



## **WineAmerica Newsletter – February 2010**

### **From The President's Desk**

#### **Taxation**

I was struck by the lack of business understanding in a recent *Washington Post* editorial calling for a large increase in alcohol excise taxes in Maryland. A significant tax increase on particular businesses or products and the corresponding reduction in demand wreaks great havoc and dislocation – undermining investments, harming the stability of operators and causing collateral damage to the economy. The *Post* cited a comprehensive review by two Johns Hopkins professors estimating that a catchy “dime a drink” tax would lead to a 5% reduction in consumption.

Whether or not the conclusion of these academics is correct, what was missing from the *Post* piece was comprehension of how the suggested policy would undermine the entire Maryland wine market both for out-of-state and local businesses. It would be disastrous in a variety of ways to reduce demand 5% overnight. Wine production is inextricably linked to vineyard investments. A change in the demand for one affects the price of the other. It is no mistake that wine grapes are called a specialty crop, when it comes to commercial utility, wine is really the only product that can be produced profitably from grapes. If you use tax policy to sharply cut demand for wine, you not only put wineries at risk, you also undermine grape growers since a small surplus often leads to a disproportionate reduction in price.

Wine sales are also a major profit component for the restaurant trade—businesses which have been severely hurt by the recession. Further damaging these businesses is also quite counterproductive.

Given the taxes generated by employment in vineyards, wineries, restaurants and the sales taxes collected on sales to Maryland consumers, it is conceivable that the loss of economic activity engendered by the shock of a large wine excise tax increase could easily lead to a net loss in tax receipts to the state. Additionally, the benefits from gains in rural tourism and protection of farm lands which have been associated with the rapid growth of Maryland wineries could easily be lost. There is simply too high a price to contemplate. If Maryland needs additional tax revenues, they should be the result of broad based taxes which will have an even impact on all businesses and spread throughout the economy.

#### **WHO Executive Committee improves Draft Global Alcohol Strategy**

For more than a year WineAmerica has been working with other concerned trade associations and companies to help shape the World Health Organization process as they

***(continued next page)***

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develop a world strategy for addressing alcohol related problems in member states. The first draft strategy which was released in December 2009 was a pretty good document which focused on reductions of harmful use of alcohol rather than all use. Nevertheless, it has been substantially improved by the WHO Executive Board in January which corrected some important details.

These improvements include the following:

- ◆ The Strategy is considered to be non-binding “guidance” on “policy options and interventions” that “could be considered” and “adjusted as appropriate at the national level.”
- ◆ Throughout the document, references now reflect a Strategy and policy focus on reducing “harmful” or “excessive” use and abuse of alcohol, not on consumption or drinking per se.
- ◆ Reference to taxing sales of alcohol in a manner that would eliminate duty free sales, and a proposal to treat alcohol as a “special commodity” (potentially subject to unique trade restrictions) in existing and new trade agreements, were rejected.
- ◆ In major areas of the draft Strategy, private sector “economic operators” are recognized as legitimate stakeholders on par with NGOs.

The substantially improved draft Global Alcohol Strategy will now be forwarded by the Executive Board to the full 192 Member World Health Assembly (WHA) for approval. The WHA will review the draft as part of its meeting May 18-22.

### Consumer Direct Shipping

In January, two U.S. Courts of Appeals issued decisions in wine shipping cases. In the Massachusetts case, the First Circuit Court of Appeals upheld a District Court ruling that a law that largely prevented both in-state and out-of-state wineries producing more than 30,000 gallons annually from obtaining direct shipping permits, was unconstitutional. Even though the law was seemingly crafted to be neutral with respect to in-state and out-of-state businesses, the Court found substantial evidence that the Massachusetts legislature was motivated to use the law to favor in-state wineries. The Court also found evidence that the law, in fact, did favor in-state wineries, that the law “altered the competitive balance to favor Massachusetts’s wineries and disfavor out-of-state competition by design.”

In another important decision, the Fifth Circuit Court of Appeals allowed Texas to enforce its retailer direct shipping law that permitted only in-state retailers to ship to local consumers. The Court found that prohibiting out-of-state retailers from shipping to Texas consumers was constitutional because of the structure of Texas’ distribution system. In the Courts words, “[t]he producers in a three-tier system often are not located in the State in which the sales occur...The wholesalers and retailers, though, are often required by a State’s law to be within that State. The distinction is seen in Texas law.”

You can read a more detailed analysis of how these cases may affect winery policy on page 3 of this newsletter.



## Legal Notes—Direct Shipping Litigation Update

By Cary Greene

It has been an active couple of weeks for direct-to-consumer shipping litigation. In the last two weeks, three federal Courts of Appeal—the courts one level below the Supreme Court—have either issued decisions or heard oral arguments addressing the constitutionality of various state laws.

Overall, we are encouraged by the thoughtfulness of the decisions and the care with which the First Circuit and Fifth Circuit Courts of Appeal considered the facts under consideration in those courts. The immediate impact of the decisions will be felt in Massachusetts (First Circuit) and Texas (Fifth Circuit). Long-term, these decisions may have a wider positive impact on how wineries are regulated, though that remains somewhat unpredictable. For now, the real issue is how we can utilize these decisions in state winery policy discussions.

The oral argument heard by the Third Circuit Court of Appeals on February 1 has limited importance for the time being since a decision may be months away. We mention it here because of the peculiar lower court decision that led to it. The case began several years ago as an attempt to open New Jersey to direct shipping. But the District Court decision issued last year had little to do with shipping and a lot to do with winery tasting room rights and licensing fees. We suggested at the time that the decision could lead “winery rights [to] be slowly and unevenly eroded.” See Cary Greene, *Direct Shipping Litigation Turning Into a Pandora’s Box*, WineAmerica Newsletter (November 2008). This remains a concern, but we are hopeful that the Third Circuit will mitigate this danger by reversing the lower court decision.

More critical for now, the court opinions in the First Circuit and Fifth Circuit offer valuable tools and useful reminders in the fight for improving state winery policy. While there has been some talk in the press that the First Circuit decision means producer size eligibility restrictions are unconstitutional, this isn’t so obvious from the decision itself. Size eligibility restrictions are often used by states and the federal government to limit who qualifies for a statutory privilege. In the First Circuit case, the size restriction was part of a Massachusetts law that allowed wineries producing less than 30,000 gallons annually to qualify for a direct shipper permit without restriction. The federal small winery tax credit for wineries producing less than 250,000 gallons annually is another example of a statutory size eligibility restriction.

WineAmerica’s approach, reflected in the amicus brief we joined in the First Circuit case, is that size eligibility restrictions are useful and Constitutional in some contexts, such as the federal small winery tax credit. We also believe that size restrictions are unconstitutional where they are used, as in Massachusetts, as a facially neutral subterfuge for in-state favoritism.

In the decision, the court highlights that the problem with the Massachusetts size restriction wasn’t the restriction itself, but the fact that the “advantages afforded” by it bore “little relation to the market challenges caused by relative sizes of the wineries.” In other words, barriers were being lowered for small Massachusetts wineries—twenty-seven of thirty-one wineries in Massachusetts obtained direct shipper permits—but not for

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many smaller out-of-state wineries—only twenty-six shipper permits were issued to out-of-state wineries. The size restriction precisely tracked “the unique attributes of Massachusetts’ own wine industry,” but specifically ignored the market challenges faced by other small wineries. This led the court to conclude that the statute was unconstitutionally protectionist, as it had the purpose and effect of discriminating against out-of-state wineries with few policy reasons for doing so.

The takeaway from the decision is that if states want to use a size eligibility restriction, they must have a valid reason for and means of implementing one. The restriction must mitigate a specific, identifiable problem not just for local businesses, but for all similarly situated businesses located out-of-state. The court even sets up criteria for appropriately defining a small winery depending on the problem that the size restriction is trying to mitigate. As we read it, size eligibility restrictions are preserved as a valid policy choice so long as they respect the legal limits that prevent their abuse.

The recent Fifth Circuit decision, meanwhile, acts as a kind of bookend for the First Circuit opinion by addressing when an alcohol beverage law is presumptively valid. While the decision dealt with retailer direct-to-consumer shipment, the principals expressed by the court could have a more general application. The Fifth Circuit begins with the premise that alcohol beverage laws are Constitutionally suspect *only* when they dictate something that is “*not inherent* in the three-tier system.” (emphasis added). What this means is that states are entitled to establish limitations on how local producers, wholesalers and retailers are licensed and operate. It also means that states are *never* required to give “dramatically greater rights” to out-of-state businesses, only to level the playing field for interstate commerce.

Reading into the court’s underlying logic, local winery privileges, such as tasting room privileges, are presumptively valid even though they are not extended to out-of-state wineries. These rights principally derive from geography and licensing and not intent to discriminate. They are also “inherent” to a local winery’s agricultural and three-tier function as evidenced by the fact that *every* state that has a three-tier system also grants these privileges *exclusively* to local wineries.

The court’s perspective is both practical and multilayered. Courts should not mandate that out-of-state wineries be given in-state winery privileges because, in the hands of an out-of-state business, these privileges are substantively different. A “tasting room” operated by an out-of-state winery is nothing more than a retail wine bar. Such “tasting rooms” would afford out-of-state wineries “dramatically greater rights” than local retailers, since presumably they wouldn’t be bound by the same licensing or three-tier restrictions.

While the effect of these decisions is limited for now to the states within the respective Circuits, they may become a template for other Circuits weighing the same or similar questions. This would probably be a good thing. Reasonable, coherent, and largely positive Court of Appeals decisions that provide structure for how the law works would mitigate the need for additional Supreme Court review. Such decisions could provide a clearer picture of what constitutes constitutional wine policy while leaving the interests of wineries largely protected. Let’s hope the other Circuits follow their example.



## Majority of Both Maryland's Houses Sponsor Direct Wine Shipping Law

*Modified from a Marylanders For Better Beer & Wine Laws Press Release dated February 2, 2010*

On Wednesday, February 3, the consumer advocacy group, Marylanders for Better Beer & Wine Laws (MBBWL), will be holding a press conference in Annapolis to announce that, for the first time ever, the bill has secured a majority of sponsors in both the House of Delegates and State Senate. The bill would allow both wineries and retailers to ship up to 24 cases of wine to a Maryland resident per year and follows other states in requiring age verification and tax collection. There are roughly 6,500 wineries in the US. Only about 15% of these wineries can currently sell their product into Maryland. Should the legislation become law, the estimated economic benefit to Maryland would be \$1.5 million per fiscal year, largely from the collection of Maryland sales and excise tax.

The bill's lead sponsor in the House is Carolyn Krysiak (D-46), a veteran Baltimore City Delegate and member of the House Economic Matters Committee, where the bill will receive its hearing. "In all my years in politics, I have never seen a truer example of a grass roots consumer issue take hold to this degree," said Del. Krysiak. The companion bill in the Senate is being introduced by Senators Jamie Raskin (D-20) from Montgomery County and Catherine Pugh (D-40) from Baltimore City. "Democrat, Republican, Independent, consumer, businessperson, winemaker—everyone who calls my office says the same thing. Let's grow up and give the people of Maryland the same freedom of choice to purchase wine and have it shipped to them that hundreds of millions of Americans enjoy. Especially in this time of scarce public dollars, it is unconscionable to allow neighboring jurisdictions to capture the revenue from wine sales that is rightfully ours. 2010 is our year to make it happen," said Raskin.

Despite the overwhelming support of House and Senate members, the Maryland State Farm Bureau and wineries, retailers and consumers throughout the State, the fate of this bill is still far from guaranteed. The legislation must still go through the two respective committees that hear all alcohol bills—the Senate Education, Health and Environmental Affairs Committee and the House Economic Matters Committee—before it can pass to the full House and Senate floors for a vote.

You can find out more about the press conference and MBBWL at:

<http://www.mbbwl.org/>



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### WineAmerica & Wine Grape Growers of America Policy Conference

#### Sunday, March 14

11:00-5:00 PM	<b>Executive Committee Meeting</b>
2:30-5:00 PM	<b>WGA Meeting</b>
5:00-7:00 PM	<b>WA/WGA Informal Welcome Reception</b>
7:00-10:00 PM	<b>No-Host Dinner</b>

#### Monday, March 15

7:30-8:00 AM	<b>Conference Registration</b>
8:00 AM	<b>Joint WGA and WineAmerica Policy Session</b>
8:00-8:20 AM	<b>Welcoming Remarks</b> <ul style="list-style-type: none"><li>• Pete Downs, Kendall-Jackson- Chairman, WineAmerica</li><li>• Ron Bitner, Bitner Vineyards- Chairman, WGA</li></ul>
8:20-11:45 AM	<b>Policy Issues &amp; General Discussion</b>
9:00- 9:40 AM	<b>Immigration Reform and Clean Plant Network-</b> Craig Regelbrugge, American Nursery and Landscape Association
9:45- 10:30 AM	<b>TTB Policy Update and Industry Relations-</b> Susan Stewart-Evans, Executive Liaison for Industry and State Matters, TTB
10:30-10:45 AM	<b>Break</b>
10:45- 11:15 AM	<b>Potential Petition on Use of the Term “Fortified” and Petition to Allow Vintage Dating of American Wines - Discussion</b>
11:15- 12:00 PM	<b>Lobbying Information Session</b>
12:00-1:30 PM	<b>Policymaker Luncheon- Speaker TBD</b>
2:00- 5:00 PM	<b>USDA Breakout Sessions (at Department of Agriculture)</b>
7:00- 10:00 PM	<b>No-Host Dinner</b>

#### Tuesday, March 16

7:30-8:30 AM	<b>Breakfast</b>
8:30-10:00 AM	<b>Concurrent WGA and WineAmerica Board Sessions</b>
8:30- 11:00 AM	<b>WineAmerica Board of Directors and Membership Meeting</b> <b>Welcoming Remarks, Pete Downs, WineAmerica Chairman</b> <ul style="list-style-type: none"><li>• Roll Call</li><li>• Approval of Minutes</li><li>• Meeting Goals</li><li>• 2010 Board Election Results</li></ul>
9:20- 10:00 AM	<b>President’s Report and Staff Updates</b>
10:00-11:00 AM	<b>Action Items &amp; General Discussion</b>
12:00- 5:00 PM	<b>Hill Visits</b>
6:00- 8:00 PM	<b>“Taste the Wines of America” Congressional Reception – 1302 Longworth House Office Building</b>

#### Wednesday, March 17

7:30 AM	<b>Breakfast</b>
8:00-11:00 AM	<b>State Associations Council &amp; Delegates Meeting</b>
11:30- 5:00 PM	<b>Hill Visits- Continued</b>

## 2010 Wine and Grape Policy Conference WineAmerica and Winegrape Growers of America

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March 14-17, 2010  
**Phoenix Park Hotel**  
520 North Capitol Street, NW  
Washington, DC 20001  
800-824-5419

### Please make your arrangements to attend the 2010 Conference

The annual Wine and Grape Policy Conference in Washington, D.C. is an important opportunity for members of both organizations to discuss and evaluate Federal policy issues of interest to our industry, and to communicate our stances directly to Members of Congress and the Administration. These meetings play an important role in the critical process of relationship building which is central to our mission of favorably influencing policy outcomes. It is also a great opportunity for wine industry leaders from across the country to network with each other in formal and informal settings. We hope that you will join us in March for this very important meeting.

*A detailed agenda can be found on the previous page.*

### Arrangements

#### Hotel:

Call the hotel at 202-638-6900 or toll free at 800-824-5419 and reference the Wine and Grape Policy Conference or use Group Code 13489 to reserve your room. The rates are \$269 for single occupancy and \$299 for double occupancy

Rooms fill up quickly in Washington, so please make your reservations as soon as possible.

*The room block closes February 12.*

#### Registration:

On-line registration is now open:

<http://wineamerica.org/membership/springmeeting.cfm>

or follow same link to get a form. Registration after March 1 will incur a surcharge.

Please contact Michael Kaiser at  
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with any questions regarding the 2010 Wine and Grape Policy Conference.

