

HOUSE BILL REPORT

2SSB 6823

As Reported by House Committee On:

Commerce & Labor

Appropriations

Title: An act relating to the distribution of beer and wine by wineries and breweries located inside and outside Washington state to Washington retail liquor licensees.

Brief Description: Modifying provisions relating to the distribution of beer and wine.

Sponsors: Senate Committee on Ways & Means (originally sponsored by Senator Kohl-Welles; by request of Liquor Control Board).

Brief History:

Committee Activity:

Commerce & Labor: 2/16/06, 2/22/06 [DP];

Appropriations: 2/25/06, 2/27/06 [DP].

Brief Summary of Second Substitute Bill

- Allows wineries, breweries, and microbreweries in Washington and other states to distribute an unlimited amount of wine and beer of their own production to Washington retailers.
- Allows Washington retailers to contract with common carriers to obtain products directly from wineries, breweries, and microbreweries in Washington and other states.
- Requires the Liquor Control Board to convene a task force to review the current regulatory system controlling the sale and distribution of beer and wine, and make recommendations about any proposed changes to the system by December 15, 2006.
- Sets an expiration date of June 30, 2008, for the provisions on direct shipment of wine and beer.

HOUSE COMMITTEE ON COMMERCE & LABOR

Majority Report: Do pass. Signed by 9 members: Representatives Conway, Chair; Wood, Vice Chair; Condotta, Ranking Minority Member; Chandler, Assistant Ranking Minority Member; Crouse, Holmquist, Hudgins, Kenney and McCoy.

Staff: Jill Reinmuth (786-7134).

Background:

Constitutional Provisions

Article I, Section 8, of the U.S. Constitution, commonly referred to as the Commerce Clause, prohibits states from protecting in-state businesses from out-of-state competition, and also from imposing undue burdens on interstate commerce.

The Twenty-First Amendment to the U.S. Constitution ended federal prohibition of the manufacture and sale of intoxicating liquors. It gives states broad authority to control intoxicating liquors.

Three-Tier Systems

Washington and many other states enacted laws establishing "three-tier" systems to regulate the distribution and sale of liquor following ratification of the Twenty-First Amendment.

The general rule of a three-tier system is that producers are prohibited from selling directly to retailers and consumers. They are required to sell their products to licensed distributors, who in turn sell to licensed retailers, who in turn sell to consumers.

An exception to the general rule allows wineries and breweries in Washington to act as distributors and retailers of wine and beer of their own production. There is no limit on the amount of wine and beer that they may distribute to Washington retailers. They may not use common carriers to deliver their wine and beer to Washington retailers. They must comply with applicable laws and rules relating to distributors and retailers.

In contrast, wineries and breweries in other states that hold certificates of approval in Washington must sell their products to licensed distributors, who in turn sell to retailers. Authorized representatives of out-of-state wineries and breweries that hold certificates of approval in Washington are similarly required to operate within the three-tier system. Out-of-state wineries and breweries, as well as authorized representatives, must agree to comply with laws and rules pertaining to liquor sales.

Direct Sale to Consumers

In *Granholm v. Heald* (2005), the U.S. Supreme Court struck down laws in Michigan and New York that allowed in-state, but not out-of-state, wineries to make direct sales to consumers. The Supreme Court concluded that: (1) the Commerce Clause prohibits laws that regulate direct shipment of wine on terms that discriminate in favor of in-state producers; (2) the Twenty-First Amendment does not allow such laws; and (3) such laws do not advance a legitimate local purpose that cannot be adequately served by nondiscriminatory alternatives. The Supreme Court noted that its decision to strike down these laws does not call into question the constitutionality of three-tier systems, and explained that the Twenty-First Amendment protects state policies when they treat liquor produced by in-state producers and out-of-state producers in the same manner.

Direct Distribution to Retailers

In *Costco Wholesale Corp v. Hoen, et al* (2005), Judge Marsha Pechman of the U.S. District Court for the Western District of Washington struck down the Washington laws that allow in-state, but not out-of-state, wineries and breweries to distribute their products directly to retailers. Relying on the Supreme Court's decision in *Granholm*, the District Court concluded that these laws discriminate against out-of-state wineries and breweries in violation of the Commerce Clause. In crafting a remedy, the District Court declined to extend the distribution privilege to out-of-state wineries and breweries or withdraw the distribution privilege from Washington producers. Instead, the District Court stayed the entry of judgment until April 14, 2006, to provide the Legislature with sufficient time to act.

Summary of Bill:

Direct Shipment to Retailers

The following may distribute an unlimited amount of wine and beer of their own production to Washington retailers: domestic wineries, domestic breweries, and microbreweries, and with direct shipment endorsements, certificate of approval holders. (Certificate of approval holders are wineries and breweries in other states.)

Authorized representatives are not allowed to distribute wine and beer to Washington retailers. (Authorized representatives are representatives of wineries and breweries in other states and in foreign countries.)

Washington retailers may purchase wine and beer from distributors, domestic wineries, domestic breweries, certificate of approval holders with direct shipment endorsements, and the Liquor Control Board (Board).

Use of Common Carriers

Washington retailers may contract with common carriers to obtain products directly from domestic wineries, breweries, microbreweries, and certificate of approval holders with direct shipping endorsements.

Jurisdiction

Certificate of approval holders are deemed to have consented to jurisdiction of Washington concerning enforcement of laws relating to liquor licenses, stamp taxes, and sales and shipments of wine and beer.

Price Posting, Reports, and Taxes

Prices posted by domestic wineries, domestic breweries, microbreweries, and certificate of approval holders must be uniform to distributors and retailers on a statewide basis less bona fide allowances for freight differentials.

Certificate of approval holders must report monthly to the Board as to the quantity of wine and beer sold or delivered to Washington retailers. Likewise, Washington retailers are required to report monthly to the Board as to the wine and beer purchased from wineries and breweries.

Domestic wineries, domestic breweries, microbreweries, and certificate of approval holders that are distributing wine and beer of their own production must pay the same taxes on wine and beer that distributors pay.

Public Disclosure

Certain information is exempt from public inspection and copying. This information includes financial or proprietary information supplied to the Board, including: (1) the amount of wine and beer distributed to Washington retailers by domestic wineries, breweries, microbreweries, and certificate of approval holders; and (2) the amount purchased from domestic wineries, breweries, microbreweries, and certificate of approval holders by Washington retailers.

Task Force

The Board must convene a task force to review the current regulatory system controlling the sale and distribution of beer and wine, and make recommendations about any proposed changes to the system by December 15, 2006. The provisions on direct shipment of wine and beer expire June 30, 2008.

Appropriation: None.

Fiscal Note: Available.

Effective Date: The bill contains an emergency clause and takes effect April 14, 2006, except sections 10 and 12, relating to the common carrier and price posting provisions and the public disclosure provision, and take effect July 1, 2006.

Testimony For: There were originally three proposals and a whole cast of characters with different perspectives and approaches. The parties tried to determine what they could live with and without.

There is now an agreement to grant out-of-state breweries and wineries the same privilege as in-state breweries and wineries without limitation. There are concerns about opening up the bill for any amendments. The bill is a compromise. No one got everything they wanted.

Retailers will be allowed to pick up beer and wine, or contract with a common carrier to obtain beer and wine. Retailers must submit monthly reports via an online system, and monthly reports are exempt from public disclosure. Retailers are required to submit monthly reports so the Board can verify sales for purposes of tax collection. The report is due in 2006, so the Legislature has two years to deal with the issues before the provisions expire in 2008.

The distributors support the bill with an amendment specifying that retailers must arrange and pay for the services of common carriers.

The food industry urges that the bill be passed with an amendment deleting the monthly reporting requirement. However, if any changes threaten the bill, we would ask that the bill be passed as is. There have been unlimited shipments by Washington wineries with no reporting requirements by retailers for the past decade, and there have been no problems. There are already five new reporting requirements this year. This monthly reporting requirement would be a burden, especially for small and independent businesses.

Testimony Against: None.

Persons Testifying: Senator Kohl-Welles, prime sponsor; Rick Garza, Liquor Control Board; Ron Main, Washington Beer and Wine Wholesalers Association; Jean Leonard and Robin Pollard, Washington Wine Institute; Joel Benoliel, Costco; Michael Transue, Washington Restaurant Association; Clif Finch, Washington Food Industry; Katie Jacoy, Wine Institute; and Roland Thompson, Allied Newspapers.

Persons Signed In To Testify But Not Testifying: None.

HOUSE COMMITTEE ON APPROPRIATIONS

Majority Report: Do pass. Signed by 30 members: Representatives Sommers, Chair; Fromhold, Vice Chair; Alexander, Ranking Minority Member; Anderson, Assistant Ranking Minority Member; McDonald, Assistant Ranking Minority Member; Armstrong, Bailey, Buri, Chandler, Clements, Cody, Darneille, Dunshee, Grant, Haigh, Hinkle, Hunter, Kagi, Kenney, Kessler, Linville, McDermott, McIntire, Miloscia, Pearson, Priest, Schual-Berke, P. Sullivan, Talcott and Walsh.

Staff: Elisabeth Donner (786-7137).

Summary of Recommendation of Committee On Appropriations Compared to Recommendation of Committee On Commerce & Labor:

No new changes were recommended.

Appropriation: None.

Fiscal Note: Available.

Effective Date: The bill contains an emergency clause and takes effect April 14, 2006, except sections 10 and 12, relating to the common carrier and price posting provisions and the public disclosure provision, and take effect July 1, 2006.

Testimony For: There is a need for both of the distribution bills, to retailers and direct to consumers. They both eliminate the discrepancy with respect to in and out-of-state producers involved in direct delivery. We urge support for this bill. All of the parties involved have come to an agreement that in the long run it is good for producers, retailers, and consumers. There is a need to address the Costco lawsuit. If the bill does not pass, starting April 14, the court will not allow any wineries to ship to retailers. We are asking that the Legislature pass the bill without amendments, as all parties involved have come to an agreement as the bill now

stands. It has been jointly worked and negotiated. Washington retailers are happy to accept the new reporting requirements which are necessary for the amount shipped to match the amount received.

Testimony Against: None.

Persons Testifying: Rick Garza, Washington State Liquor Control Board; Martin J. Durkin, Jr., Costco; Jean Leonard, Washington Wine Institute; and Ron Main and Michael Transue, Washington Restaurant Association.

Persons Signed In To Testify But Not Testifying: None.