations of state laws and minor sales but is taking a cautious approach as it tries to learn more about the issue.

Question 2. Mr. Klein, your testimony indicates that you are prosecuting an Illinois company for illegal shipments of alcohol into Utah. You also mention that the state of Utah had warned the defendant in your case to stop shipping alcohol into your state. Could you elaborate on how the defendant was warned and whether the defendant responded to this warning in some way?

Answer. Yes, the defendants in our case were advised that their conduct violated the law and were requested to cease shipments. It was only after shipments continued six months later (over a hundred cases per month) that the state determined to bring a criminal prosecution.

The Affidavit of Probable Cause, accompanying the criminal charges provides the background of this warning:

9. On or about April 19, 1996, a representative from UPS, Loss Prevention, reported that UPS had in its possession several cases of beer (each case containing twelve bottles) which were shipped from BAA [Beer Across America] to residents within the State of Utah. Sgt. Braegger, Utah Division of Investigations (“UDI”), contacted Amoroso [Louis Amoroso, President of Beer Across America] on this same day and advised him that BAA was illegally importing alcoholic beverages into the State of Utah. Amoroso was also told at this time that Utah law required BAA to obtain an appropriate license, that all shipments must be sent through the Utah Department of Alcoholic Beverages, and that if shipments continued without the appropriate license, the product would be seized and legal action taken. Sgt. Braegger was then immediately contacted by Morton Siegel who identified himself as the attorney for BAA. After a discussion of the laws of the State of Utah and the expressed intent of UDI to enforce the alcoholic beverage laws, Mr. Siegel advised that BAA would cease imports into the State of Utah and the expressed intent of UDI to enforce the alcoholic beverage laws, Mr. Siegel advised that BAA would cease imports into the State of Utah until legal arrangements could be made with the Utah Department of Alcohol Beverages.

10. Upon checking with Earl Dorius, Utah Department of Alcoholic Beverages, I [the affiant, UDI agent Evan Terry] was advised that BAA had not filed for nor received a license from the State of Utah for the import of any alcoholic beverage before April 19, 1996. Subsequent to that time, BAA has never filed for or received a license.

11. In my contacts with numerous customers within the State of Utah, I was advised that in many instances after April 19, 1996, BAA advised the customers that BAA could not ship into Salt Lake City, but encouraged customers to list a shipping address outside of the city. In addition, upon reviewing printed materials for BAA, I have noted that these materials contain information stating that BAA will refuse orders and will not ship into certain states because of legal requirements. The State of Utah is not on this list.

The records of seized shipments bear out that BAA encouraged customers to list false addresses. A review of 244 invoices from shipments from BAA to Utah residents in October and November 1996 shows that 33 of them (or 13.5 percent) listed an out-of-state address for billing, but a Utah address for shipment.

In addition to warnings by Sgt. Braegger, Lt. Mitch Ingersoll of UDI spoke with Mr. Siegel on two occasions during this period. Lt. Ingersoll explained the operation of Utah’s liquor laws and Utah’s intent to prosecute if shipments continued. Mr. Siegel told Mr. Ingersoll that he refused to advise his client (BAA) to stop shipping into Utah.

Question 3. From the written testimony, I get the impression that direct sellers of alcohol use common carriers like “UPS” or “FEDEX” to deliver the alcohol to customers. Are there any laws on the books to go after the carriers who transport alco-

hol into a state in violation of state law on behalf of direct seller[s] of alcohol? If not, should there be such laws?

Answer. There is a Utah statute that prohibits carriers from transporting alcohol in a state in violation of state laws. Utah Code Ann. § 32A-12-504 provides:

It is unlawful for any motor carrier, or any officer, agent, or employee of a motor carrier, or any other person, to order or purchase any alcoholic product or to cause any alcoholic product to be shipped, carried, or transported into this state, or from one place to another within this state, when the alcoholic product is intended by any interested person to be received, possessed, sold, or in any manner used, either in the original package or otherwise, in violation of the laws of this state.

I believe that many, if not most, states have similar laws. There are good arguments in favor of, and against, strictly enforcing such laws. There is an initial question of fairness in enforcing laws such as this against *innocent* shippers. Since some shippers (and perhaps the majority) do not label the packages as containing alcohol and do not completely identify the source of the package as an alcohol shipper, it is possible that shippers can be transporting alcohol without knowing the contents of the package. The state must determine whether it is fair to punish them?

A further complication is that some manufacturers have alcohol products packaged and introduced into the shipping process by other companies. This further disguises the contents, sometimes resulting in the alcohol being described as glassware or fruit juices.

On the other hand, practical considerations indicates that it might not be unfair to impose such requirements, if the shipper knows the contents of the packages. In many cases, the same company picks up the alcohol from the warehouse of the alcohol producer and then distributes the packages through its network to the ultimate destinations. Thus, while the delivery driver at the destination may not know what is in the package, the company knows very well that the alcohol was picked up from an alcohol seller and that it was destined for delivery in various states. Indeed, UPS representatives told me that in many cases, companies that do a significant amount of shipping prepare the delivery documents using computers and computer programs provided by UPS. In other words, UPS easily can know whether it is shipping alcohol. FEDEX and UPS say they have corporate policies against transporting alcohol into states where it is illegal, but they also do not ask what is in packages picked up from wineries. In such cases, the carrier can be considered to be aiding and abetting the alcohol marketer in selling its alcohol products into states where the sales are illegal.

Unfortunately, there may be significant limitations on the ability of states to regulate common carriers who are delivering alcohol to consumers in the various states. It is my understanding that the Airline Deregulation Act, and perhaps other statutes, prohibit the states from imposing rules or regulations on federally-regulated air carriers. I believe that FEDEX is such a carrier. States may be unable to impose restrictions on interstate shipments because of the Constitution's Commerce Clause without express permission from Congress.

As to whether there should be laws prohibiting carriers from transporting alcohol, it is my opinion that this is a decision that should be made by the various states as part of their regulatory structure for alcohol control. But, if a state desires to restrict the transport of alcohol, Congress should assist that state by removing the ability of violators to claim immunity from enforcement because of the Commerce Clause. Importantly, S. 577, would permit the Attorney General to bring enforcement actions against carriers as well as alcohol producers—so long as the conduct violates state law. It is left to the individual state to (a) determine whether to make transportation unlawful, and (b) decide whether the facts of a particular case justify initiation of an enforcement action. This bill will help those states who choose to go after carriers who are aiding in the illegal conduct.

Question 4. One of the major arguments used against the direct sale of alcohol is that states into which alcohol is shipped will miss out on sales tax revenue. Are any of the witnesses aware of whether the internet tax commission is looking at this issue or has made any pronouncements on this issue?

Answer. I do not know whether the Internet tax commission is examining this issue. There have been no pronouncements as yet. The commission likely will examine this issue only within the broader context of sales taxes being collected on all types of remote selling.

However, it is important to keep in mind that the sale of alcohol involves more than just the collection of sales tax. Alcohol production and sales are subject to excise taxes and the collection of fees on producers, distributors, and retailers as part of the regulatory process. These alcohol-specific taxes serve a distinctly different

function than sales tax. Sales taxes generally are designed as pure revenue sources and are paid into the general tax coffers of a state.

By contrast, alcohol-specific taxes serve a different function. They may be intended to discourage sales (by increasing the cost to consumers), to fund the costs of regulation (e.g. public education, training of servers, enforcement efforts, defraying costs to society of alcohol use), or to fund social projects (such as school lunches in Utah, where 13 percent is added to the markup of alcohol purchases to fund school lunch programs). Often these alcohol-specific taxes provide the funding for the alcohol regulatory agencies.

Alcohol-specific taxes are imposed by states pursuant to exercise of their police powers and exist in furtherance of policy goals selected by the states. Thus, these taxes are of a very different nature than sales taxes and they should be treated in a different manner than sales taxes.

It should be noted that S. 577 is not an anti-Internet nor is it a tax bill. It is a simple law enforcement device allowing state enforcement action against anyone who violates state law, regardless of how the sale was solicited or consummated.

I hope this provides sufficient response to your questions. If you have further questions, please feel free to contact me.

INDUSTRY CIRCULAR—DEPARTMENT OF THE TREASURY, BUREAU OF ALCOHOL,
TOBACCO AND FIREARMS—NUMBER 96-3

DIRECT SHIPMENT OF ALCOHOL BEVERAGES

February 11, 1997.

Bonded Wineries, Breweries, Importers, Wholesalers, Retailers and Other Concerned

Purpose. The purpose of this circular is to inform industry members that an ATF Ruling will be published in a future issue of the Alcohol, Tobacco and Firearms Bulletin. The ruling will read substantially as follows:

The Bureau of Alcohol, Tobacco and Firearms (ATF) has recently received a number of requests from various States for our assistance in the enforcement of State alcohol beverage laws. The States are concerned with mail order, telephone, and Internet sales and shipments made directly to consumers in a State from sellers located outside the State. These transactions usually involve small quantities of wine or beer shipped by out-of-State sellers (including beer and wine of the month clubs) and, when considered individually, seem to have a negligible effect on interstate commerce. taken in the aggregate, however, these shipments result in a substantial revenue loss to the States of the purchasers. The National Conference of State Liquor Administrators has estimated that these types of interstate sales currently amount to \$300 million annually and result in State tax revenue losses of tens of millions of dollars. The States are also concerned that shipments may be made to underage drinkers.

The States have asked ATF whether these types of transactions violate the Webb-Kenyon Act, 27 U.S.C. § 122. The States have also asked about the circumstances under which ATF will take enforcement action against these types of transactions.

Background. Section 202(b) of the Liquor Law Repeal and Enforcement Act, known as the Webb—Kenyon Act, was enacted relative to the adoption of the Twenty-first Amendment and is, in effect, a statutory declaration of the constitutional prohibition. The Twenty-first Amendment provides that the transportation or importation into any State, Territory, or possession of the United States for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is prohibited.

The Webb-Kenyon Act provides that the shipment or transportation of any beverage alcohol product, from one State into any other State in violation of any law of such State is prohibited. Neither the Twenty-first Amendment nor the Webb-Kenyon Act provide for any criminal or civil penalties for violations thereof.

The Federal Alcohol Administration Act (FAA Act), 27 U.S.C. § 203, requires a basic permit in order to engage in the business of importing into the United States, distilled spirits, wine or malt beverages. Likewise, a basic permit is required to engage in the business of distilling spirits or producing wine. Finally, a basic permit is required for persons who engage in the business of purchasing for resale at wholesale distilled spirits, wine, or malt beverages. Retailers are not required to obtain basic permits under the FAA Act. In addition, 27 U.S.C. § 204(d) provides that basic permits are conditioned upon compliance with the Twenty-first Amendment and other Federal laws relating to its enforcement.

Consequently, ATF could under appropriate circumstances take administrative action against a basic permit where a basic permittee ships alcohol beverage products into a State in violation of the laws of that State. However, the extent of this authority does not extend to situations where an out-of-State retailer is making the shipment into the State of the purchaser.

Held, the Webb-Kenyon Act is a law relating to the enforcement of the Twenty-first Amendment and is a condition of the basic permit under 27 U.S.C. § 204(d) for violations of which ATF may suspend or revoke the basic permit.

Held further, ATF will respond to an official State request for assistance only where a written determination has been made by the chief administrative officer of the State liquor enforcement agency or the State Attorney General that the conduct violates State law *and* ATF has independently determined that the State law violation has some pronounced impact on the regulatory and/or criminal enforcement scheme of the State in question. That is, ATF will evaluate the conduct in question in relation to the proper exercise of its federal authority over matters that necessitate federal intervention. For example, ATF will not take action to suspend or revoke a basic permit for a violation of a local ordinance prohibiting the sale or delivery of alcohol beverage products prior to 10 a.m., when the direct shipment is delivered by a common carrier earlier than 10 a.m.

RESPONSES OF STEPHEN DIAMOND TO QUESTIONS FROM SENATOR HATCH

Answer 1. There was language in some of Justice Brandeis' decisions in the 1930's that suggested that the Twenty-first Amendment immunized discriminatory state regulations. In *Young's Market*, however, Brandeis found the challenged California statute to be a reasonable, i.e. nondiscriminatory, one. In other decisions, he suggested that retaliatory state legislation might better be described as protective, implying that the legislation was reasonable. In *Ziffirin*, decided contemporaneously, Justice McReynolds explicitly evaluated the reasonableness of the challenged law.

Subsequently, in *Bacchus*, the Supreme Court explicitly rejected protectionist, i.e. facially discriminatory, tax legislation in which Hawaii attempted to exempt two locally produced alcoholic beverage products from a general tax on all other alcoholic beverages. Facial discrimination, exempting in-state products from taxes, permitting only products created from locally grown grapes to be sold in grocery stores, [(see *Loretto* 601 F. Supp. 850 (1985))] is therefore forbidden.

That a wine producing state has a lower tax rate on wine or a beer producing state has a lower tax rate on beer has not been deemed discriminatory. A policy that benefits local producers, but does not do so explicitly or exclusively, is thus permitted. States also can do permit in-state breweries and wineries to sell retail on site. All states require that sales be through regulated channels. Most of these states do not produce wine—about which much of the present controversy seems to be focused. They are not protecting their own producers either explicitly or implicitly.

Answer 2. If the judicial interpretation of extra-territoriality was such that a state could not prevent unregulated interstate shipments, i.e. no jurisdiction over sellers, no realistic possibility of action against transportation companies, then the state's capacity to collect taxes or regulate prices in ways that justices of the Supreme Court have recently suggested are options available to states would be vitiated.

Answer 3. Those who supported Repeal believed that there could and should be no single, centrally imposed, regulatory structure for alcoholic beverage sale and use. To create its own regulatory regime, either a monopoly or a license system, a state needed and needs the capacity to control its own borders. State wholesale monopolies or regulated private wholesalers were the techniques used to structure access to and permit regulation of the state market.

Answer 4. If states cannot control the flow of alcohol across their borders, they cannot realistically protect their tax or monopoly mark-up revenues. They also cannot regulate the distribution system in the interest of temperance or orderly markets (the ultimate purpose of orderly markets again being temperance). If the business of in-state retailers is significantly reduced by out-of-state shipments, they may, to survive, engage in sales to the underaged or intoxicated, sales after hours, etc. A lesson of Prohibition was that government should not simply ban what are perceived to be undesirable activities. It should instead administer a system which reduces the likelihood of illegal behavior rather than simply punishing it when it is discovered. It is the unregulated and potentially limitless nature of the shipments that threaten state regulatory interests.

Answer 5. It is unlikely that voluntary codes of ethics would work. This is not because the alcoholic beverage industry is any more lawless than any other industry. It is because voluntary codes, to the extent they have ever worked, have only done so when the activities involved were sufficiently public and visible, at least within the trade, that they could be effectively policed by competitors, who would report or threaten to report violations to the authorities. This does not appear structurally possible with interstate shipments.

RESPONSES OF STEPHEN DIAMOND TO QUESTIONS FROM SENATOR GRASSLEY

Answer 1. BATF rejected requests that it pursue interstate shipments under Webb-Kenyon, but did eventually, as *amicus*, support Florida's unsuccessful effort to get injunctive relief under the Act. In Industrial Circular No. 96-3, issued February 11, 1997, BATF stated:

ATF could under appropriate circumstances take administrative action against a basic permit where a basic permittee ships alcohol beverage products into a State in violation of the laws of that state. However, the extent of this authority does not extend to situations where an out-of-State retailer is making the shipment into the State of the purchaser.

BATF has announced, I believe, that it would investigate state complaints about winery shipments.

Answer 2. Common carriers are included in several states' penal statutes prohibiting unauthorized interstate shipments. Some state regulators have voiced concern that carriers might successfully defend themselves from felony prosecutions, by asserting their ignorance of the contents of the package, especially when the shipment is not made directly from the winery or retail store, but from, for instance, a packaging company. On the other hand, several states have informally put pressure on common carriers to refuse such shipments.

Recently a federal court in Massachusetts, in *Wine and Spirits Wholesalers of Massachusetts, Inc. v. Net Contents, Inc.*, 10 F. Supp. 3d 84 (1998), a suit brought by wholesalers against an out-of-state shipper and Fed. Ex, held that, with regard to the tort claim against Fed Ex, state law was pre-empted by the Airline Deregulation Act, which prohibits states from regulating prices or services. If the same result were to be reached in a suit brought by a state, states would not be able to pursue legal action against air carriers unless Congress were to amend the Act.

Answer 3. I have no information on this subject. The commission may not be considering alcoholic beverage taxes since states prohibit such sales for regulatory as well as fiscal reasons.

ADDITIONAL SUBMISSIONS FOR THE RECOED

AMERICAN VINTNERS ASSOCIATION,
Napa, CA, March 5, 1999.

Senator ORRIN HATCH,
Chairman, Senate Judiciary Committee,
U.S. Senate, Washington, DC.

DEAR SENATOR HATCH, *Free the Grapes!* is a national, non-profit coalition of 145,000 wine consumers and associations representing over 1,000 of America's winemakers. Our mission is to ensure consumer access to fine wine by exposing pending legislation that is anti-consumer and anti-free trade. Our strategy is to rally wine lovers who are fed up with laws which protect wholesaler middlemen at the expense of their ability to enjoy wines not available in their market.

Our funding comes exclusively from wine consumers tired of unnecessary government intervention, and individual winemakers who just want to satisfy demand for their wines and get back in the cellar to blend the latest vintage. (Some of the organizations at left provided seed money in mid-1998.) From the stacks of letters and emails I receive, I can assure you that our consumer supporters show an enthusiasm for this issue which is inversely proportional to the size of our modest budget.

These same wine lovers, your voters, are very aware that America's wineries produce far more labels each vintage than any wholesalers or retailers could possibly stock and sell. Of America's 1,800 wineries located in 48 states, over 1,700 of them are small, family owned and operated; cumulatively, they produce less than 5 percent of all the wine produced in the U.S. Yes, less than 100 U.S. wineries produce over 95 percent of all wine, and they *need* the 3-tier system to efficiently distribute millions of cases.

We advocate *augmenting*, *not replacing* the current 3-tier system by allowing the estimated 1 percent of wine that is direct shipped to be appropriately regulated. Buying wine by catalogue or online is not like buying sweaters from Maine; both consumers and wineries understand the differences with a socially sensitive product. As evidenced by their model legislation, the wine industry supports purchasing licenses in each state, making excise tax payments, volunteering to pay sales tax liabilities, reporting shipments, labeling cartons, and using couriers accustomed to validating identification of adult recipients. Additionally, *Free the Grapes!* issued in January a voluntary "Wine Industry Code for Direct Shipping" which includes these provisions and is now open for a comment period, although the Santa Barbara County Wineries Association already endorsed the code without changes.

I urge you to carefully consider the costly implications and motivations behind this effort to more aggressively prosecute out-of-state winemakers for shipping a bottle of wine. Certainly every state should be able to enforce its law. My fear is that legislation resulting from your hearing will put a damper on creative state-by-state solutions that have been enacted (e.g., NH, LA) or are currently being considered (e.g., AZ, TX, MT, NY) which satisfy my consumer constituents, and are supported by the wine industry.

One wonders how the public is served, and what the motivations are, behind legislation which seems unrelated to legitimate state interests for ensuring public safety. You should know that California, which accounts for 29 percent of the nation's table wine consumption, allows direct shipping—wholesalers, wineries, retailers and consumers all thrive. If there are no problems with direct shipping in California, or with the other 29 states that allow intra-state direct shipping, what other motivations can there be for the legislation you are considering?

In some states (e.g., FL, GA, KY), harsh felony laws are only meant to intimidate winemakers into compliance with laws seemingly inimical to the letter and spirit of the commerce clause. In North Dakota, a pending bill supported by wholesalers names wine consumers accomplices to felony offenses for direct shipping. In Texas, a pending bill carries the same penalty as a conviction for assault with a deadly weapon. Do you really want to criminalize wine connoisseurs and winemakers?

The motivations for this legislation are simple: the powerful wine wholesaler middlemen mistakenly fear that direct shipping is the first step towards dismantling the 3-tier wine distribution system. They want 100 percent of sales to flow through their coffers, not 99 percent, because they wrongly fear that 99 percent will eventually decrease. They are using the 21st Amendment to prop up a business model that was appropriate when created 65 years ago. Direct shipping has two main causes: it is pressure relief valve for wineries to satisfy tourism-generated demand for small production wines; and secondly, for small family-owned and operated wineries to

gain access to consumers in states where wholesalers have no financial incentive to represent them.

Undoubtedly our well-funded opponents will cry foul over lost state tax revenues and underage access. I've addressed the tax issue; in fact, state revenue may increase as states establish the provisions to receive both the excise and sales taxes wineries are willing to pay. The underage access issue will no doubt capture your imagination with colorful testimony from well-meaning but misguided witnesses. Reports of elaborate PR "stings," concocted purely for TV cameras, are artificial, forced sales attempting to prove a hypothetical point. They are not indicative of legal, responsible transactions that are the norm.

Do you really believe that the clerk at the corner store is better qualified to validate identification than a courier who is trained to deliver radioactive materials, flammable liquids, and body organs?

Is the system perfect? Of course not. We do not condone, nor turn a cheek, to those who break any state laws. But the industry is voluntarily establishing standards and supporting provisions to mitigate any risks to public safety and state revenue sources. As you know, Congress has established a commission to grapple with the issues of burgeoning Internet commerce and there is a laudable effort to interject interstate wine shipments into the discussion.

If you're going to shackle the winemakers, and criminalize the connoisseurs, where does this lead? Under the 21st Amendment Enforcement Act—which I would rename the "Wholesaler Protection Act"—are Americans now subject to not only federal and state law, but also the laws of any other state which chooses to use the 21st Amendment to prosecute them? Are the states, in effect, enacting laws that they cannot themselves enforce?

This legislation may only add the number of cases before the Federal judiciary and could end up costing Americans more in taxes. Please, let the states and the industry solve this industry squabble for the benefit of adults who just want to enjoy a delicious glass of wine with tonight's dinner.

Thank you very much for your time and for considering the viewpoint of thousands of consumers.

Sincerely yours,

JEREMY BENSON,
Executive Director.

UNIVERSITY OF CALIFORNIA,
Berkeley, CA, March 5, 1999.

The Hon. ORRIN G. HATCH,
Chairman, Senate Judiciary Committee,
U.S. Senate, Washington, DC.

The Hon. PATRICK J. LEAHY,
Ranking Minority Member, Senate Judiciary Committee,
U.S. Senate, Washington, DC.

DEAR SENATORS HATCH AND LEAHY: I write about Senator Hatch's Bill, scheduled for hearing before the Judiciary Committee on March 9, 1999, that has been said to "add enforcement" to the Webb-Kenyon Act passed by Congress in 1913. I am a Professor specializing in Constitutional Law (and the former Dean) at the School of Law of the University of California at Berkeley (Boalt Hall). I attach a copy of my curriculum vitae.

I believe it is most important to underline that the Bill goes far beyond simply providing a remedy for a violation of Webb-Kenyon. Instead, it makes fundamental changes in current law and in doing so affects serious constitutional and public policy issues. Webb-Kenyon prohibits the importation of alcoholic beverages into a state in violation of that state's laws. It is generally understood that Congress' intent in passing the statute in 1913 was to give federal sanction to a state's decision to "go dry," an authority that had been denied to the states by the Supreme Court in *Leisy v. Hardin*, 135 U.S. 100 (1890).

Webb-Kenyon does not authorize a state to erect discriminatory barriers to interstate commerce. Indeed, in the absence of an express federal enactment, any attempt by a state to do so—by conferring different rights on in-state and out-of-state producers of alcoholic beverages—would violate the core principle underlying the Commerce Clause of Congress can so regulate trade between the states.

Nor does the 21st Amendment, which confers special powers on the states regarding alcoholic beverages, affect that conclusion. In *Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263 (1984), the Supreme Court held the 21st Amendment did not permit state

regulations of the local sale or use of liquor to discriminate against interstate commerce. To do so, the Court reasoned, would be inconsistent with a central tenet of the Commerce Clause: forbidding economic protectionism.

I believe that the Bill, rather than simply creating a federal remedy for a violation of Webb-Kenyon in its current form, would dramatically expand the powers of the states to regulate alcoholic beverages. Most significantly, it would run counter to the spirit of Bacchus and remove the protection that the Commerce Clause grants the alcoholic beverage industry, along with all others, from state erection of barriers to free trade.

I would be happy to provide any further information you may find helpful.

Sincerely,

JESSE H. CHOPER,
Earl Warren Professor of Public Law.

UNIVERSITY OF CALIFORNIA,
Berkeley, CA, March 9, 1999.

The Hon. ORRIN G. HATCH,
Chairman, Senate Judiciary Committee,
U.S. Senate, Washington, DC.

The Hon. PATRICK J. LEAHY,
Ranking Minority Member, Senate Judiciary Committee,
U.S. Senate, Washington, DC.

DEAR SENATORS HATCH AND LEAHY: I wish to add an important addendum to my letter to you of March 5 concerning my views on the proposed amendment to the Webb-Kenyon Act.

I should have noted and I regret not doing so in my letter, that I was retained in this matter by the American Vintners Association. Further, my opinion is my own, not that of the University of California or Boalt Hall, and my title appeared for purposes of identification only.

Needless to say, I want to underline that my conclusion in that letter was reached as a matter of objective appraisal of the governing constitutional and statutory provisions, not simply put forward as advocacy.

With best wishes.

Sincerely,

JESSE H. CHOPER,
Earl Warren Professor of Public Law.

KENDALL-JACKSON,
Santa Rosa, CA, March 2, 1999.

The Hon. PATRICK LEAHY,
Senate Judiciary Committee,
Russell Senate Office Building,
Washington, DC.

DEAR SENATOR LEAHY: On behalf of the wine industry in general and, more specifically, Kendall-Jackson winery, I would like to take this opportunity to express to you my concerns the upcoming Judiciary Committee Hearing and any potential legislation that may be introduced for that hearing. We understand that legislation may be modeled in part after H.R. 1063, a bill that was introduced in the house last session by Congressman Ehrlich to expand the jurisdiction of the Webb-Kenyon Act to Federal courts. That bill died in committee last session. Chairman Coble's position was that the bill would not move forward unless members of the industry came to a compromise, although the wine industry proposed a compromise solution, the alcohol beverage wholesalers would not agree to this compromise.

There is a tendency to muddy this issue with serious matters of concern for public policy, namely, underage consumption of alcohol and State taxation. However, we believe that two facts are important to remember (1) based on our experience with direct shipping in California, we believe that underage purchases of wine is anomalous, and there is nothing but anecdotal evidence about underage internet access to alcohol (few teens for or can afford cabernet sauvignon); and (2) there are existing remedies at the state and federal levels to address violations of underage purchases of alcohol.

As a threshold matter, Kendall-Jackson questions whether it is necessary to grant states access to Federal courts to enforce violations of state law given that there is

an existing Federal remedy available to the states at present. Pursuant to the 21st Amendment to the United States Constitution the “transportation or importation into any State * * * in violation of the laws thereof, is * * * prohibited.” The Federal government does not have a role in regulating the liquor industry through the Federal Alcohol Administration Act. 27 U.S.C. §201 *et seq.* A federal “basic permit” is required to engage in the business of producing, importing or purchasing an alcohol beverage for resale. 27 U.S.C. §203. The basic permit is conditioned on compliance with federal law. 27 U.S.C. §204 (d). Even with the Constitution empowering states to regulate alcohol, the Commerce Clause could arguably be interpreted to erect an impediment to state regulation of liquor. *See*, U.S. Const., Art. I, Sec. 8, Cl. 3. However, Congress passed the Webb-Kenyon Act to prohibit “[t]he shipment or transportation * * * of any * * * intoxicating liquor * * * into any other State * * * in violation of any law of such State.” 27 U.S.C. § 122.

While the Webb-Kenyon Act did not provide for federal remedy or jurisdiction (*see Florida Dept. of Business Regulation v. Zachy’s Wine and Liquor*, 125 F. 3d 1399 (11th Cir. 1997), *cert. denied*, 118 S.Ct. 1402 (1998) (holding the 21st Amendment and Webb-Kenyon do not confer on the states a civil remedy)), it does serve two important functions: (1) liquor has been divested on its interstate character and States are empowered to restrain trade and burden commerce (with some limitations)¹ as they regulate liquor; (2) the Federal government which issues basic permits to distillers and wineries can revoke the basic permits upon the violation of federal law. Webb-Kenyon “assimilated” state law violations into federal law violations for this purpose. Therefore, a violation of Webb-Kenyon by shipping liquor in violation of state law subjects the basic permit to suspension or revocation. 27 U.S.C. §204(e).

The Department of Treasury is charged with enforcement of the Federal Alcohol Administration Act, but it has delegated this task to ATF. Under current law, a state may submit a complaint, ATF will investigate the complaint and, if it is credible, take appropriate action, including the withdrawal of the offenders basic permit. ATF Industry Circular 96-3. This avenue is rarely used—perhaps due to the effectiveness of State enforcement efforts—but in the single instance of which I am aware involving a producer in Louisiana, ATF investigated the case which resulted in the voluntarily withdrawal of its permit. This example demonstrates that the intended result will occur if the available remedies are used. If there is serious concern that AFT would not take the appropriate action, there may be adequate remedies to encourage more appropriate action by AFT short of an additional federal law such as H.R. 1063.

Kendall-Jackson seeks to comply with all local, state and federal laws and would never jeopardize its ATF basic permit—that permit is the life of its business, as is true with all wineries. Clearly, the Federal remedy is an adequate deterrent and remedy. State courts already have jurisdiction over those who violate their state laws—unless there are no minimum contacts. Therefore, the only remaining issue that Congress could consider is how to reach out-of-state brewers and retailers who do not have minimum contacts with the state.

Cases in Florida and Utah have touched upon this issue. The Florida state court case (*State of Florida v. Sam’s Wines & Liquors*) held that mere shipment does not constitute minimum contacts. The Florida Federal court case (*State of Florida v. Rachambeau Wines and Liquor*) confirms that there is no Federal court jurisdiction to enforce Webb-Kenyon. The court’s discussion of the legislative history, including the intent of Congress to exclude jurisdiction, is worth reviewing. The Utah case (*State of Utah v. Amoroso and Beer Across America*) addressed the question of where the sale occurs, holding that the sale takes place in the State where the seller is located and that the shipment is for the convenience of the customer. In other words, there is no violation of State law in the recipient State that would seek to enforce Webb-Kenyon. Therefore, one is left wondering what hypothetical situation the proponents of Webb-Kenyon Act reform hope to reach.

States have been enforcing their liquor laws against out-of-state entities and continue to do so today. *See, e.g., Ivey v. Bacardi Imports, Inc.*, 541 So.2d 1129 (Fla. 1989); *James B. Beam Distilling Co. v. State*, 382 E.2d 95 (Ga. 1989), *rev’d* 501 U.S. 529 (1991), *appeal after remand*, 437 S.E. 2d 782 (1993), *cert. denied*, 513 U.S. 1056 (1994); *All Brand Importers, Inc. v. Department of Liquor Control*, 567 A.2d 1156 (Conn. 1989); *Division of Alcoholic Beverages and Tobacco, Department of Bus. Regulation v. McKesson Corp., et al*, 524 So. 2d 1000 (Fla. 1988) *rev’d on other grounds*,

¹The Supreme Court held that the “Twenty-first Amendment grants the States virtually complete control over whether to permit importation or sale of liquor and how to structure the liquor distribution system. Although States retain substantial discretion to establish other liquor regulations, those controls may be subject to the federal commerce power in appropriate situations.” *California Retail Liquor Dealers Assn. v. Medcal Aluminum*, 445 U.S. 97, 110 (1980).

496 U.S. 18 (1990); *Williams v. Commonwealth*, 56 S.E. 2d 537 (Va. 1949); *Oregon Liquor Control Comm'n v. Coe*, 99 P.2d 29 (Or. 1940).

Last session, proponents of H.R. 1063 decried the limited reach of state court jurisdiction. However, the exercise of state court jurisdiction is limited by the lack of personal jurisdiction, which is a fundamental legal principle with roots in due process that stands for the common sense proposition that you cannot sue someone and exercise a judgment against them in a place where they have no connection. *H.R. 1063 did not solve this problem.* the fallacy of the approach of H.R. 1063 is twofold. First, the limits of due process and personal jurisdiction do not disappear in federal court—they are essentially the same. Second, the grant of federal jurisdiction to enforce the recipient-state laws is useless: since the sale occurs out of state, *the recipient-state laws would not even apply.* See e.g., *State of Utah v. Amoroso and Beer Across America* (holding that the sale takes place where the seller is located and that the shipment is for the convenience of the customer).

Even so, one needs to address the emotional issue of underage drinking. Fundamentally, I believe the history of New York and California—two States that allow direct shipment—demonstrates that direct shipment of wine is not a factor with underage drinking. Panelists speaking about direct shipping at the Unified Wine and Grape symposium in Sacramento, including Manuel R. Espinoza, the Deputy Director of California's Alcoholic Beverage Control Board, came to the same conclusion. Unfortunately, if a law enforcement official wants to create a sting operation by directing an underage person to obtain wine through direct shipment, sooner or later it will result in an improper shipment. Nevertheless, we are confident that this contrived situation does not occur with any statistical significance.

The vast majority of wine produced by Kendall-Jackson is distributed through the traditional three-tier distribution system. To put this issue of direct shipment in perspective; during a period between February 1992 and December 1998, Kendall-Jackson sold approximately 15 million cases of wine. Over the same timeframe it shipped about 2 tenths of 1 percent (0,0002 percent) to consumers outside California. Kendall-Jackson presently does not ship outside of the State of California due to the danger of entrapment sting operations and harsh state laws, some imposing felonies—punishable with jail time—simply for shipping a bottle of wine. This situation simply harms small family-owned wine businesses and adults who wish to purchase wine without addressing any real world problem such as underage drinking. There are commonsense ways to address underage drinking problems. For one, producers and shippers should always require the purchasers to certify their age and the container should be marked indicating an adult signature is required before it is released. Several States, including New Hampshire, have enacted laws requiring producers to register with the State before they can ship into the State. This seems to be a reasonable approach—and one that can be achieved without burdening the Federal judiciary.

Another issue concerns the States' ability to tax transactions over the internet. I know that you are keenly interested in legislation affecting internet tax. For the highly regulated wine industry, taxation is a way of life. federal and state regulators have free and open access of our records in order to verify that all the taxes that are levied on our product have been paid. This is not something that is new to our industry. Look at the States of Louisiana and New Hampshire. While working with legislators in those progressive states to craft permit legislation that would allow us to reach loyal customers, we have openly agreed and encouraged these states to have access our records to document that the appropriate taxes have been remitted for wines shipped to their states. The issue is not payment of Texas, the industry would agree to pay its fair share, the issue is the undue barrier to interstate commerce.

The industry is highly concentrated among the top few wholesalers. According to the Johnson Liquor Handbooks, wine producers in the U.S. have increased from 377 to 1,772 from 1963 to 1994 (over 400 percent). In the same period, the wholesale tier has dropped dramatically from 10,900 to 2,928 distributors nationwide. Therefore 25 percent as many wholesalers are left to serve 4 times as many wineries. This proliferation of primarily small, family owned, wine businesses and consolidation of distributors has significantly restricted access to reasonable commerce channels. Clearly, the small wineries are not able to get representation to serve loyal customers in many markets. The top 15 U.S. wine and spirits wholesalers distribute over 50 percent of the market share. We the producers, on the other hand, want to provide the consumers with a greater choice in products at a reasonable price. Simply put, we want to encourage entrepreneurs to continue to devise new legal methods to bring their products to market.

There is a final piece of the puzzle that needs consideration. Attorneys-General has targeted wine producers as the villain in some states with sting operations. I

find it very interesting that the other two parties to the transaction escape scrutiny. The producers have put safeguards in place at the time of ordering that require certification by the customer that they are adults. When we give our product to the second party in the chain, the shipper, it is clearly labeled "adult signature required". The carrier must be diligent and confirm that our wine is delivered to a legal consumer. The third party is the consumer. Have there actually been prosecutions by these same Attorneys-General of underage purchasers using direct shipment to acquire alcohol? The simple answer is no. A sting operation is one thing, actual violations are another. Kids are not going to use direct shipment to acquire alcohol. They don't want the paper trail of a credit card purchase. They are not going to purchase relatively expensive table wine. They are not willing to wait for the period of the delivery time. They can not risk the possibility of delivery when their parents are home, and if the carrier does its job, they would not be able to take delivery since they are not adults and would not be able to sign for the shipment.

Kendall-Jackson supports direct interstate shipments. Please call if you have questions or concerns. Again, thank you for your willingness to hear our side of this issue.

Sincerely,

JESS S. JACKSON,
President, Kendall-Jackson.

UNIVERSITY OF BALTIMORE,
SCHOOL OF LAW,
Baltimore, MD, March 8, 1999.

Re: S. ____: 21st Amendment Enforcement Act

M. CRAIG WOLF, Esquire,
Counsel, Senate Judiciary Committee,
U.S. Senate, Washington, DC.

DEAR MR. WOLF: Thank you very much for your request for comment on S. _____. I suppose that it is not very often that elementary principles of civil procedure are essential to the deliberation of our country's highest legislation. S. _____ appears to present such a rare occasion and I am happy to assist you.

I will address service of process and venue, though only briefly, and comment more fully on personal jurisdiction. I note that the "latest draft" that you faxed me provides for venue in the district where the defendant resides. This differs from an earlier draft you sent me that provides a suit may be brought in "a judicial district where a person resides or is found that has *received* liquor transported or shipped to that person from another person * * *" (emphasis added). Presumably this means a district court in the state which seeks to bring such an action.

If the Committee has decided to abandon an approach which allows a state to enforce its liquor laws in its "own" federal courts, and instead, to require state attorney general offices to chase "electronic bootleggers" around the country (no doubt, an expensive proposition for some states in hard times), there is not much for me to comment upon. Suing a defendant where it resides or ships liquor from poses no serious issues of process, venue or personal jurisdiction. Assuming the possibility that the plaintiff's venue approach of the earlier draft was discarded because of constitutional personal jurisdiction concerns, I presume to address such concerns. In my opinion, they are not serious enough to require state officials to chase long distance violators of their liquor laws around the country.

As to the matter of service of process, I submit that Rule 4(k)(1)(A) of the Federal Rules Civil Procedure would suffice even if state plaintiffs were able to sue in federal courts in their own states. Process under this rule is effective if the defendant is amendable to suit under the due process analysis I will discuss below.

As to venue, I submit that it would not be objectionable to fix venue in the district courts in the plaintiff state. Although 28 U.S.C. § 1391, the general venue statute, no longer provides for plaintiff's venue as such, it did so until 1990. In light of the jurisdictional considerations I discuss below, I believe that venue could appropriately be fixed in federal courts in the plaintiff's state.

With respect to personal jurisdiction, the question that jumps out at one who considers S. _____ is: how is it possible to assert personal jurisdiction over a party in a forum across the country from where that party conducts its operations simply because that party has shipped a few cases of wine to the forum? The answer to this question is not as simple as might appear at first glance.

The seductively simple answer that the suit to prevent interstate violation of state liquor laws may not be brought in the state where liquor is shipped in violation of state laws rests on the notion that the Supreme Court, since *Hanson v. Denckla*,

357 U.S. (1958), has tended to construe personal jurisdiction restrictively. While it is true that defendants resisting state personal jurisdiction have won in the Supreme Court more frequently than plaintiffs asserting it, that is not the central reality of the Supreme Court jurisprudence of due process and personal jurisdiction of the modern era, *i.e.*, the era opened by *International Shoe v. Washington*, 326 U.S. 310 (1945). The central reality of the court's jurisprudence in this area is the development of protection for three interests:

1. Fairness to a defendant, requiring that the burden of defense not be disproportionate to defendant's affiliating circumstances *vis a vis* the forum;
2. Protection of the mutual sovereignties of the states from judicial encroachment; and
3. Protecting the right of states to provide forums for controversies in which they or their citizens have substantial interests.

The first of these interests, the protection from constitutionally inconvenient litigation springs in the modern era from *International Shoe Co., v. Washington*, 326 U.S. 310 (1945). The court, pursuant to the Fourteenth Amendment, required minimum contacts between a defendant and a forum in order to require a defendant to defend in the forum. In that case the suit was to collect Washington State employment taxes from a manufacturer of shoes that had sent shoe salesmen to the state. In holding that assertion of jurisdiction by Washington over the out of state defendant was constitutional the Court noted, among other things, that the suit arose out of the defendant's activities in the state. In the years since *International Shoe*, the Court has looked to whether or not agents of a defendant have been physically present in the forum, but the Court has not always required some sort of physical presence in the forum as a precondition of a determination of constitutional fairness.

An interesting example of a finding of jurisdiction over a defendant who was never present in a state may be seen in *Calder v. Jones*, 465 U.S. 783 (1984). In that case actress Shirley Jones sued the *National Enquirer* and a reporter, one Calder, in a California state court for defamation. The reporter, who lived in Florida and did not travel to California in connection with the story, asserted lack of personal jurisdiction. The Court upheld California's jurisdiction over the reporter on the basis of the foreseeable effects the story caused in California.

In a case decided the same day, *Keeton v. Hustler Magazine, Inc.*, 465 U.S. 770 (1984), the Court upheld personal jurisdiction under New Hampshire law over a libel suit against *Hustler*, an Ohio corporation. It found minimum contacts on the basis of the sale of 10,000 to 15,000 copies of *Hustler* every month in New Hampshire.

In both cases, it might be argued that the "presence" of the defendants in the forums was of a lesser magnitude than that of the defendant in *International Shoe*, which actually had employees in Washington. Nonetheless, the Court in both cases was influenced by the interest of both forums in protecting their citizens from the harm of defamation.

It is clear that the object of due process to protect a defendant from unconstitutional inconvenience has not been viewed in isolation. It has been balanced with the interests of the forum. A number of lower federal and state courts have upheld jurisdiction based upon the sending of goods or services into a forum state. *See e.g., APC Commodity Corp. v. Ram Dis Ticaret, A.S.*, 965 F. Supp. 461 (S.D.N.Y. 1997); *Digital Equipment Corp. v. Alta Vista Technology, Inc.*, 960 F. Supp. 456 (D. Mass. 1997); *Connecticut Nat. Bank v. Hoover Treated Wood Products, Inc.*, 376 Mass. App. Ct. 231, 638 N.E.2d 942 (1994); *Bergherr v. Sommer*, 523 N.W.2d 17 (Minn. App. 1994), review granted and appeal dismissed, *Univ. of Iowa Press v. Urrea*, 211 Ga. App. 564, 440 S.E.2d. 203 (1993), *cert denied*.

The second interest that the Supreme Court has acted to safeguard in the post-*International Shoe* era is the scope of jurisdiction of individual state judiciaries. It has done so by preventing state courts from adjudicating controversies more appropriate for the resolution by courts of other states owing to firmer connection of the parties with such states. That a state must not adjudicate the personal rights of persons with whom it lacks sufficient connection so as to avoid encroachment on states which have such connections is not a novel proposition. It generally prevented state courts from exercising jurisdiction over persons not found within a state, particularly in the nineteenth century. *See Pennoyer v. Neff*, 95 U.S. 714 (1878).

The notion was resuscitated in *Hanson v. Denckla*, 357 U.S. 235 (1958). In that case the testamentary beneficiaries of a Florida decedent sought, in a declaratory judgment action, to have an inter vivos trust established by the decedent invalidated. All of the parties except the trust company that held the property were Floridians. The trustee was a Delaware corporation. The trustee had no corporate pres-

ence in Florida. It had simply continued to deal with the decedent after she had moved to Florida, sending her reports on the affairs of the trust.

In rejecting Florida's exercise of jurisdiction over the Delaware trustee, the court conceded that "progress in communications and transportation has made the defense of a suit in a foreign tribunal less burdensome." *Id.* at 251. That may have been sufficient to vitiate the inconvenience that was crucial to *International Shoe*. But the Court articulated another rationale for the due process restrictions on personal jurisdiction: "They are a consequence of a territorial limitation on the power of the respective states." *Id.* Implicit in this is the proposition that for Florida to adjudicate the status of the trust on the basis of such tenuous contacts to the Delaware trustee would amount to an encroachment of the sovereignty and jurisdiction of Delaware.

This principle became clearer over time. In *Kulko v. Superior Court*, 436 U.S. 84 (1978), the Court rejected California's exercise of jurisdiction over a suit for child support against a New York father whose children lived with their mother in California. The father's "contact" with California was essentially limited to acquiescence in the choice of the children to live with their mother and whatever effects the presence of the children in California may have had there. The Court held, *inter alia*, that California should not have adjudicated a suit that more properly should have been maintained in New York: "[T]he controversy between the parties arises from a separation that occurred in the State of New York; appellee * * * seeks modification of a contract that was negotiated in New York and that she flew to New York to sign." *Id.* at 97.

In *Worldwide Volkswagen Corp. v. Woodson*, 444 U.S. 286 (1980) persons injured in an automobile accident in Oklahoma sued the manufacturer, national distributor, regional distributor and local dealer of the vehicle they had purchased in New York and then drove to Oklahoma. The regional distributor, which did business only in New York, New Jersey and Connecticut, and the local dealer, which served a community in New York, resisted jurisdiction in Oklahoma. In upholding the objections of these parties to jurisdiction, the Court again acted to prevent the forum from encroaching on the jurisdiction of a state with stronger connections to the defendants:

Even if the defendant would suffer minimal or no inconvenience from being forced to litigate before the tribunals of another State; even if the forum State has a strong interest in applying its law to the controversy; even if the forum state is the most convenient forum for litigation, the Due Process Clause, acting as an instrument of interstate federalism, may sometimes act to divest the State of its power to render a valid judgment.

Id. at 294.

Finally, in the last word on the subject, *Asahi Metal Industry Co., Ltd. v. Superior Court of California*, 480 U.S. 102 (1987), the Supreme Court extended its protection through the Due Process Clause of the jurisdiction of the states to protection of the jurisdiction of foreign countries. *Asahi* initially involved a product liability suit in a California state court by injured plaintiffs against the Taiwanese manufacturers of a motorcycle tire. The Taiwanese defendant impleaded the Japanese manufacturer of the tire's valve stem. After all other parties were removed from the case by settlement, the Japanese defendant moved to dismiss the Taiwanese defendant's claim for indemnification on the basis of lack of jurisdiction.

The Japanese defendant sent no products directly to California, though many of its products made their way to California through the efforts of others. In light of the limited contacts of the Japanese defendant with California, the Court regarded California's exercise of personal jurisdiction as an infringement on the jurisdiction of foreign states with which the defendant had a closer relationship. *Id.* at 115.

The protection of the jurisdiction of the states and, where applicable, foreign countries, has become as significant a component of due process in the context of personal jurisdiction, as inconvenience to the parties. It should not play an important role in limiting jurisdiction under S. _____ since suits under that provision would be in federal courts. Nevertheless, the affiliating circumstances that permit a dispute to be adjudicated in one forum rather than another are indicia of the forum with the strongest interest in a suit. That a state under S. _____ would be adjudicating its claim in a *federal* court would not mean that it should be precluded from benefitting from advantages it would enjoy in litigating in its own courts. These would include access to proof and ease in administration of the remedy. Divesting completely the place most affected by conduct proscribed by S. _____ would amount to a departure from the sound logic of state personal jurisdiction cases that have manifested a purpose to limit adjudication to the most appropriate forums.

The third interest that the Court has protected in the course of post-*International Shoe* jurisprudence is the interest of a state to provide a convenient forum for adjudication of controversies in which it or its citizens have an interest.

The leading case involving this interest is *McGee v. International life Insurance Co.*, 355 U.S. 220 (1957). That case involved a suit in a California state court by the beneficiary of a small life insurance policy against a Texas insurer. The insurer defaulted in California and the insured sought to enforce the California judgment in the Texas courts. The Texas courts refused to enforce the judgment based on lack of personal jurisdiction of the California court. The Supreme Court held that the Texas courts erred in not giving full faith and credit to the California judgment.

McGee involved the slightest connection with a forum that the Court has approved as a basis for jurisdiction. there was no indication that the defendant insurer had any connection with California other than the policy at issue, which it had offered to the insured when it took over an Arizona insurer with which the insured had previously had a policy.

An important factor in the Court's approval of California's assertion of jurisdiction on the basis of such limited contacts was the enactment by California of a statute that subjected out-of-state insurance companies to personal jurisdiction in suits by California residents on insurance contracts with such companies. The Court stated:

It cannot be denied that California has a manifest interest in providing effective means of redress for its residents when their insurers refuse to pay claims. These residents would be at a severe disadvantage if they were forced to follow the insurance company to a distant State in order to hold it legally accountable.

Id. at 223. Clearly the interest of California, as expressed in a statute led the Court to permit it to require an out of state company to incur expense in defending that was undoubtedly disproportionate to the business it did there.

Although *McGee* is the high-water mark for personal jurisdiction in decisions of the Supreme court, the significance of providing a home forum for the state or its citizens has not been overlooked in subsequent decisions.

In *Shaffer v. Heitner*, 433 U.S. 186 (1977), plaintiff attempted to sue directors of Greyhound Corp., a Delaware corporation, in Delaware in a shareholder's derivative suit. the defendants had no contact with Delaware other than ownership of stock in Greyhound which a Delaware statute deemed to have a situs in Delaware. Plaintiff attached the stock at the beginning of the suit (effected by stop transfer orders on the books of the corporation) in order to exercise quasi-in rem jurisdiction.

There was no connection between the property seized and the cause of action. There was no connection by the defendants with Delaware other than ownership of stock in a Delaware corporation. The Court applied the minimum contacts test of *International Shoe* to the assertion of quasi-in rem jurisdiction and held that Delaware's assertion of jurisdiction violated due process.

Justice Brennan argued vigorously in dissent that jurisdiction was warranted on the basis of Delaware's interest in "vindicating [its] substantive policies regarding the management of its domestic corporations." *Id.* at 222. Justice Marshall responded for the majority that "[t]his argument is undercut by the failure of the Delaware Legislature to assert the state interest [the plaintiff] finds so compelling." *Id.* at 214.

Weeks after the court's decision in *Shaffer*, the Delaware legislature enacted a statute that provided that acceptance of election as a director in a Delaware corporation was deemed as consent to service of process upon a registered agent in actions for violation of duty as a director. Jurisdiction under this statute was upheld by the Delaware Supreme Court in *Armstrong v. Pomerance*, 423 A.2d 174 (Del. 1980). The court stated:

Clearly, Delaware's interest in providing a sure forum for shareholders derivative litigation involving domestic corporations is firmly grounded on considerations more important and compelling than mere convenience of the parties.

Id. at 178.

As in *McGee*, the interest of the forum outweighed other factors relevant to the personal jurisdiction inquiry.

In *Kulko v. Superior Court*, 436 U.S. 84 (1978), although the Court, as discussed above, rejected jurisdiction, it addressed the matter of "California's legitimate interest in ensuring the support of children resident in California * * * *Id.* at 98. It responded to that consideration by noting that Californians could prosecute claims for child support without leaving California through the Uniform Reciprocal Enforce-

ment of Support Act. The Court took cognizance of California's need to provide a forum for its residents and found it had been met.

The interest of a state in providing a convenient forum to effectuate important interests of the state or plaintiff is an interest that the Court has recognized. It carried the day in *McGee*.

I submit this interest should be considered as informative on the issue of where jurisdiction under S. _____ should be exercised.

The 21st Amendment grants the states broad powers to regulate the importation and use of intoxicating liquors. This interest is probably stronger than that involved in providing a forum for insurance claims in *McGee* and in providing a forum for shareholder's derivative actions in the wake of *Shaffer*. The interest in providing a forum where the impact of violations of liquor laws are felt, in the state the laws of which are violated, may outweigh the inconvenience to senders of such beverages entailed in defending in places in places where laws are violated. This is particularly so since offending shipment is sent intentionally per a customer's order.

Looking at due process decisions involving assertion of jurisdiction by states. I do not believe that it would violate due process to require interstate shippers of alcoholic beverages to defend suits under S. _____ at the places to which such beverages are shipped. I believe that the state law precedents are most relevant because these suits would entail collisions between state and private interests that are analogous to those at issue in post-*International Shoe* Supreme Court jurisprudence. In that jurisprudence, inconvenience to a defendant has not been an absolute that has negated jurisdiction. It has been balanced with other interests.

Once again, I appreciate this opportunity to comment on this important proposal.

Sincerely,

JOHN A. LYNCH, JR.,
Professor of Law.

PREPARED STATEMENT OF THE HON. RON SARASIN, PRESIDENT, NATIONAL BEER
WHOLESALE ASSOCIATION

Mr. Chairman, thank you very much for scheduling this hearing on an issue of great importance to the 3,000 federally licensed beer wholesalers in the United States. Beer wholesalers are the independent, often family-owned small businesses that proudly distribute America's beverage.

The National Beer Wholesalers Association opposes the direct shipment of licensed beverages to consumers in violation of state law. This is a large and growing problem that poses grave risks to the health and safety of the American people, and especially those who are underage. As you will hear and see today, young people may, with ease, order beer, wine and distilled spirits over the phone or via the Internet and have these licensed beverages delivered to their home or dorm room days later, no questions asked. Almost as troubling, young people and older consumers can and do order licensed beverages and have them delivered to their homes even though such direct shipments violate the law in at least 20 states. It is incumbent on this Committee to give state law enforcement officials the tools necessary to enforce their own laws, and your bill will do just that.

As you know, the 21st Amendment to the Constitution, which repealed Prohibition, also granted to States extraordinary authority over licensed beverages within their borders. Section 2 of the Amendment bears repeating here:

The transportation or importation into any State, Territory, or Possession of the United States for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited.

Some 24 states prohibit such shipments outright; 19 others have significant restrictions on the quantities of licensed beverages that can be directly shipped. Nonetheless, many companies continue to ship licensed beverages into states that prohibit direct shipments.

A recent Internet search by my staff found two dozen companies offering to ship beer directly to anyone filling out the on-line questionnaire. Most of these web sites contained a line about the buyer having to be 21 to make the purchase, but one click of the mouse removes that barrier. However, none of them contained any indication that half the states prohibit direct shipments and many more place heavy restrictions on the quantities that may be purchased in this manner. In my opinion, Mr. Chairman, that comes close to fraud.

The main justification for enactment of this legislation is that States face a nearly impossible enforcement task in trying to identify and take action against direct shipments that violate state law. Often, the only way a state can even find out

about a violation of law is through a “sting” operation, when an agent of the state places the order, receives the illegally shipped order, and then files a complaint against the shipper. Even then, out of state companies are often beyond the reach of the authorities.

Mr. Chairman, enactment of your bill will provide incentive for all to obey the law. It will provide state law enforcement authorities with the ability to go into federal court to enforce its law against direct shipments. It is fundamental a states’ rights approach to this vexing problem.

Indeed, there are many sound reasons for a state to prohibit direct shipments to consumers:

- To stem the loss of state tax revenue, estimated to be at least \$200 million a year;
- To keep minors from getting licensed beverages delivered to their doors;
- To prevent deliveries to the 400 “dry” counties in the United States;
- To ensure a level playing field for licensed, law-abiding and taxpaying wholesalers and retailers within the state;
- To preserve and protect the three-tier system for licensed beverage distribution.

Of these reasons, perhaps the most misunderstood today is the last. I submit to you that the three-tier system, developed in nearly every state in the wake of Prohibition, is more vital today than when it was established. The system requires an independent wholesale tier to insulate retailers from undue influence by suppliers, ensure the integrity of the product, provide a paper trail of handling of the product, and permit state enforcement officials to stop the flow of particular licensed beverages into their state for reasons of health, safety or violation of law.

There are legal alternatives to direct shipping. In Maryland, for instance, a consumer may order a particular beverage not normally available and secure delivery through a wholesaler and retailer at no great additional cost. The CellarMasters wine program is another notable success in providing consumers access to hard-to-find beverages while conforming to state laws. NBWA is committed to helping small brewers and microbreweries get their product to market and, to that end, we have joined forces with the Brewers Association of America, representing small brewers, to make it happen.

But direct shippers who operate in violation of state law are more interested in avoiding the state excise taxes and keeping the increased profits obtained by eliminating the in-state retailer and wholesaler than they are in consumer welfare. This is simply not a consumer issue.

Mr. Chairman, the beer wholesalers in your state are licensed, pay all appropriate taxes, keep all required records and sell one of the most regulated products available today. Simply put, we believe that a beer-of-the-month club halfway across the country should have to obey the same laws.

We strongly support the right of states, as guaranteed by the 21st Amendment, to regulate the distribution and sale of licensed beverages within their borders. Enactment of your bill will that possible.

PREPARED STATEMENT OF SIMON SIEGL, PRESIDENT, AMERICAN VINTNERS
ASSOCIATION

CHAIRMAN HATCH AND MEMBERS OF THE COMMITTEE: I am grateful for the opportunity to submit written comments on proposed legislation titled “The Twenty-First Amendment Enforcement Act.” The American Vintners Association is the national trade association, representing over 550 wineries in 43 states. On behalf of our members, and all American wineries, we urge you to tread very cautiously in making any changes to federal statutes in this area. Any federal legislation must represent a balanced approach of controlling undesirable commerce while enabling negotiations, on a state-by-state basis, to continue in a manner that permits wineries and their customers to conduct business.

I. THE DEMOGRAPHICS OF THE INDUSTRY UNDERSCORE THE IMPORTANCE OF THE ISSUE
TO WINERIES

Wine is enjoying a period of tremendous growth in the United States. Consumer interest is fueling high demand, supporting increases in vineyard acreage and wine production which, in turn, allows existing wineries to grow in size and new wineries to be established. During this growth, the industry remains very much “90-10” in profile: 90 percent of the country’s wine is produced by 10 percent of the wineries. This serves to illustrate that the majority of America’s wineries are small in size,

and sell primarily to a select market of customers who often have visited the winery and retain an active relationship.

II. THE ISSUE IS CONSUMER-DRIVEN AND NATIONAL IN SCOPE

Wine is a very complex—occasionally intimidating—subject and beverage. Through promotion efforts and media exposure, wineries are able to gain consumer attention and interest. The explosion of communications—especially the presence of the Internet—has provided consumers more information about wineries all over the world than ever before.

Like any business, a winery always wants to satisfy its customers requests. When a consumer learns that wines of interest are not available in local stores. It is very easy for him or her to communicate directly with the winery. When that consumer learns that the winery cannot sell or ship its wines to them they become very frustrated. Wineries and their customers ought to be able to complete these sales with a minimum of difficulty.

The situation is national in scope. It is matrix of the production of wine in 47 states and the presence of consumers everywhere.

III. DIRECT SHIPMENT IS NOT A THREAT TO WHOLESALERS

Wholesalers seem to be convinced that direct shipment is their death-knell. This is hardly the case. Wholesalers are thriving in the thirty states that currently have inter- and/or intra-state direct shipment. It is more convenient and economical to purchase wines from the local retail stores when possible. Consumer orders for direct shipment are focused on hard-to-find wines, or wines from very small wineries that cannot effectively work in the conventional distribution system.

Opponents of direct shipment put forward two primary arguments that are easily addressed. First, is the statement that underage access will be increased. While the perception can be simulated with “stings”, the fact is that states with many years of experience in intrastate shipment to consumers have not received complaints. The suggestion that greater protection is offered against direct shipments to minors by “face to face” sales with the retail sector is challenged by a study conducted by the Department of Health and Human Services that show 50 percent of 18–20 year olds consume alcohol at least once a week. Clearly these underage citizens are obtaining their beverages through the three-tier system, and needn’t face the higher cost, risk and delay of direct shipments.

The second opposition argument is that direct shipments are an effort to evade taxes. Wineries are ready and willing to pay applicable state excise and sales taxes. The state need only establish a mechanism, as New Hampshire and Louisiana have already done. The Electronic Commerce Tax Commission is poised to address the tax collection system for all interstate commerce, and can easily include wine in its deliberations.

Wineries view direct shipment of wine as a supplement to the three-tier system, not a substitution. Direct shipment allows the very small wineries to generate a customer base outside their immediate home market, to grow and develop into a viable brand that a wholesaler will want to represent. This mechanism also allows larger wineries to respond to customers who seek special bottlings or older vintages that are too small in volume to distribute through their distribution network.

IV. BALANCE IS REQUIRED IN CONSIDERING THE LEGISLATION BEFORE THE COMMITTEE

We view the potential of adding federal jurisdiction over state laws through the Webb Kenyon Act a major change in the delicate balance of the political solution that ended prohibition. The draft legislation under consideration by the Committee allows significant expansion of states’ ability to regulate business in other states and will be subject to abuse. Congress should not alter the balance between the protections of competition conferred by the Commerce Clause and the regulatory needs embodied by the 21st Amendment. If Congress believes it is necessary to control undesirable commerce it should not harm negotiations, on a state-by-state basis, to continue in a manner that permits wineries and their customers to conduct business.

In 1933, the antidote to widespread bootlegging was not greater enforcement of unpopular laws. It was legalization and regulation under the auspices of the 21st Amendment. If direct shipment of wine is viewed as “widespread bootlegging”, then today’s antidote should be establishing reasonable market access for limited shipments of wine to consumers by United States wineries.

On behalf of the member wineries of the American Vintners Association, and the millions of responsible wine consumers throughout our nation, I am hopeful that

you will be fair, will encourage competition, and will seek a balanced resolution of this issue.

Sincerely,

SIMON SIEGL,
President.

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