



Self-distribution for wineries

Before May 2005, when the U.S. Supreme Court published its decision on *Granholm v. Heald*, both New York and Michigan allowed in-state wineries to ship wine directly to consumers, but prohibited out-of-state wineries from doing so. The Supreme Court ruled that such a prohibition violated the 21st Amendment.

Since that decision was issued, there has been a significant increase in the number of states that allow direct-to-consumer sales from out-of-state wineries. Today, according to the California Wine Institute, 35 states allow sales to consumers allowing wineries access to about 80% of the U.S. population of legal drinking age.

What is self-distribution?

The *Granholm* decision and subsequent litigation around the U.S. (such as *Costco Wholesale Corp v. Hoen*), have made it illegal in many states to provide an unfair advantage to in-state wineries with regard to sales to restaurants and retailers.

Until 2007, wineries that wanted to place their wines in out-of-state restaurants, grocery stores, or wine retail stores had to sell to a wholesaler in that state, who would then sell to the restaurants or retailers. Today, several states allow wineries to act as their own wholesaler under certain conditions. Here is a link for the state-by-state summary of self-distribution compliance requirements:

<http://www.compli-beverage.com/oos/sd/>

In an attempt to secure their position in the three-tier distribution system, wholesalers around the U.S. are trying to block self-distribution. But the Supreme Court notes in the *Granholm* decision that "State policies are protected under the 21st Amendment when they treat liquor produced out-of-state the same as its domestic equivalent. The in-state cases, in contrast, involve straightforward attempts to discriminate in favor of local producers. The discrimination is contrary to the Commerce Clause and is not saved by the 21st Amendment."

The Commerce Clause prohibits states from passing laws that improperly burden or discriminate against interstate commerce. Thus, in states where self-distribution is permitted for in-state wineries but prohibited for those outside the state, legislators have two options: they must either open the state to self-distribution from outside the state or disallow that privilege for in-state producers.

One result of this conflict is that wholesaler associations (in hopes of presenting a united front to legislative bodies) are negotiating with wineries to allow self-distribution, but with a production cap. The cap is large enough to allow most small in-state producers to self-distribute, but small enough to exclude larger producers in California, Oregon, and Washington.

The Losers

There are winners and losers in this contest for control of wine sales. Losers are the wineries in states where self-distribution has recently been outlawed, including Louisiana, Mississippi, Delaware, Kentucky, and Virginia. 160 wineries in Virginia enjoyed self-distribution in their home state until 2005, when the U.S. Court of Appeals for the Fourth Circuit ruled that self-distribution by Virginia wineries was unconstitutional.

In *Wine East* magazine (May/June 2007), Terri Cofer Beirne wrote, "The court's reasoning was consistent with the *Granholm* decision by the U.S. Supreme Court that was soon to come; namely, that a state cannot create a scheme that benefits the in-state industry while burdening the out-of-state industry. Self-distribution by only Virginia wineries, the Fourth Circuit ruled, created an economic benefit for the in-state industry in the form of lower prices. No mandatory use of independent wine wholesalers reduced mark-up, costs, and prices."

Since then, small wineries in Virginia have lost significant business because they have lost access to their customers and wholesalers are unwilling to distribute their wines? However, when this column was written (March-2008), Virginia wineries could see some light at the end of the tunnel.

The Virginia Department of Agriculture has established a nonprofit company called the Virginia Winery Distribution Company (VWDC) that, in essence, will allow wineries to self-distribute under its auspices. To get their wines into restaurants and retailers, participating wineries must act as an agent of the VWDC and share their employees, some physical space, and their delivery vehicles with the VWDC. It is not a simple solution, but it allows the state to prohibit self-distribution by out-of-state wineries while allowing it for in-state wineries.

The Winners

Winners in this situation are the small wineries in states where the wine industry plays a major role in the economy. California, Oregon, and Washington are home to hundreds of small wineries that, in most cases, will not exceed the production caps that are being imposed in other states with self-distribution privileges.

What the future holds

We will continue to see states coming down on both sides of the self-distribution issue. In regions where the wine industry is strong, there may be some contentious battles, like the one in Virginia. New York currently allows self-distribution for in-state wineries, but the powerful wholesalers in that state will challenge any move to extend the privilege to out-of-state wineries. Because *Granholm* did not specifically address self-distribution in New York, the state legislature has not been forced to pass laws allowing it.

Other large markets for wine, such as Florida and Texas, have fewer wineries and are home to major wholesaler players — self-distribution will probably not be allowed in those states.

Washington and Oregon provide the models for self-distribution legislation: there are no capacity caps and no

volume limits. The strength of the wine industry in this part of the U.S. has resulted in liberal laws for direct-to-retail sales. Currently, California does not allow self-distribution for out-of-state wineries. Self-distribution privileges may be extended to those wineries rather than the prohibition of direct-to-retail sales for wineries in California.

Conclusion

We are a long way from dismantling the government-mandated three-tier system of distribution for alcoholic beverages although that is the goal for many in the wine industry. Meanwhile, the changes in both direct-to-retail and direct-to-consumer laws around the country are allowing wineries greater access to their customers. The playing field is slowly leveling out. ■

Rachel Dumas Rey is president of Compli, a full service beverage compliance firm in Paso Robles, CA. Prior to establishing Compli in 1997, she worked for the U.S. Department of Commerce's Export Administration in Washington D.C.