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To: The Honorable Pamela Beidle, Chair, and Members of the Senate Finance Committee

From: Brad Rifkin, Mike Johansen and Matt Bohle on behalf of Brewers Association of Maryland, Maryland Distillers Guild, and Maryland Wineries Association

Re: SB1041 Priority Legislation for Maryland Alcohol Manufacturers - General Policy Considerations for Legislation

Date: February 22, 2024

The purpose of this memo is to summarize the priority legislation for the Maryland Distillers Guild (MDG), Brewers Association of Maryland (BAM) and Maryland Wineries Association (MWA). As a general matter, the proposed legislation seeks to permanently codify many of the privileges extended to the alcohol manufacturers dating back to 2020, and in some cases bring parity to the alcohol manufactures by granting breweries and distilleries the same privilege(s) that the Maryland General Assembly permanently authorized for Maryland wineries dating back to 2011.

In addition to briefly describing the broad policy considerations for the Maryland General Assembly, the memo also touches on some of the public concerns expressed by opposition to the legislation, notable case law and additional components set forth in the 2024 legislation.

General Description of 2024 Priorities:

1. Permanent Removal of Off-Premises Sales Caps

The bill proposes to permanently remove restrictive off-premises sales caps for certain distilleries and breweries. Without legislation this session, the current law will sunset and revert to pre-existing sales caps on these manufacturers whereby breweries are limited to 288 ounces per off-premises transaction (beer; see 2-207) and distilleries are limited to 2.25 liters per off-premises transaction (spirits; see 2-202).

2. Authorization of Direct-to-Consumer Delivery (Employees Only)

The bill proposes to permanently authorize statewide direct-to-consumer (DTC) delivery of products manufactured by a distillery, brewery or winery. The authorization is limited to delivery by way of an employee only. A distillery, brewery or winery would not be permitted to use 3rd party services like DoorDash, UberEats, etc. Without legislation this session, the current law which permits DTC delivery will sunset.

3. Authorization of Direct-to-Consumer Shipping (Common Carriers)

The bill proposes to permanently authorize statewide direct-to-consumer shipping of products manufactured by a distillery or brewery. The authorization is limited to direct shipping using a common carrier like FedEx, UPS, etc. Notably, the Maryland legislature granted direct shipping for in-state and out-of-state wineries back in 2011. Granting direct shipping rights to distilleries and breweries provides parity to the industry. Without legislation this session, the current law which permits DTC shipping using common carriers will sunset for distilleries and breweries. The law for wineries dating back to 2011 remains unchanged.

Bill Drafting Considerations:

Industry concerns stemming from DTC delivery and shipping privileges have been expressed dating back to the authorization of these privileges in 2020. **In an effort to assuage some of these concerns, the ATCC examined common elements of DTC policy from other states, current case law and reviewed existing Maryland law to make suggestions as to how such a policy could be applied in Maryland.** Most notably, this analysis was used to assist DLS in the drafting of the proposed 2024 legislation to ensure best practices and legal footing for DTC policy should it be authorized permanently.

1. Constitutional Concerns

Concerns have been expressed by all stakeholders (including proponents of the legislation) as to the constitutionality of Maryland's temporary DTC shipping privileges authorized by the General Assembly in 2020 (and in subsequent legislative sessions). Due to the Covid-related impetus of the legislation back in 2020, the General Assembly chose to forgo those concerns and pass legislation to grant DTC direct shipping (common carrier) for in-state distilleries and in-state breweries only.

The question of constitutionality stems from the state's preferential treatment of in-state manufacturers dating back to 2020 and the fear that this preferential treatment is in violation of the dormant commerce clause. These concerns are addressed by creating separate direct shipping permits which may be accessed by in-state or out of state manufacturers utilizing existing limited wholesale licensing and non-resident permitting channels. Doing so ensures the alcohol still technically funnels through Maryland's three tier system and that it does so in a way that achieves parity between in-state and out-of-state entities.

Attached to this memo please find a recent 4th circuit case where the Court affirmed a District Court decision to uphold a North Carolina law that granted in-state retailers direct shipping privileges while barring out of state retailers from the same direct shipping right to North Carolina residents (*B-21 Wines, Inc v. Bauer*, 36 F.4th 214). The importance of *B-21 Wines, Inc. v. Bauer* is that the Court refrained from overturning the North Carolina law despite the preferential treatment it gave to in-state retailers – which the court acknowledged was discriminatory to out-of-state industry participants. In upholding the law, the Court referenced

the state's right to regulate alcohol under the 21st Amendment and that there are situations where there is clear tension between the commerce clause and the 21st amendment whereby a state's right preserves the integrity of its regulatory regime over alcohol takes precedence:

To address a “tension” between the dormant commerce clause and the Twenty-First Amendment, the court used a two-step test. First, the court concluded that the scheme would violate the dormant commerce clause without the Twenty-First Amendment because it facially discriminated against out-of-state interests. Second, it held that in light of the Twenty-First Amendment, the shipping restrictions were constitutional because they were essential to preserving a three-tier system, which is a “legitimate non-protectionist ground. (136 Harv. L. Rev. 2160).

The proposed 2024 legislation was drafted to avoid facially discriminatory treatment of in-state versus out of state manufacturers while also preserving the essential aspects of Maryland's three-tier system alcohol regime as it relates to DTC shipping. Conditioning the qualification of a DTC shipping permit for breweries and distilleries upon those manufacturers obtaining a non-resident dealer's permit (out-of-state) or a limited wholesaler license (in-state) – and satisfying the requirements therein – arguably fulfills the state's right to protect its three-tier system. Lastly, granting DTC delivery (using only employees aged 18 and older and certified by an approved alcohol awareness program in the state) to in-state manufacturers is arguably justified based on the holding of *Bauer and Maryland's* 21st amendment right to preserve the integrity of its three-tier system.

2. Industry Disruption Concerns

Production Threshold and DTC Permit Accessibility: The proposed legislation attempts to alleviate the overarching concern expressed by Maryland's alcoholic beverage retailers and wholesalers. Notably, the retailers and wholesalers have expressed strong opposition to direct shipping. Part and parcel to that opposition is the potential impact on retailers and wholesalers should large macro conglomerates and their affiliated out-of-state manufacturers be able to ship directly to consumers. We acknowledge that the DTC sale of macro brands could pose harm to those tiers. **For that very reason, the bill as drafted bars macro brand accessibility of DTC shipping and delivery by limiting the accessibility of direct shipping and delivery permits to only those in-state and out-of-state manufacturers that qualify for an existing limited wholesaler's license (in-state) or a non-resident dealer's permit (out-of-state). Most importantly, to qualify for the limited wholesaler's license or non-resident dealer's permit, a manufacturer must:**

- **Produce less than 45,000 barrels of beer annually.**
- **Produce less than 100,000 gallons of distilled spirits annually.**

This condition precedent applies to affiliates of macro manufacturing conglomerates. **In essence, should this bill pass with the conditions set forth (including various licensing requirements to ensure the sanctity of the three-tier system), brands like Titos, Johnnie Walker, Patron, etc. cannot be shipped or delivered directly to consumers.**

DTC Quantity Limitation Per Household: Moreover, the bill limits the quantity that any direct shipping or delivery permit holder may sell directly to a household on an annual basis to:

- **Not more than 3,456 ounces of beer to be delivered to a single delivery address in a single calendar year.**
- **Not more than 24 standard 750 milliliter bottles of liquor, or an equivalent amount, to be delivered to a single delivery address in a single calendar year.**

This protection is put in place to further alleviate industry apprehension, while allowing for smaller manufacturers (after obtaining the required wholesale license and corresponding permit) to continue increasing the awareness of their brand through direct-to-consumer sales. The proposed legislation limits shipping or delivery quantities per household.

3. Additional Provisions in Proposed Legislation

- **Application and Fee** – Requires a permit holder to file an application provided by the Executive Director of the ATCC for direct shipping and delivery for beer and liquor. The application fee is set at \$200. This is the same application fee for direct wine shippers. See Alc. Bev. Can. 2-145(a)(4).
- **Annual Renewal Fee** – Sets the renewal fee for a permit at \$200. This is the same renewal fee for direct wine shippers. See Alc. Bev. Can. 2-149(a)(4).
- **Payment of Excise or Sales Tax** - Requires any DTC shipping and delivery permit holder to pay all Excise and Sales Taxes for all alcoholic beverages sold under DTC provisions. Such provisions are applicable to direct shippers of Wine. See Alc. Bev. Can. 2-148(a)(4).
- **Bond** – Requires any DTC shipping and delivery permit holder to post a security bond (for ensuring the payment of excise taxes) in the amount of at least \$1,000. See Tax. Gen. Art. 13-825(b)(3).
- **Reports and Recordkeeping** – Requires any DTC shipping and delivery permit holder to file quarterly reports to the Comptroller. Mandates a three-year recordkeeping requirement for permit holders. Allows for the Comptroller or the Executive Director to audit permit holders. Such provisions are applicable to direct shippers of Wine. See Alc. Bev. Can. 2-148(a)(2), (3), (5), (6), and (7).
- **Common Carriers** – Requires that out of state entities use common carriers, approved by the State, to ship their product – this is the same treatment for direct wine shipping. See Alc. Bev. Can. 2-151 for provisions for Common Carriers. See the reporting requirements for Common Carriers that should also apply to DTC permit holders at Alc. Bev. Can. 2-152.
- **Under 21 Policies/Labeling** – Requires the conspicuous labeling for each delivery or shipment as alcohol, which can only be purchased and received by an individual 21 years or older. There are currently provisions in place for direct wine shipping. See Alc. Bev. Can. 2-148(a)(1)(iii). Also see Alc. Bev. Can. 2-150, which lists the requirements of those that can receive alcoholic beverages and restricts what they can do with them.