UNITED STATES OF AMERICA
FEDERAL TRADE COMMISSION
WASHINGTON, D.C. 20580

Office of Policy Planning
Bureau of Competition
Bureau of Consumer Protection
Bureau of Economics

April 10, 2006

The Honorable Paula Dockery
326 Senate Office Building
404 South Monroe Street
Tallahassee, FL 32399-1100

Re: Comment on Proposed Direct Shipment Legislation

Dear Senator Dockery:

The staff of the Federal Trade Commission's ("FTC" or "Commission") Office of Policy Planning, Bureau of Competition, Bureau of Consumer Protection, and Bureau of Economics[1] is pleased to respond to your invitation for comments on Florida SB 282,[2] which would allow the direct shipment of wine to Florida consumers from manufacturers inside or outside of Florida if certain requirements are met.

We believe that, if enacted, the proposed legislation would enhance consumer welfare and allow Florida to meet its other public policy goals. By allowing interstate direct shipping, SB 282 likely would allow Florida residents to purchase both a greater variety of wines and many wines at lower prices. In addition, by requiring manufacturers to comply with certain regulatory requirements, SB 282 would allow Florida to prevent shipments to minors and to collect taxes on direct shipments. However, if SB 282 is amended to prohibit direct shipping by wineries producing more than 250,000 gallons of wine annually, as you suggest is being considered, such limitation likely would significantly reduce the benefits to competition and consumers that SB 282 otherwise would provide.

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[1] This letter expresses the views of the Federal Trade Commission's Office of Policy Planning, Bureau of Competition, Bureau of Consumer Protection, and Bureau of Economics. The letter does not necessarily represent the views of the Federal Trade Commission or of any individual Commissioner. The Commission has, however, voted to authorize us to submit these comments.

[2] S. 282, 2006 Leg., 108th Sess. (Fla. 2005) (as amended and reported favorably by the Regulated Industries Committee on Mar. 27, 2006) (hereinafter referred to as "SB 282 " or "the proposed legislation").

Interest and Experience of the FTC

The FTC enforces laws prohibiting unfair methods of competition and unfair or deceptive acts or practices in or affecting commerce.[3] Pursuant to this statutory mandate, the Commission seeks to identify and prevent, where possible, business practices and regulations that impede competition without offering countervailing benefits to consumers.[4] The Commission and its staff have considerable experience in analyzing the competitive impact of regulations affecting the alcoholic beverage industry. For example, FTC staff has commented in the past on various restrictions on the vertical relationships between alcoholic beverage producers and wholesalers.[5]

FTC staff also has extensively analyzed the effects of bans on direct wine shipping. In October 2002, the Commission held a workshop to evaluate possible anticompetitive barriers to e-commerce in wine and many other industries ("E-Commerce Workshop").[6] At the workshop, FTC staff heard testimony from several parties with divergent interests, including wineries, wholesalers, and state regulators. The staff also gathered evidence from package delivery companies, the Alcohol and Tobacco Tax and Trade Bureau ("TTB"),[7] and regulators in states that allow direct shipping. In addition, as discussed in more detail below, FTC staff conducted the first empirical study of a wine market in a state that banned interstate direct shipping. In July 2003, FTC staff issued a comprehensive report on the competitive effects of bans on direct shipments of wine ("FTC Wine Report"),[8] and in October 2003, the staff testified at a related

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

4 Specific statutory authority for the FTC's competition advocacy program is found in Section 6 of the FTC Act, under which Congress authorized the FTC "[t]o gather and compile information concerning, and to investigate from time to time the organization, business, conduct, practices, and management of any person, partnership, or corporation engaged in or whose business affects commerce," and "[t]o make public from time to time such portions of the information obtained by it hereunder as are in the public interest." *Id.* § 46(a), (f).

5 *See, e.g.*, Letter from FTC Staff to Ohio State Rep. Bill Seitz (Dec. 12, 2005), *at* http://www.ftc.gov/os/2005/12/051212cmntohiolegiswinefranchis.pdf; Letter from FTC Staff to Cal. State Sen. Wesley Chesbro (Aug. 24, 2005), *at* http://www.ftc.gov/os/2005/08/050826beerfranchiseact.pdf; Letter from Chicago Regional Office to Ill. State Sen. Dan Cronin (Mar. 31, 1999), *at* http://www.ftc.gov/be/v990005.htm; Letter from Atlanta Regional Office to North Carolina State Sen. Hamilton C. Horton, Jr. (Mar. 22, 1999), *at* http://www.ftc.gov/be/v990003.htm; Statement of Phoebe Morse, Dir., Boston Regional Office to the Mass. Alcoholic Beverages Control Comm'n (June 26, 1996), *at* http://www.ftc.gov/be/v960012.htm.

6 Public Workshop: Possible Anticompetitive Efforts to Restrict Competition on the Internet, 67 Fed. Reg. 48,472 (July 24, 2002). The workshop's homepage is at http://www.ftc.gov/opp/ecommerce/anticompetitive/index.htm.

7 The TTB was formerly known as the Bureau of Alcohol, Tobacco, and Firearms.

8 POSSIBLE ANTICOMPETITIVE BARRIERS TO E-COMMERCE: WINE, FTC STAFF REPORT (2003), *at* http://www.ftc.gov/os/2003/07/winereport2.pdf.

congressional hearing.[9] Most recently, FTC staff has commented on proposed legislation involving the direct shipment of wine in New York[10] and Ohio.[11]

The Proposed Legislation

In May 2005, the United States Supreme Court decided *Granholm v. Heald*,[12] holding that the laws of Michigan and New York that discriminated against out-of-state wine manufacturers and in favor of in-state wine manufacturers in the sale and shipping of wine within those states violated the Commerce Clause of the United States Constitution. In August 2005, a federal district court ruled that Florida law similarly violated the Commerce Clause to the extent that it discriminated against out-of-state wineries by prohibiting them from selling and delivering wine directly to consumers in Florida while permitting in-state wineries to do so.[13]

The proposed legislation, which is designed to bring Florida law into compliance with the *Granholm* decision, would allow the direct shipment of wine to Florida consumers from manufacturers inside or outside of Florida if certain requirements are met, including, among others, the following: First, any manufacturer that ships directly to Florida consumers must obtain a direct-shipper's license from the Florida Division of Alcoholic Beverages and Tobacco ("Division").[14] Second, the manufacturer must use an age-verification process that is approved by the Division to ensure that any sale of wine is made to a person at least 21 years of age.[15] Third, the manufacturer must require the signature of a person 21 years of age prior to delivery and include conspicuous labeling on direct shipments indicating that such a signature is

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9 *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 (Oct. 30, 2003), *at* http://www.ftc.gov/os/2003/10/031030ecommercewine.htm.

10 *See* Letter from FTC Staff to New York State Rep. William Magee *et al.* (Mar. 29, 2004) ("New York Letter"), *at* http://www.ftc.gov/be/v040012.pdf. New York ultimately enacted legislation permitting (interstate and intrastate) direct shipping of wine to its consumers. *See* N.Y. Alco. Bev. Cont. Law §§ 79-c, 79-d (McKinney 2005).

11 *See* Letter from FTC Staff to Ohio State Senator Eric D. Fingerhut (Mar. 22, 2006), *at* http://www.ftc.gov/os/2006/03/V060010CommentReOhioSB179DirectShipmentofWine.pdf.

12 125 S. Ct. 1885, 1907 (2005).

13 *See Bainbridge v. Turner*, No. 8:99-CV-2681-T-27TBM (M.D. Fla. Aug. 5, 2005) (order enjoining Florida from enforcing relevant statutes), *at* http://www.law.indiana.edu/webinit/tanford/wine/FLOrder.pdf.

14 SB 282 § 2, at 5-6 (listing requirements for obtaining license, including, among other things, a $100 annual license fee, maintenance of a wine manufacturer's license issued by Florida or another state, and registration of the manufacturer's individual brands with the Division).

15 *Id*. at 6.

required.[16] Fourth, the manufacturer must collect and remit all applicable excise and sales taxes on wines delivered to Florida consumers.[17] Fifth, the manufacturer must file with the Division a bond of $5,000 as surety for the payment of required taxes.[18] Finally, the manufacturer must abide by various reporting and record-keeping requirements.[19] Any violation of these requirements would be punishable by suspension or revocation of the manufacturer's direct-shipper's license or a fine of up to $2,500.[20] Further, a direct shipper that knowingly and intentionally ships, or causes to be shipped, wine to any Florida consumer under the age of 21 would commit a third-degree felony, while a common carrier that knowingly and intentionally delivers wine directly to any underage Florida consumer would commit a second-degree misdemeanor.[21]

Competitive Effects of the Proposed Legislation

Based on extensive research in the area of direct shipping, FTC staff believes that the proposed legislation would enhance consumer welfare. By allowing interstate direct shipping, SB 282 likely would allow Florida residents to purchase a greater variety of wines, as well as many wines at lower prices. In addition, SB 282 would allow Florida to meet its other policy goals. States that have addressed the direct shipping issue typically cite underage drinking and tax collection as the primary concerns raised by direct shipping. By requiring manufacturers to comply with certain regulatory requirements, SB 282 would allow Florida to prevent shipments to minors and to collect taxes on direct shipments. However, if SB 282 is amended to prohibit direct shipping by wineries producing more than 250,000 gallons of wine annually, as you suggest is being considered, such limitation likely would significantly reduce the benefits to competition and consumers that SB 282 otherwise would provide.

A. The Proposed Legislation Likely Would Allow Florida Consumers to Purchase a Greater Variety of Wines

SB 282 likely would substantially increase the variety of wines available to Florida consumers. Through direct shipping, and particularly through the Internet, consumers can

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16 *Id*. at 6-7.

17 *Id*. at 8.

18 *Id*. The Division may reduce the amount of the bond to an amount not lower than $1,000, and any license applicant that has a surety bond for another license on file with the Division that is in excess of $5,000 is deemed to be in compliance with the surety bond requirement. *Id*.

19 *Id*. at 8-9 (manufacturers required to report, among other information, amount of wine shipped to Florida consumers and amount of tax paid thereon; manufacturers required to maintain separate records of wine shipped to Florida consumers and to permit Division to audit records upon request).

20 *Id*. at 9-10.

21 *Id*. at 10.

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. Further, an individual online store may feature more products than many bricks-and-mortar retail locations, as bricks-and-mortar retailers may not have the demand or shelf space to justify keeping a large variety of wines in stock.[22] Moreover, smaller wineries may be unable to distribute their wines effectively through the three-tier (*i.e.*, manufacturer/wholesaler/retailer) system that is mandated in most states. As the Supreme Court recently noted in its *Granholm* decision, "many small wineries do not produce enough wine or have sufficient consumer demand for their wine to make it economical for wholesalers to carry their products. This has led many small wineries to rely on direct shipping to reach new markets."[23]

More importantly, the total number of varieties available online likely surpasses the total number available in bricks-and-mortar stores that are within a reasonable distance of a particular consumer. Consumers are likely to value having a variety of wines from which to choose. One of the most popular wine magazines, *The Wine Spectator*, reviews over 10,000 different wines annually.[24] Further to this point, a Nobel laureate in economics testified at the E-Commerce Workshop that "the value to consumers of direct wine shipments com[es] primarily from access to wines that are not available in their communities."[25] Thus, direct shipping can give consumers convenient access to many more wines, including popular labels and smaller labels from around the country.

As part of its analysis of the impact on consumers of interstate direct shipping bans, FTC staff conducted a study of wine prices and availability in the McLean, Virginia area ("2002 McLean Study").[26] At the time of the study, Virginia prohibited interstate direct shipping. Using the *Wine & Spirits* annual list of the top fifty most popular wines in America, the 2002 McLean

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22 According to a trade association that participated in the E-Commerce Workshop, 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 bricks-and-mortar stores. *See* FTC Wine Report at 24.

23 *Granholm*, 125 S. Ct. at 1892 (citation omitted). *See also Dickerson v. Bailey*, 212 F. Supp. 2d 673, 695 (S.D. Tex. 2002) (finding that the three-tier system "may lock most [out-of-state wineries] out of any access to Texas markets, even if they are willing to take on the additional costs. Such discrimination is especially felt by small, family-run wineries with limited production . . . ."), *aff'd*, 336 F.3d 388 (5th Cir. 2003); Gina M. Riekhof & Michael E. Sykuta, *Politics, Economics, and the Regulation of Direct Interstate Shipping in the Wine Industry*, 87 AM. J. AGRIC. ECON. 439, 442 (2005) ("For small wineries seeking to increase their volume, consumer base, and geographic market, direct shipment prohibitions represent a significant obstacle to growth.").

24 *See* David Sloane, E-Commerce Workshop Written Statement 1, *at* http://www.ftc.gov/opp/ecommerce/anticompetitive/panel/sloane.pdf.

25 Daniel L. McFadden, E-Commerce Workshop Written Statement 2, *at* http://www.ftc.gov/opp/ecommerce/anticompetitive/panel/mcfadden.pdf.

26 The 2002 McLean Study, which is attached to the FTC Wine Report at Appendix A, has been published as Alan E. Wiseman and Jerry Ellig, *Market and Nonmarket Barriers to Internet Wine Sales: The Case of Virginia*, BUS. & POL., Vol. 6, No. 2, Art. 4 (2004).

Study found that 15% of the wines in the sample were available online but not in retail wine stores within ten miles of McLean.[27] Moreover, many of these wines were popular labels. Approximately 53% of the wines that were unavailable in the McLean area came from among the twenty most popular labels.[28] As noted in the FTC Wine Report, these quantitative findings likely understated the impact on variety of the interstate shipping ban. Because the sample was limited to the most popular labels, it excluded thousands of lesser-known labels that bricks-and-mortar stores may not have carried, as well as those that may not have been known to consumers.[29]

Subsequent research by the authors of the 2002 McLean Study confirms the negative effects on variety caused by interstate direct shipping bans. Following the statutory repeal of Virginia's direct shipping ban in July 2003, the study's authors conducted an analysis in 2004 to determine the impact on availability and prices of such repeal ("2004 McLean Study"),[30] using procedures identical to those used in the 2002 study. The findings of the latter study with respect to availability were similar to those of the previous study. That is, 12.5% (as compared to 15%) of the wines in the sample of popular wines were available online but still not in bricks-and-mortar wine stores within ten miles of McLean at the time of the data collection.[31] As demonstrated by these empirical analyses, online sources provide consumers with access to wines that local retail stores do not carry. Adoption of SB 282, therefore, likely would provide Florida consumers with access to a greater variety of wines.

B. The Proposed Legislation Likely Would Allow Florida Consumers to Purchase Many Wines at Lower Prices

Depending on the wine's price, the quantity purchased, and the method of delivery, consumers can achieve substantial savings by purchasing wine online. The 2002 McLean Study found that, excluding shipping costs, wines in the sample cost on average 16% less if purchased online.[32] Because shipping costs do not vary with the wine's price, consumers can save more money on more expensive wines, while less expensive wines may be cheaper in bricks-and-mortar stores. The 2002 McLean Study also found that if consumers use the least expensive shipping method, they can save an average of 8-13% on wines costing $20 or more per bottle and

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27 FTC Wine Report at 18 (excluding wines that could not be found either online or offline, 12 of 79 wines in sample available only online).

28 *Id.* (8 of 15 wines unavailable offline among 20 most popular wines in *Wine & Spirits* poll).

29 *Id.* at 22.

30 *See* Alan E. Wiseman & Jerry Ellig, *Legislative Action and Market Responses: Results of Virginia's Natural Experiment with Direct Wine Shipment* (Dec. 15, 2005) (Mercatus Center working paper), *at* http://www.mercatus.org/pdf/materials/1481.pdf.

31 *Id.* at 12 (9 of 72 wines in sample available only online).

32 FTC Wine Report at 19.

an average of 20-21% on wines costing $40 or more per bottle.[33] In addition, direct shipping lets consumers avoid the cost of spending time to travel to bricks-and-mortar stores.[34]

Moreover, even if consumers choose to buy wine from bricks-and-mortar retailers, direct shipping still encourages price competition between online and offline sources. In states that allow direct shipping, the Internet allows wineries and other merchants, including online retailers, who often have the lowest prices for a particular product,[35] to compete with local bricks-and-mortar retailers. The Internet also helps consumers comparison shop and lets suppliers compete in geographic markets that otherwise may be closed to them, perhaps due to the three-tier system or franchise laws.[36] This competition likely forces down prices. One court found that the ban on interstate direct shipping constituted "economic protectionism, negatively impacting Texas consumers because of more limited wine selection and higher prices."[37] An economist who participated in the E-Commerce Workshop observed:

> [C]onsumers benefit from free markets operated with the minimum government regulation required for consumer protection. . . . The restrictions on direct 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 State taxation and to protect minor consumers.[38]

By allowing direct shipping, SB 282 would increase competition and allow Florida consumers to find lower wine prices. In fact, that conclusion was confirmed in the case of Virginia, which recently repealed its ban on interstate direct shipping. The 2004 McLean Study

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33 *Id.*

34 *See, e.g.*, Clifford Winston, *Conceptual Developments in the Economics of Transportation: An Interpretive Survey*, 23 J. ECON. LIT. 57, 75-77 (1985) (discussing costs of travel time).

35 The 2002 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." FTC Wine Report App. A at 25 n.22. It appears that SB 282, which limits the privilege of direct shipping to "manufacturers" (*see* SB 282 § 2, at 5-6), would not permit such retail outlets to ship directly to Florida consumers. As FTC staff indicated in its March 2004 letter to New York legislators (*see* New York Letter, *supra* note 10, at 7), allowing out-of-state retailers, as well as wineries, to ship directly to consumers would provide additional competition that likely would lead to even lower prices for such consumers.

36 *See generally* American Bar Association, Section of Antitrust Law, E-Commerce Workshop Public Comment (describing various state statutes that may restrict e-commerce), *at* http://www.ftc.gov/opp/ecommerce/anticompetitive/comments/aba.pdf.

37 *Dickerson v. Bailey*, 87 F. Supp. 2d 691, 709 (S.D. Tex. 2000).

38 Daniel L. McFadden, E-Commerce Workshop Written Statement 1, *at* http://www.ftc.gov/opp/ecommerce/anticompetitive/panel/mcfadden.pdf.

found that, following the statutory repeal, online prices were on average 9% lower than offline prices, excluding shipping costs.[39] More importantly, the study found that legalization of direct shipping resulted in a reduction in the differential between online and offline prices, as bricks-and-mortar retailers became more competitive. The differential between average online and offline prices fell by nearly 40% between 2002 and 2004, by one estimate, while the spread between the lowest online and average offline prices fell by 26% during that time, according to another estimate.[40]

C. States Can Satisfy Their Legitimate Concerns About Underage Alcohol Access Without Impeding Competition

Although direct shipping can provide consumers with important benefits, policymakers often express concern that direct shipping might exacerbate the problem of underage drinking. Underage alcohol use is a significant national concern.[41] Nonetheless, states may satisfy their legitimate interest in preventing unauthorized alcohol use by minors without unduly burdening interstate commerce.

In *Granholm*, the Supreme Court rejected the arguments of New York and Michigan that interstate direct shipping bans were justified by concerns over underage drinking. After consideration of the record, including the evidence presented in the FTC Wine Report, the Court concluded that there was no concrete evidence that direct shipping of wine is likely to increase alcohol consumption by minors.[42] Indeed, as the Court noted, direct shipping is an imperfect avenue of obtaining alcohol for minors, who generally want instant gratification.[43] Further, the Court observed that less restrictive means are available to minimize the risk that minors will order wine by mail, citing a Model Direct Shipping Bill developed by the National Conference of State Legislatures that requires an adult signature on delivery and a label so instructing on each

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39 2004 McLean Study at 15. Consistent with the 2002 findings, online savings were smallest for wines priced below $20 (7.6%) and largest for wines priced at or above $40 (21%). *Id.*

40 *Id.* at 17-19. This latter comparison reflects the assumption that, given available Internet search capabilities, a consumer can more readily find the lowest online price for a particular wine than the lowest offline price for such wine. *See id.* at 18 n.38.

41 The FTC is a member of the Interagency Coordinating Committee to Prevent Underage Drinking, a congressionally-mandated working group of federal government agencies seeking to reduce underage alcohol use. The FTC has submitted two reports to Congress addressing alcohol marketing and youth. *See* FTC, *Alcohol Marketing and Advertising: A Report to Congress* (Sept. 2003), *at* http://www.ftc.gov/os/2003/09/alcohol08report.pdf ("2003 Alcohol Report"); FTC, *Self-Regulation in the Alcohol Industry: A Review of Industry Efforts to Avoid Promoting Alcohol to Underage Consumers* App. A (Sept. 1999), *at* http://www.ftc.gov/reports/alcohol/alcoholreport.htm. FTC staff recently initiated a new study of alcohol industry advertising self-regulation. *See* FTC, *Agency Information Collection Activities*, 71 Fed. Reg. 11,659 (Mar. 8, 2006), *at* http://www.ftc.gov/os/2006/03/P064505ProposedInfoRequeststoBeverageAlcoholManufacturers.pdf.

42 *Granholm*, 125 S. Ct. at 1905.

43 *Id.*

package.[44]

State legislative initiatives relating to distribution of alcohol should include effective mechanisms to prevent underage purchases of alcohol, whether online or offline. There are a variety of means to accomplish this goal.[45] SB 282 incorporates several safeguards against direct shipping to minors. It would require the direct shipper to use an approved age-verification process at the time of purchase, as well as conspicuous package labeling indicating that a signature of a person at least 21 years of age is required prior to delivery. Any violation of such requirements would be punishable with suspension or revocation of the direct-shipper's license or a fine of up to $2,500. In addition, a direct shipper that knowingly and intentionally ships, or causes to be shipped, wine to any Florida consumer under the age of 21 would commit a third-degree felony, while a common carrier that knowingly and intentionally delivers wine directly to any underage Florida consumer would commit a second-degree misdemeanor. As a result, SB 282 would allow Florida to satisfy its legitimate interest in preventing sales to minors while facilitating benefits to competition and consumers.

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

SB 282 would require manufacturers to collect and remit all applicable excise and sales taxes on direct shipments of wine to Florida consumers and file with the Division a bond of $5,000 as surety for the payment of required taxes. Of the states permitting direct shipping and collecting taxes therefrom, most report few, if any, problems with such tax collection. Nebraska, for example, reports that they "have also not, as yet, had any problems with the collection of excise tax[es]."[46] North Dakota reports that "[t]axes are collected. [There are n]o problems to date that we are aware of."[47] To the extent that states have problems with out-of-state suppliers, they have addressed such problems in less restrictive ways than banning all interstate direct shipping.[48]

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44 *Id*. at 1906.

45 In the 2003 Alcohol Report, the FTC recommended that operators of Web sites that permit consumers to order alcohol online use age verification technologies that limit sales to consumers demonstrated to be 21 or over. 2003 Alcohol Report at 18 & n.59. In response, the Wine Institute, a trade association representing California vintners, has established mechanisms to facilitate use of such technologies by its members. *See* Wine Institute, *at* http://www.wineinstitute.org/shipwine/.

46 FTC Wine Report App. B (Nebraska letter).

47 *Id.* (North Dakota letter).

48 *See, e.g., id.* (New Hampshire letter) ("[New Hampshire] collects an 8% fee on all shipments into the [state]. 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.").

Furthermore, as discussed in both the FTC Wine Report[49] and the *Granholm* opinion,[50] to the extent that out-of-state manufacturers fail to comply voluntarily with tax (or any other) regulations, states can report problems to TTB, which has the authority to revoke a manufacturer's federal license – necessary to operate in any state – for violating state law, or utilize the Twenty-First Amendment Enforcement Act,[51] which provides state attorneys general the power to bring civil actions in federal court for injunctive relief against out-of-state manufacturers that violate state liquor laws.

Finally, regardless of whether a state permits or prohibits interstate direct shipping, there is no reason to believe that legalizing direct shipping would increase tax evasion. It is unlikely that states would increase illegal interstate direct shipping by creating procedures that would allow out-of-state suppliers to ship legally and pay taxes. If suppliers who currently ship illegally continue to ship illegally, then the level of tax evasion would remain unchanged; however, if some suppliers who currently ship illegally decide to ship legally, then tax evasion would fall. Moreover, if interstate direct shipping increases overall commerce in wine, overall tax revenue likely would rise.[52]

E. Prohibiting Direct Shipping by Wineries Producing More than 250,000 Gallons Annually Likely Would Significantly Reduce the Benefits to Competition and Consumers That SB 282 Otherwise Would Provide

You indicated in your letter of March 21, 2006, that one of the amendments to SB 282 being considered by the Florida Senate would prohibit any winery from shipping directly to consumers if such winery produces more than 250,000 gallons of wine annually, or is owned by a winery that exceeds such annual production. As you stated in your letter, "the effect of the provision would be to exclude a significant number of wineries (in excess of 150 wineries in California alone) from shipping to Florida consumers, while allowing all Florida wineries to ship to consumers."[53]

Although we take no position regarding the constitutionality of such a prohibition in light of the *Granholm* decision, we believe that such a prohibition likely would significantly reduce the benefits to competition and consumers that SB 282 otherwise would provide. In particular,

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49 *See id.* at 39.

50 *See Granholm*, 125 S. Ct. at 1906. The Supreme Court in *Granholm* found the states' tax collection justification for banning interstate direct shipping as unconvincing as the proffered underage drinking justification. *See id.* at 1906-07.

51 27 U.S.C. § 122a (2000).

52 *See* FTC Wine Report at 39-40.

53 As you indicated in your letter, "the reality is that no Florida winery even remotely approaches a production level of 250,000 gallons."

limiting direct shipping in such a manner would reduce the variety of wines that SB 282 would allow Florida consumers to access directly. As discussed in more detail above, direct shipping allows consumers to purchase wines that may not be available in nearby bricks-and-mortar retail stores due to, among other things, limited shelf space at such stores. Although FTC staff has not undertaken a rigorous empirical analysis of the effect of a production-based limitation, information readily available to staff demonstrates the impact on variety that such a limitation would have. For example, a review of the survey of most popular wines of 2005 compiled by *Wine & Spirits* magazine[54] – the same survey utilized in the 2002 and 2004 McLean Studies discussed above – indicates that 25 of the 50 most popular wines are produced by wineries with production in excess of 250,000 gallons per year.[55] Thus, the production limitation being considered would prevent Florida consumers from direct access to half of the most popular wines identified in this prominent survey.[56]

In addition, a production-based limitation likely would reduce the price competition provided by the country's largest wineries. As explained above, consumers can achieve substantial savings by obtaining wine via direct shipping. A production-based limitation would diminish such savings opportunities by preventing direct consumer access to a large number of wines.[57] Further, even if consumers choose to buy wine from bricks-and-mortar retailers, direct shipping fosters price competition between offline and online sources. The contemplated production-based limitation would reduce such price competition, to the detriment of consumers.

Conclusion

The Internet lets consumers purchase an unprecedented array of goods and services from the convenience of their homes. Consumers can find thousands of goods, from thousands of suppliers around the country, and have those goods delivered to their doors. State bans on interstate direct shipping represent the single largest regulatory barrier to expanded e-commerce

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54 *See 17th Annual Restaurant Poll*, WINE & SPIRITS, Apr. 2006, at 82-83.

55 Wineries with production levels greater than 250,000 gallons annually were identified using the following sources: Adams Beverage Wine Handbook 2005, Impact U.S. Wine Market 2005 Edition, Gomberg Fredrickson 2004 Annual Wine Industry Review, and *Wines & Vines*' July 2004 list of the largest U.S. wineries.

56 If one excludes foreign wineries, for which there likely are additional barriers to direct shipping to Florida consumers, the production limitation would work to exclude 25 of the 40 most popular wines in the *Wine & Spirits* survey. In a less objective exercise, *The Wine Spectator* magazine ranked the top 100 wines of 2005 based on quality, value, availability, and "excitement." A review of this ranking indicates that the production limitation would work to exclude at least 4 of the 29 top-rated domestic wines, including the overall wine of the year. *See The Wine Spectator*'s 2005 Top 100, *at* http://www.winespectator.com/Wine/Top100/Top100Intro/0,4148,,00.html (last visited Mar. 27, 2006).

57 As the 2002 McLean Study found, the amount of savings available via direct shipping increases with the price of the wine. *See* FTC Wine Report at 19.

in wine.[58] In states that ban interstate direct shipping, the bans prevent consumers from conveniently and less expensively purchasing wine from suppliers around the country.

Based on our review, FTC staff believes that, if enacted, SB 282 would enhance consumer welfare and allow Florida to meet its other public policy goals. By allowing interstate direct shipping, SB 282 likely would allow Florida residents to purchase both a greater variety of wines and many wines at lower prices. In addition, by requiring manufacturers to comply with certain regulatory requirements, SB 282 would allow Florida to prevent shipments to minors and to collect taxes on direct shipments. However, if SB 282 is amended to prohibit direct shipping by wineries producing more than 250,000 gallons of wine annually, as you suggest is being considered, such limitation likely would significantly reduce the benefits to competition and consumers that SB 282 otherwise would provide. We urge the Florida Legislature to take into account these likely effects on consumers when considering SB 282.

Respectfully submitted,

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58 *Id*. at 14.