[1] This letter expresses the views of the FTC's Office of Policy Planning, Bureau of Competition, Bureau of Consumer Protection, Bureau of Economics, and Northeast Regional Office. The letter does not necessarily represent the views of the Commission or of any indivi

For these reasons, we believe that, if enacted, the bills would enhance consumer welfare and allow New York to meet its other public policy goals.

Interest and Experience of the Federal Trade Commission

The FTC is charged by statute with preventing unfair methods of competition and unfair or deceptive acts or practices in or affecting commerce.[3] Under this statutory mandate, the Commission seeks to identify business practices and regulations that impede competition without offering countervailing benefits to consumers. In particular, Commission staff have often assessed the competitive impact of regulations involving alcohol distribution. For example, the staff has analyzed franchise laws that grant wholesalers preferential contract rights. In Illinois, the staff examined a bill that would have prevented suppliers from terminating contracts with wholesalers except for good cause, and suggested that the bill would harm consumers by limiting suppliers' flexibility in changing distributors.[4] In North Carolina, the staff noted that a bill that would have tightened exclusive territorial arrangements between wineries and wholesalers would likely diminish consumer welfare.[5] Another type of state regulation deters wholesalers from cutting prices. In Massachusetts, FTC staff discussed the consumer benefits of a proposal that would have repealed regulations requiring wholesalers to post prices on a monthly basis and to adhere to those posted prices for an entire month.[6]

FTC staff have also studied the direct shipping issue. In October 2002, the Commission held a workshop to evaluate possible anticompetitive barriers to e-commerce in wine and many other industries.[7] At the workshop, FTC staff heard testimony from all sides of the wine issue, including wineries, wholesalers, and state regulators. The staff also gathered evidence from package delivery companies, the Alcohol and Tobacco Tax and Trade Bureau ("TTB"), and regulators in states that allow direct shipping. Finally, FTC staff conducted the first empirical study of a wine market in a state that banned interstate direct shipping. The study examined the wine market in McLean, Virginia ("McLean study"), and compared the prices and choices that consumers could find in area stores to those available online. The authors chose McLean as a relevant retail area because the socio-economic status of many residents in McLean (and northern Virginia, generally) made it likely that several local bricks-and-mortar outlets would

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[3] Federal Trade Commission Act, 15 U.S.C. § 45.

[4] FTC Staff Letter to Illinois Sen. Dan Cronin (Mar. 31, 1999), at http://www.ftc.gov/be/v990005.htm.

[5] FTC Staff Letter to North Carolina Sen. Horton and Rep. Miller (Mar. 22, 1999), at http://www.ftc.gov/be/v990003.htm.

[6] FTC Staff Statement to the Commonwealth of Massachusetts Alcoholic Beverages Control Commission (June 26, 1996), at http://www.ftc.gov/be/v960012.htm.

[7] Public Workshop: Possible Anticompetitive Efforts to Restrict Competition on the Internet, 67 Fed. Reg. 48,472 (2002). The workshop's homepage is at http://www.ftc.gov/opp/ecommerce/anticompetitive/index.htm, its transcript is at http://www.ftc.gov/opp/ecommerce/anticompetitive/021008antitrans.pdf, and all of the panelists' written statements are at http://www.ftc.gov/opp/ecommerce/anticompetitive/agenda.htm.

cater to sophisticated wine drinkers.[8] In July 2003 FTC staff issued a comprehensive report on the direct shipping issue ("Wine Report"),[9] and in October 2003, the Commission testified at a related congressional hearing.[10]

Analysis of Pending Bills

All three bills would allow out-of-state vendors to ship wine directly to New York residents if those vendors satisfy certain regulatory requirements. Under Senate bill 1192, both out-of-state manufacturers and retailers could obtain an out-of-state shipper's license if those vendors hold a license to sell or manufacture wine in another state, and if that other state affords New York's vendors reciprocal treatment. To obtain an out-of-state shipper's license, vendors must pay an annual fee of $125 and present New York's state liquor authority with a copy of a current license from the other state. A license allows vendors to ship wine directly to New York residents who are 21 years or older.

Senate bill 1192 imposes several requirements on out-of-state shippers. In sending the wine, the shipper must ensure that the delivery package has a conspicuous label noting that the package contains alcohol and requires an adult signature for delivery, and the shipper must require common carriers to obtain an adult signature at the time of delivery. In addition, the shipper must provide the state liquor authority with annual reports that include, among other information, the total volume of shipments into New York and the purchaser's name and birth date. The shipper must pay all state and local sales and excise taxes, keep records for three years, and consent to New York's jurisdiction for enforcement purposes. Finally, the bill gives the state liquor authority the power to suspend or revoke an out-of-state shipper's license.

Assembly bill 9560-A and Senate bill 6060-A have similar provisions, with a few important exceptions. These bills would allow only out-of-state wineries, not retailers, to obtain out-of-state shipper's licenses, and in addition to a license, an out-of-state winery would have to obtain a "certificate of authority" and a "registration as a distributor." The bills also cap wine shipments at two cases per month to any New York resident. Finally, the bills directly require common carriers to verify the age of recipients.

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[8] *See* Wine Report at 18 n.81. It is likely that, in larger markets, bricks-and-mortar retailers may offer somewhat more choices, and that in smaller markets, bricks-and-mortar retailers may offer somewhat fewer choices.

[9] FTC Staff Report, *Possible Anticompetitive Barriers to E-Commerce: Wine* (July 2003), at http://www.ftc.gov/os/2003/07/winereport2.pdf.

[10] *See* Prepared Statement of the FTC Concerning "E-Commerce: The Case of Online Wine Sales and Direct Shipment," Before the Subcommittee on Commerce, Trade, and Consumer Protection of the Committee on Energy and Commerce, United States House of Representatives (October 30, 2003), at http://www.ftc.gov/os/2003/10/031030ecommercewine.htm.

I. The Bills Would Allow Consumers to Purchase a Greater Variety of Wines

The bills would substantially increase the variety of wines available to consumers. Through direct shipping, and particularly through the Internet, consumers can conveniently purchase many wines that are not available in nearby bricks-and-mortar stores. The Internet effectively expands the geographic market by allowing online vendors to compete nationally. An individual online store may feature more products than many bricks-and-mortar retail locations. More importantly, the total number of varieties available online may surpass the total number available in bricks-and-mortar stores that are within a reasonable distance of a particular consumer. As a result, direct shipping can give consumers convenient access to many more wines, including popular labels. Using the *Wine and Spirits* list of the top 50 most popular wines in America, the McLean study found that 15% of the wines available online were not available from retail wine stores within ten miles of McLean. For the bottles that were unavailable in the McLean vicinity, 8 out of 15 came from among the 20 most popular bottles.[11] In addition to popular wines, direct shipping also gives consumers access to thousands of smaller labels from around the country.

Bricks-and-mortar retailers may not have the demand or shelf-space to justify keeping a large variety of wines in stock. According to a trade association, domestic wineries produce approximately 25,000 wine labels, and even in a large market like Illinois, only slightly more than 500 of these labels are available through the three-tier system.[12] Moreover, smaller wineries may be unable to distribute their wines through the three-tier system. One court found that Florida's interstate direct shipping ban "has the practical effect of preventing many small wineries from selling their wine in Florida. This result occurs because it is not cost-effective for the smaller out-of-state wineries to acquire a Florida wholesaler."[13]

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[11] *See* Wine Report, App. A. The FTC's Bureau of Economics contributed to the Wine Report, and the McLean study, which is attached to the report, has been published as Alan E. Wiseman and Jerry Ellig, *How Many Bottles Make a Case Against Prohbition?* (Bureau of Economics, Federal Trade Commission, Working Paper No. 258, March 2003).

[12] *See* Wine Report at 24.

[13] Bainbridge v. Bush, 148 F.Supp.2d 1306, 1311 n.7 (M.D. Fla. 2001), *vacated on other grounds*, Bainbridge v. Turner, 311 F.3d 1104 (11th Cir. 2002).

[14] Dickerson v. Bailey, 212 F.Supp.2d 673, 694-95 (S.D. Tex. 2002), *aff'd*, 336 F.3d 388 (5th Cir. 2003).

> purchase of premium wines and their interstate shipment that have been adopted by a number of States are, I believe, another example of abuse of the regulatory process to protect concentrated economic interests, going far beyond the minimum regulations needed to maintain the integrity of taxation and to protect minor consumers.[19]

Because all three bills permit direct shipping, all would increase competition and allow consumers to find lower prices. Of the three bills, Senate bill 1192 would increase competition the most by allowing out-of-state retailers, as well as wineries, to obtain out-of-state shipper's licenses. This additional competition likely would allow consumers to find even lower prices. The McLean study found that "the lowest online prices overwhelmingly come not from wineries, but from out-of-state retail outlets that have web-accessible inventories."[20]

To provide New York consumers with the greatest benefits, the bills should ensure that licensing procedures for out-of-state vendors are not overly burdensome. For example, to ship into New York, Assembly bill 9560-A and Senate bill 6060-A require out-of-state wineries to obtain a "certificate of authority" and a "registration as a distributor" in addition to an out-of-state shipper's license. All three bills require out-of-state vendors to pay an annual fee of $125. Such restrictions may constrain competition. Depending on the volume of purchases in a state, even seemingly small fees can deter smaller wineries from shipping wine.[21] In addition, some states have created complex licensing procedures and regulations that deter suppliers and package delivery companies from shipping wine to those states. Furthermore, all three bills allow out-of-state vendors to obtain New York licenses only if those vendors are located in states that afford New York's vendors reciprocal treatment. This restriction will prevent some out-of-state vendors from shipping to New York residents, thereby somewhat limiting competition and consumer choice. To obtain the greatest benefits from competition, a policy should ensure that permit procedures, fees, and regulations are reasonably calculated to meet the state's legitimate regulatory goals.

III. States that Permit Interstate Direct Shipping of Wine Generally Report Few or No Problems with Direct Shipments to Minors

Although direct shipping can provide consumers with important benefits, policymakers have expressed concern that direct shipping might exacerbate the problem of underage drinking. As FTC staff recognized in the Wine Report and in other documents, underage alcohol use

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[19] *See* Daniel L. McFadden, Written Statement 1, at http://www.ftc.gov/opp/ecommerce/anticompetitive/panel/mcfadden.pdf.

[20] Wine Report at App. A 25 n.22.

[21] *See* Wine Report at 41.

Of course, the fact that states have received few complaints about direct shipments to minors does not establish that minors are not purchasing wine online. As noted by a Michigan Assistant Attorney General, minors who buy wine online are unlikely to report their purchases to the authorities, and neither the package delivery company nor the supplier may know or care that they are delivering wine to a minor.[29] FTC staff cannot rule out the possibility that minors are buying wine online undetected by state officials.

Nevertheless, the staff is aware of no systematic studies assessing whether direct shipping increases alcohol consumption by minors. FTC staff found only one study that might address the impact of direct shipping of wine on underage drinking. This study examines the impact of "home delivery" of keg beer and other alcohol on underage drinking from such traditional retailers such as local liquor stores.[30] Although the study raises important issues of concern, it provides little information upon which to assess interstate direct shipping of wine. The study does not specifically address online sales, interstate direct shipment via package delivery companies, or wine. For example, one of the study's key findings is that "[o]utlets providing delivery services were more likely to sell keg beer." Moreover, the study itself states that "data presented here do not reveal the frequency of delivery use or whether delivery purchases served as a primary source of alcohol," and the study does not assess whether home delivery or direct shipping increases underage alcohol consumption above the level that would occur without those channels.[31]

The data from state compliance checks, or stings, in theory could provide additional evidence on the impact of interstate direct shipping on underage drinking. Several states have conducted stings on interstate direct shipments of wine. Typically in these stings, states provide a minor with a credit card to see whether the minor can purchase wine online, and whether the supplier or package delivery company will refuse to deliver it to the minor. These data, however, are also inconclusive. Stings and anecdotes have shown that minors are able to buy wine online, but there are not enough data from which to conclude that minors can buy wine more or less easily online than offline. For instance, Michigan found that "[a]bout one in three websites contacted" (roughly 33%) agreed to sell alcohol to the minor with no more age verification than a mouse click, and that UPS delivery people did not properly verify the recipients' ages.[32] On the other hand, New Hampshire has run compliance checks in the past but

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[29] *See* Testimony of Irene Mead 196, at http://www.ftc.gov/opp/ecommerce/anticompetitive/021008antitrans.pdf.

[30] Linda A. Fletcher et al., *Alcohol Home Delivery Services: A Source of Alcohol for Underage Drinkers*, J. STUD. ALCOHOL 61: 81-84 (2000).

[31] The National Academy of Sciences cites this study, and only this study, for the proposition that "[s]urveys of underage purchase of alcohol over the Internet or through home delivery show that small percentages (10 percent) of young people report obtaining alcohol in this manner." *See* Reducing Underage Drinking: A Collective Responsibility 174-75 (2004). As noted in the text, however, the cited study does not discuss the Internet or sales from out-of-state vendors.

[32] *See* Wine Report at 35.

[33] *See id*. at App. B (New Hampshire letter).

[34] *See id*. (noting a success rate of 30% in bricks-and-mortar

they can readily inspect in-state wholesalers and retailers on-site, run compliance checks, and punish violators with the loss of a license, fines, and other penalties.[37]

States, however, have a variety of legal remedies against out-of-state suppliers that ship to minors. The Twenty-First Amendment Enforcement Act gives state attorneys general the power to bring civil actions in federal court for injunctive relief against out-of-state suppliers that violate the state's liquor laws.[38] At the time the law took effect, in 2000, state authorities agreed that the Act would help them enforce their laws against out-of-state suppliers. The National Alcohol Beverage Control Association ("NABCA"), an association of state regulators, stated that the Act would "provide state governments with an effective tool to use in preventing the illegal interstate flow of alcohol beverages, some of which finds its way into the hands of underage drinkers."[39] NABCA also said that the Act would help states "overcome the jurisdictional hurdles" in enforcing their laws.[40] Finally, TTB, which has authority to revoke a winery's basic permit, will assist states in combating significant violations of state law.[41]

States also can request assistance from other states' alcohol agencies. New Hampshire will punish suppliers licensed in New Hampshire if another state proves that the supplier is shipping wine illegally into that state.[42] Likewise, when officials in Louisiana learn of a violation, they have a duty to notify both TTB and the state that licensed the violator, and to "request those agencies to take appropriate action."[43]

Overall, the evidence shows a few clear results. States that permit interstate direct shipping have adopted various procedural safeguards and enforcement mechanisms to prevent sales to minors. These states generally say that direct shipping to minors currently is not a serious problem, and that they have received few or no complaints about direct shipping to minors. The McLean study suggests that an interstate shipping ban primarily deprives consumers of access to lower-cost sources of high-end, expensive wines, and to a larger variety

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[37] *See* Wine Report at 29-30.

[38] 27 U.S.C. § 122a (2002); Letter from Sheryl L. Walter, Acting Assistant Attorney General, U.S. Department of Justice, to Hon. Dennis Hastert, Speaker, U.S. House of Representatives 2 (May 3, 2001); Bolick v. Roberts, 199 F.Supp.2d 397, 442 (E.D. Va. 2002) (addendum), *vacated on other grounds*, Bolick v. Danielson, 330 F.3d 274 (4th Cir. 2003).

[39] Letter from James M. Goldberg, counsel for NABCA, to Jonathan Rusch, Special Counsel for Fraud Prevention, U.S. Department of Justice 2 (Mar. 19, 2001), attached as an enclosure to the Walter letter.

[40] *Id*. *See also* Wine Report at App. B (noting that Illinois could use the Act).

[41] ATF, Industry Circular No. 96-3, Direct Shipment Sales of Alcohol Beverages (Feb. 11, 1997), at http://www.atf.treas.gov/pub/ind_circulars/ic_96-3.htm.

[42] N.H. REV. STAT. ANN. § 178:14-a(VIII) (2000).

[43] LA. REV. STAT. ANN. § 26:359(G) (West 2001).

of all wines. FTC staff has seen no evidence indicating whether higher prices for these types of fine wines would curtail consumption significantly either among the general populace, minors, or problem drinkers. There is, therefore, apparently no empirical evidence that bans on interstate direct shipping promote temperance. Because New York's bills contain the same types of recommended safeguards as those adopted by states that allow interstate direct shipping and report few problems, it is likely that New York will experience few, if any, problems with direct shipments of wine to minors.

IV. States that Permit Interstate Direct Shipping of Wine Generally Report Few or No Problems with Tax Collection

Some states also have adopted less restrictive means of protecting tax revenues while permitting direct shipping, such as by requiring out-of-state suppliers to obtain permits and to collect and remit taxes.[44] New York's bills incorporate these types of requirements. Of these states, most report few, if any, problems with tax collection. Nebraska, for example, reports that they "have also not, as yet, had any problems with the collection of excise tax[es]."[45] North Dakota reports that "Taxes are collected. No problems to date that we are aware of."[46]

To the extent that states have problems with out-of-state suppliers, they have addressed the problem in less restrictive ways than banning all interstate direct shipping. New Hampshire, for example, works with out-of-state suppliers:

> [T]he State of New Hampshire Liquor Commission collects an 8% fee on all shipments into the State of New Hampshire. When the NH Liquor Commission discovers an improper shipment we contact the company and inform them of the laws in NH. Once the company learns of NH laws they normally get a permit or stop shipping into NH. The NH Liquor Commission is working with out-of-state supplier[s] and encouraging them to obtain a permit.[47]

Furthermore, to the extent that out-of-state suppliers fail to comply voluntarily, states can report problems to TTB or other states, or use the Twenty-First Amendment Enforcement Act. On the other hand, there is no evidence showing that states must ban interstate direct shipping, rather

[44] *See, e.g.*, LA. REV. STAT. ANN. § 26:359(B)(1); N.H. REV. STAT. ANN. § 178:14-a(V); NEV. REV. STAT. § 369.462.

[45] *See* Wine Report at App. B (Nebraska letter).

[46] *See id.* (North Dakota letter).

[47] *See id.* (New Hampshire letter).

[48] *See id*. at 39-40.

[49] *See, e.g.*, Virginia Postrel, *A Look at Wine Sales over the Internet Shows the Price of Some Regulations in the Name of Consumer Protection*, N.Y. TIMES, July 17, 2003, at C2 (criticizing bans on interstate direct shipping as a barrier to e-commerce).

[50] At the workshop, FTC staff examined potentially anticompetitive barriers to e-commerce in many other industries: auctions; automobiles; caskets; contact lenses; cyber schools; online legal services; real estate, mortgages, and financial services; retailing; and telemedicine and online pharmaceutical sales. *See* Workshop Homepage, at

to in-state and out-of-state firms. In reality, though, these requirements impose disproportionate

[52] *See* Prepared Statement of the Federal Trade Commission on Efforts to Combat Unfair and Deceptive Subprime Lending, before the Senate Special Committee on Aging 4-8, February 24, 2004, at http://www.ftc.gov/os/2004/02/02242004subprimelendingtest.pdf.

[53] *See, e.g.*, The Associates, No. 1:01-CV-00606 (N.D. Ga. 2001); First Alliance Mortgage Co., et al., No. SACV 00-964 DOC (Eex) (C.D. Cal. 2000); Mercantile Mortgage Co., No. 02-5079 (N.D. Ill. 2002).

[54] *Cf. Swedenburg*, 358 F.3d at 237-38.

[55] *See*