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HB 6644 Would End Retail Sales of Alcoholic Beverages by Direct Delivery

By Ryan K. Kauffman

The Michigan House of Representatives recently passed a bill that would prevent retail licensees from making direct deliveries to their customers. Currently, under a rule issued by the Liquor Control Commission, off-premises licensees, both specially designated merchants (SDM) and specially designated distributors (SDD), are permitted to deliver a preordered quantity of alcoholic beverages to a customer. There are, of course, statutes in place that carefully regulate these deliveries to ensure minors cannot make purchases and to ensure that the appropriate taxes are paid.

With these safeguards, direct delivery is a convenient exception to the general rule that retail sales of alcoholic beverages for carry out may occur only at the licensed premises. The exception permits, for example, a specialty retailer to prepare and deliver directly to a customer a holiday gift basket containing a selection of gourmet foods and cheeses along with a bottle of wine. Other retailers rely on the exception to deliver alcoholic beverages to a catered event. While these types of sales may not represent the overwhelming source of revenue for most retailers, they are nevertheless an important component to the on-going operations of many businesses.

However, HB 6644, seeks to end the practice direct delivery by retailers. The basis for HB 6644 appears to be a recent decision by the United States District Court for the Eastern District of Michigan, which held that out-of-state retailers must also be permitted to directly ship to Michigan consumers. The federal district court concluded in September, 2008, that because only Michigan retail licensees were permitted to ship directly their customers, the State's statutory scheme violated the Commerce Clause of the United States Constitution. The Commerce Clause generally prohibits a state from enacting laws and regulations that discriminate against the sale of goods and services by citizens from another state and, thereby, impede interstate commerce.

In fact, in 2005, the United States Supreme Court considered a similar issue in *Granholm v Heald*. In that case, the Supreme Court held that Michigan's then-existing statute, which allowed Michigan wineries to ship directly to customers, but prohibited out-of-state wineries from doing so, violated the Commerce Clause. The recent decision from United States District Court for the Eastern District of Michigan is premised on the rationale of *Granholm v Heald*.

The Courts' decisions highlight two important and competing interests. On one hand, Michigan has a strong interest in maintaining its established three-tier system for distributing alcohol to the public. In essence, the three-tier system, created by Michigan and many other states, requires producers and suppliers to sell only to licensed wholesalers, who then sell to licensed retailers, who, in turn, sell to the public. On the other hand, however, is the federal interest embodied in the Commerce Clause that ensures that goods freely flow through interstate commerce. There is now some question regarding how these competing interests are properly weighed. The issue is whether Michigan's practice of allowing its own licensed retailers (i.e., those with a brick and mortar store in the state) to deliver or ship orders directly to customers discriminates against out-of-state retailers who cannot.

The Legislative Analysis of HB 6644 suggests that if Michigan is ultimately required to allow out-of-state retailers to directly ship alcoholic beverages to customers inside of Michigan, the State's entire three-tier distribution would be in jeopardy. The concern is that mail order and internet sales would soon displace many sales that are currently being made from retail stores. As a result, the Michigan Liquor Control Commission, would have less ability to regulate the retail sale of alcohol to ensure, among other things, that all taxes are collected and accounted for, that underage drinking laws are complied with, and that labeling laws are enforced. HB 6644 attempts to resolve these potential problems by prohibiting both in-state retailers and out-of-state retailers from delivering sales through the mail or other similar means. In this way, HB 6644, if enacted into law, would treat both in-state and out-of-state retailers the same and any potential violation of the Commerce Clause would be eliminated.

However, the "throw-the-baby-out-with-bath-water" approach taken by HB 6644 is overly broad and unnecessary. Instead, it is easily possible to allow Michigan's off-premises retail licensees to continue to deliver preordered quantities of alcoholic beverages to their customers, without destroying the three-tier system and without violating the Commerce Clause.

For example, the Legislature could simply create a new classification of retail licensee for out-of-state retailers. On this point, it is important to note, that with very limited exception, Michigan's retail licensees are required to purchase alcoholic beverages from either the Commission or a licensee authorized to make sales to retailers (i.e., a licensed wholesaler). These same limitations could also apply to an out-of-state retail licensee without violating the Commerce Clause because it would merely treat Michigan retailers and other retailers exactly the same. Consequently, the goal of funneling retail sales through licensed wholesalers would be preserved.

Moreover, because the out-of-state retailer would be required to obtain a licensee, the state could exercise the same oversight over those retailers as it does all of its licensees to ensure that underage sales do not occur and that taxes are paid. Any violations, whether committed by an in-state or out-of-state retailer, would subject the license to revocation. Again, there would be no discrimination.

Finally, the Liquor Control Commission could simply amend its rule that allows direct retail sales to customers to impose a fair quantity limitation. The limit could be set at an amount that would permit most retailers to use direct sales to enhance their business, but also prevent large internet retailers from flooding the market with excessive sales that bypass the three-tier system.

In short, HB 6644 goes too far. The rule allowing direct retail sales is important to many retailers and it should be maintained, in at least some form. Although it is not clear that the Michigan Senate will act on HB 6644 in the lame duck session, the issues underlying the bill's enactment will likely remain, and new legislation could arise next year. Hopefully, if other legislation is introduced in an attempt to deal with the issues related to direct retail, that legislation will take a more tempered approach.

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