



FAKE ALCOHOL AND INTERSTATE E-COMMERCE

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A Report on the Need for States to Evaluate the Risks of Fake Alcohol in Interstate E-Commerce Activity From Alcohol Retailers Direct-to-Consumer Sales in the United States (March, 2020)

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EXECUTIVE SUMMARY

Alcohol beverages are an integral part of our society. On average, each American consumes 2.3 gallons of alcohol beverages each year.¹ Notwithstanding the fact that alcohol can enrich our social occasions, culinary experiences, family gatherings and sporting events, it also poses grave risks to individuals and society as a whole. This paper will address one of these risks: fake or counterfeit alcohol and alcohol products. This specific risk increases with the loosening of state regulations including the advent of retailer direct-to-consumer (DTC) sales.

Past studies have demonstrated that the current three-tier, closed distribution system for alcohol beverages has played an important role in protecting the United States' marketplace from a plethora of fake and counterfeit alcohol beverage products. This transparent and accountable system of alcohol distribution is rooted in a dependable set of laws and rules created after Prohibition and enables regulators to oversee the manufacture, distribution and sale of alcohol to consumers from cradle to grave in the interest of public health and safety. The system also allows the industry to quickly react to and track any product-related problem and remove it from the marketplace.

The world of e-commerce, however, has opened up the introduction of counterfeit or fake products into the stream of commerce around the globe. Government entities from various countries and private sector companies recognize this issue as a major threat to commerce and have joined together to create laws and regulations in response to this crisis.

***"19 Deaths in Costa Rica
Tied to Tainted Alcohol,
Officials Say"***

- The New York Times

Unlike most other fake and counterfeit products found throughout the e-commerce marketplace, fake or counterfeit alcohol poses a far higher risk to public health and safety, as well as to the business of legitimate industry operators. Several countries (not including the United States) have reported serious health risks and deaths attributed to fake alcohol.

In the United States, our federal and state regulatory systems for the alcohol industry have been designed to protect the public from the potential dangers of counterfeit alcohol, as well as the other risks related to unregulated sales.

¹ Wallace, D. (2017, July 20). Gallons of Alcohol Consumed in the United States Per Capita, <https://infographicjournal.com/gallons-of-alcohol-consumed-in-the-us-per-capita/>

The enforcement of alcohol law and rules has always been important to law enforcement and alcohol regulators in the United States. These agencies will have unique challenges if laws are loosened to include the expansion of DTC sales to out-of-state retailers due to limited resources, the inability to regulate business outside their borders and the identification of “bad” actors.

“More than 100 Dead in Indonesia After Drinking Bootleg Alcohol”

- USA TODAY

If these laws and rules are dismantled to allow companies to bypass regulatory safeguards and escape oversight, it would increase the exposure of fake and counterfeit alcohol beverage products to the alcohol industry, specifically to the consumer. Public policymakers, responsible industry members and public health advocates should resist “weakening” of the current safeguards in place to protect the U.S. consumer.

INTRODUCTION

According to the Centers for Disease Control and Prevention (CDC), excessive alcohol use is responsible for about 88,000 deaths a year in the United States, including one in 10 total deaths among working age adults aged 20 to 64 years.² This statistic alone is a stark reminder that alcohol is and should be a regulated substance.

Most people understand that tainted alcohol, especially high alcohol spirituous liquors, can cause serious illness and even death. And fake alcohol is not limited to wine and liquor. Recently, at least two men in Brazil are believed to have died from drinking local craft beer contaminated with a chemical compound used in antifreeze and other products.³ These reports add to the continued need for the common framework of laws in the United States that were put into place to regulate the alcohol industry since Prohibition.

In 2018, there were over 274 million Internet users in the United States and that number is expected to increase to over 317 million in 2023.⁴ With the seemingly ever-increasing use of mobile devices and the Internet, more consumers will continue to use e-commerce each year for reasons that include competitive pricing searches, convenience and delivery directly to their home or business. How do alcohol products fit into e-commerce retail sales? This report looks at some of the significant public health and safety issues that arise when retailers sell alcohol across state lines to consumers via e-commerce.

² Center for Disease Control. *Excessive Alcohol Use. CDC works to reduce the four main risk factors for preventable chronic diseases: tobacco use, poor nutrition, lack of physical activity, and excessive alcohol use.*

<https://www.cdc.gov/chronicdisease/resources/publications/factsheets/alcohol.htm>

³ Eisenhammer, S. (2020, January 15). *Brazil Police Investigate Craft Brewer After Two Poison Deaths,*

<https://www.reuters.com/article/us-brazil-beer-casualties/brazil-police-investigate-craft-brewer-after-two-poison-deaths-idUSKBN1ZE20C>

⁴ Clement J. (2019, December 2). *United States: Number of Internet Users 2017-2023,*

<https://www.statista.com/statistics/325645/usa-number-of-internet-users/>

Other issues, including tax avoidance, defective alcohol product recalls, state alcohol compliance efforts and the lack of state resources to properly combat these issues are mentioned even though they are not the primary focus of the report.

STUDIES ON FAKE ALCOHOL ESTABLISH THE IMPORTANCE OF A REGULATED DISTRIBUTION SYSTEM

This paper is the third in a series of reports prepared under grants from the Center for Alcohol Policy (CAP) examining and documenting the ways in which regulated distribution systems and restrictions protect consumers from fake alcohol or counterfeit alcohol. Unlike the first two studies (described more below), this study is focused on potentially weak entry points in the distribution system for “fake alcohol” or illicit alcohol products to reach consumers.

In 2014, the CAP published an important report, “The ‘Fake Alcohol’ Situation in the United States: The Impact of Culture, Market Economics, and the Current Regulatory Systems” explaining why fewer incidents of counterfeit, contraband, surrogate and fake alcohol products are found in the United States marketplace than those widely reported in other countries.⁵ Incidents of fake alcohol found in the United States were either “moonshine” or “refilled liquor bottles” by on-premises retailers.⁶ Incidents of tainted alcohol like those reported in other countries were not found in the United States due, in large part, to the regulated three-tier distribution system that created a closed distribution system preventing fake, counterfeit, or contraband products from entering lawful commercial channels of commerce. This system continues to succeed today in preventing these types of tainted alcohol incidents and is supported by a vast majority of Americans. A recent survey from the CAP reports that 86 percent of respondents agree that alcohol is a product that needs to be regulated and 82 percent agree that alcohol is different than other products, and therefore should be regulated differently.⁷

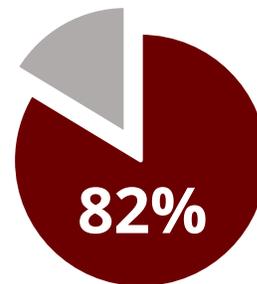
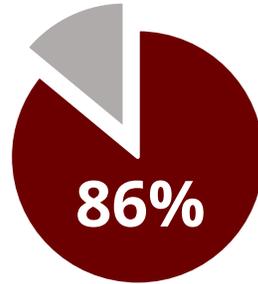
The general population recognizes the need for public health and safety when it comes to the laws and regulation of alcohol products. The understanding that solid regulation for alcohol helps protect consumers is one of the themes of this report.

⁵ Tobiassen, R. (2014). *The “Fake Alcohol” Situation in the United States*, <https://www.centerforalcoholpolicy.org/2014/09/04/new-study-explains-how-alcohol-regulation-prevents-counterfeit-alcohol-in-the-united-states/>. The 2014 Report has been cited by a Federal Court (*Lebamoff Enterprises, et al. v. Snyder, et al.*, Case No. 17-10191 (E, D, Mich. 2018) at page 18. Among other venues, the Report has been presented at an international trade conference (FIVS) in Brussels and at an industry seminar hosted by the Wine and Spirits Trade Association in London.

⁶ Refill incidents by on-premises retailers continue to be a problem in the United States. See, <https://www.safeproof.org/abc-liquor-violations/>

⁷ National Survey: Support for State Regulation Alcohol Bridges Partisan Gap; <https://www.centerforalcoholpolicy.org/2019/05/06/national-poll-shows-support-for-state-regulation-of-alcohol-bridges-partisan-gap/>

Center for Alcohol Policy
National Survey on
Attitudes toward Alcohol
Regulations (2019): 86% of
Americans say alcohol
should remain regulated,
and 82% of Americans
agree that it should be
regulated differently than
other products.



The 2014 report evaluated the three tiers of the traditional distribution system in the United States showing how this system prevents the introduction of these fake products in local commercial channels. The report did not focus on any one tier of the distribution system but identified the totality of the three-tier distribution system as the key for preventing “fake alcohol” or illicit alcohol products from finding its way into the retail marketplace, either on the shelves of off-premises retailers or the back bars of on-premises retailers.

While the 2014 report is helpful to advance the debate on e-commerce and online sales of alcohol beverages, it does not directly address the question of retail sales activities as a weak link posing greater consumer risks for fake or counterfeit alcohol products in the United States. Accordingly, this study updates that report in this regard.

Since 2014, news reports continue to highlight the presence of fake alcohol products in many countries with the accompanying danger and risk to consumer health, safety and lives.⁸ Invariably, these reports emanate from countries which do not have a closed distribution system for alcohol like the United States. Fake alcohol concerns reached a point where the U.S. State Department issued a warning on alcohol consumption risks in Mexico.⁹

The continued reports of fake alcohol incidents internationally show a need for United States public policymakers, legislators, regulators and the judicial branch to be aware of what features and characteristics of the United States’ unique regulatory system mitigate these health and safety risks in the nation’s marketplace.

⁸ Transnational Alliance To Combat Illicit Trade, (2019, September). *Illicit Trade in Alcohol in India, Challenges and Solutions*, https://www.tracit.org/uploads/1/0/2/2/102238034/tracit_-_india_alcohol_report_-_master_copy_-_september_2019.pdf

Swahn, M. (2019, July 8). *Commentary: Vacationers, beware: Bootleg liquor can kill*, <https://www.chicagotribune.com/opinion/commentary/ct-opinion-dominican-republic-counterfeit-alcohol-deaths-20190708-ejccangwi2zbbdgvafw33aygqxy-story.html> and (2019, July 11). *Counterfeit alcohol, sometimes containing jet fuel or embalming fluid, is a growing concern for tourists abroad*, <https://www.pri.org/stories/2019-07-11/counterfeit-alcohol-sometimes-containing-jet-fuel-or-embalming-fluid-growing>

Sampson, H. (2019, July 2). *State Dept. report on allegedly tainted alcohol in Mexico highlights red tape tourists face in emergencies*, <https://www.washingtonpost.com/travel/2019/07/03/state-dept-report-allegedly-tainted-alcohol-mexico-highlights-red-tape-tourists-face-emergencies/>

Jacobo, J. (2019, July 24). *20th person dies of suspected methanol poisoning from tainted alcohol in Costa Rica, officials say*, <https://abcnews.go.com/US/20th-person-dies-suspected-methanol-poisoning-tainted-alcohol/story?id=64548174>

Stuart, R. and Miskelly, G. (2018, June 18). *Fake scotch and tequila are being sold in liquor stores, and you don't need to look far to find it*, <https://www.abc.net.au/news/2018-06-18/fake-alcohol-brands-being-sold-in-australian-bottle-shops/9845350>

⁹ Rutledge, R. (2017, December 29). *Feds warn tourists about tainted alcohol at Mexico resorts*, <https://www.jsonline.com/story/news/investigations/2017/07/26/u-s-state-department-issues-travel-warning-tainted-alcohol-mexico-resorts-after-tourists-blackouts/513563001/>

RISKS TO CONSUMERS FROM VARYING TYPES OF RETAIL ACTIVITIES IN E-COMMERCE

Retail sales activity is usually the main connection point where consumers may obtain fake products. Retailers in this context may be “brick and mortar” stores in the local community, online retailers, online merchandisers or simply a website seller. The latter may be either the e-commerce extension of a “brick and mortar” retailer or an online-only retailer. The online retailer may inventory its products in the state of sale or ship it in from out-of-state or possibly from another country. The online seller may rely on third-party merchants in its state or may rely on third-party entities to fulfill the order from out-of-state or outside of the United States. Additionally, large online retailers may use fulfillment centers to complete the order and in some instances such centers have been identified as the entry point. In a recently published congressional report titled “The Fight Against Fakes,” the Senate Finance Committee found these centers are “providing counterfeiters with an opportunity to penetrate the platform’s supply chain by comingling counterfeits with legitimate goods.”¹⁰

The business models here are numerous.

For example, Amazon is one of the largest retailers in the world. It sources many goods through third parties that ship or deliver directly to the purchasing consumer. In its letter submission for the congressional report titled “The Fight Against Fakes”¹¹ Amazon stated:

“Every day, millions of consumers use Amazon’s website to purchase a wide range of products across dozens of product categories from Amazon and **third-party sellers**. More than 1 million U.S.-based small and medium-sized businesses from every state in the country now sell on Amazon, and **half of the items sold on Amazon worldwide are from small and medium-sized businesses that offer their product through the Amazon Marketplace.**” (Emphasis added.)

As a retailer, Amazon sells some products it may never possess or have in physical inventory. Much of the remainder of Amazon’s letter explains the company’s efforts to prevent fake or counterfeit products from being sold through this business model.

Beyond the business model of Amazon, products other than alcohol have a wide path to get into the stream of commerce. There is no regulation on who can sell, where they source product or quality testing. This “take anything and allow anyone to sell” paradigm for general products is not the rule for alcohol sales.

¹⁰ The United States Senate – Senate Finance Committee (2019, November 7). *The Fight Against Fakes*. [https://www.finance.senate.gov/imo/media/doc/The%20Fight%20Against%20Fakes%20%20\(2019-11-07\).pdf](https://www.finance.senate.gov/imo/media/doc/The%20Fight%20Against%20Fakes%20%20(2019-11-07).pdf) This bi-partisan staff report is the compilation of results, data and survey information sought by the Finance Committee from the private sector. The fact that alcohol beverages are not specifically noted in the report in no way reflects that “fake” and counterfeit alcohol is not available through e-commerce and online, as discussed more in this report.

¹¹ See footnote 10, page 122.

For example, compare this to the in-state retailer that sells alcohol beverages online to consumers through a business model such as Drizly, which is a company that collaborates with retail liquor license holders to help facilitate the ordering and delivery of alcohol beverages to consumers from the retail store. The alcohol beverages have a high degree of authenticity because they were acquired through the three-tier distribution system that is tightly regulated at the federal¹² and State levels. It is a delivery facilitated by e-commerce directly from the retailer rather than a delivery filled by a third party in which the retailer has no knowledge about the true source of the alcohol beverage. Qualitatively these are very different transactions.

HIGH PROPENSITY OF FAKE AND COUNTERFEIT GOODS IN E-COMMERCE

The examination of this qualitative difference is a significant issue for this report. Are these diverse e-commerce channels making it safer for consumers or are they raising greater risks of fake, illicit and counterfeit alcohol beverage products coming to consumers? To assist in evaluating these risks, we need to look at other consumer goods and fake, illicit and counterfeit products because of the limited experience with alcohol beverages in the e-commerce environment.

Current reports from United States government and international organizations confirm the high propensity of fake and counterfeit goods sold through various online third-party retailers. In context of third-party retailers, these are online sales websites of sellers who are not the original producer of the goods.

The aforementioned “The Fight Against Fakes” report by Senate Finance Committee was prepared after a committee investigation, public hearings and review of public letters (released with the 245-page report) from 29 trade associations, companies, platforms, shippers, transporters and payment processors, along with a number of confidential submissions summarized by the committee.¹³ The public letter responses to the 16-pointed questions asked by the committee reveal complex, extensive and expensive investigation and monitoring programs by the private sector to combat fake and counterfeit products and efforts to protect consumers. Yet huge numbers of fake and counterfeit consumer goods are still found in the United States domestic marketplace.

¹² Internal Revenue Code of 1986, Title 26, United States Code, Sections 5121 – 5124, and Title 27, Code of Federal Regulations, Part 31 – Alcohol beverage Dealers. Federal Alcohol Administration Act (1935), Title 27, United States Code, Section 203, and Title 27, Code of Federal Regulations, Part 1 – Basic permit requirements under the Federal Alcohol Administration Act, nonindustrial use of distilled spirits and wine, bulks sales and bottling of distilled spirits.

¹³ See footnote 10, supra.

The United States Government Accountability Office (GAO) issued a report in 2018 titled “Intellectual Property: Agencies Can Improve Efforts to Address Risk Posed by Changing Counterfeits Market” (GAO-18-216).¹⁴ Cosmetics, shoes, travel mugs and phone chargers were ordered from respected retailer websites. Of the 47 items purchased, 20 were determined by manufactures to be counterfeit and all 13 cosmetics were determined to be counterfeit.



The Organization for Economic Co-operation and Development (OECD) has published several reports on illicit goods found in local markets as a result of global trade. “Trade in Counterfeit and Pirated Goods – Mapping the Economic Impact”¹⁵ notes that food and beverages are within the scope of counterfeit and pirated goods. The OECD concluded recently that fake goods represent 3.3 percent of world trade.¹⁶

Within the Executive Branch United States Government, the impact of counterfeit goods in e-commerce is under investigation and study. On April 3, 2019, the President issued a “Memorandum on Combating Trafficking in Counterfeit and Pirated Goods” tasking the Secretary of Homeland Security in coordination with other designated Executive Branch officials to prepare a report and recommendation on the state of counterfeit and pirated goods in the United States with respect to online third-party marketplaces.¹⁷ The U.S. Department of Homeland Security issued a report to the President on January 24, 2020 titled, “Combatting Trafficking in Counterfeit and Pirated Goods.”¹⁸ It is increasingly apparent that counterfeit goods in the marketplace continues to be an important issue and requires a strong, dedicated and ongoing effort to combat these fake goods. The report states:

“Despite public and private efforts to-date, the online availability of counterfeit and pirated goods continues to increase. Strong government action is necessary to fundamentally realign incentive structures and thereby encourage the private sector to increase self-policing efforts and focus more innovation and expertise on this vital problem.”

¹⁴ United States Government Accountability Office (2018, February 27). *Agencies Can Improve Efforts to Address Risks Posed by Changing Counterfeits Market*. <https://www.gao.gov/products/GAO-18-216>

¹⁵ Organization for Economic Co-Operation and Development (2016). *Trade in Counterfeit and Pirated Goods*. <http://www.oecd.org/governance/risk/trade-in-counterfeit-and-pirated-goods-9789264252653-en.htm>

¹⁶ Organization for Economic Co-Operation and Development (2019, March 18). *Trade in fake goods is now 3.3% of world trade and rising*. <https://www.oecd.org/newsroom/trade-in-fake-goods-is-now-33-of-world-trade-and-rising.htm>

¹⁷ Office of the President of the United States (2019, April 3). *Memorandum on Combating Trafficking in Counterfeit and Pirated Goods*. <https://www.whitehouse.gov/presidential-actions/memorandum-combating-trafficking-counterfeit-pirated-goods/>

¹⁸ United States Department of Homeland Security, Office of Strategy, Policy & Plans (2020, January 24). *Combating Trafficking in Counterfeit and Pirated Goods - Report to the President of the United States*. https://www.dhs.gov/sites/default/files/publications/20_0124_plcy_counterfeit-pirated-goods-report_01.pdf

Just a week later, on January 31, 2020, the President issued an Executive Order titled “Ensuring Safe & Lawful E-Commerce for US Consumers, Businesses, Government Supply Chains, and Intellectual Property Rights.”¹⁹ The Executive Order states, “It is the policy of the United States Government to protect consumers, intellectual property rights holders, businesses, and workers from counterfeit goods, narcotics (including synthetic opioids such as fentanyl), and other contraband now being introduced into the United States as a result of the recent growth in e-commerce. The United States Government must also protect the revenue of the United States from individuals and entities who evade customs duties, taxes, and fees.” This report is another recognition of the United States government on the need to protect public health, protect American businesses and to combat the seriousness of counterfeit and fake products within the e-commerce marketplace.

In contrast to the United States, online alcohol beverage sales have been more widely used in the United Kingdom (UK). Consumers in the UK seem to recognize and accept that fake alcohol products are procured through online sales. One report prepared by an accounting and consulting firm in the UK stated that 16 percent of those surveyed would expect to buy fake alcohol products online.²⁰ The UK leads the European Union countries in online alcohol sales.²¹ The UK similarly has been reported as having a significant number of fake alcohol incidents causing death and serious harm to consumers though none of the press reports indicate whether online sales were implicated.

As the states evaluate changes to the regulation and sale of alcohol beverages, the reality of the availability of fake products marketed more easily through online third-party retailers should be a factor in developing a regulatory response and framework. The surge of recent governmental studies on fake and counterfeit products in general e-commerce is aimed at developing corrective methods to prevent these goods from reaching consumers and shows that finding the right solution is of extremely high importance. The increased recognition of dangerous fake goods in other commodities with less regulation must serve as a warning sign for those in charge of alcohol policy that loosening regulations protecting the American consumers and legitimate alcohol industry increases the risks of harm.

¹⁹ Office of the President of the United States (2020, January 31). Executive Order - *Ensuring Safe & Lawful E-Commerce for US Consumers, Businesses, Government Supply Chains, and Intellectual Property Rights*. <https://www.whitehouse.gov/presidential-actions/ensuring-safe-lawful-e-commerce-us-consumers-businesses-government-supply-chains-intellectual-property-rights/>

²⁰ James, M. and Lemon, F (2013, October). *Counterfeit goods in the UK Who is buying what, and why?* https://pwc.blogs.com/files/counterfeitgoodsintheuk_pwc_final_011013-1.pdf at page 12.

²¹ Mileham, A. (2017, April 11). *UK Leads Europe For Online Booze Sales*. <https://www.thedrinksbusiness.com/2017/04/uk-leads-europe-for-online-booze-sales/>

CHALLENGES OF WEAKENING THE REGULATIONS OF ALCOHOL BEVERAGES YET CONTINUING TO KEEP OUT FAKE, COUNTERFEIT AND DEADLY ALCOHOL

Changes in technology have exposed the consumer to an unprecedented number of fakes or counterfeits – fake guarantees, fake services, fake offers and an unlimited universe of fake commodities.

Balanced against the convenience of online orders is the reality of the dangers of purchasing defective and harmful products that are particularly dangerous to consumers. Certain products are particularly vulnerable to fake or counterfeit risks such as cosmetics, pharmaceuticals, toys and vaping equipment, among others. ²²

As stated earlier, counterfeit alcohol perhaps poses one of the most dangerous categories of fake goods. Except for some DTC sales by wineries of wines produced at their own wineries and local deliveries of alcohol by local retailers that are compliant with the three-tier system, alcohol beverages in the United States have not been heavily present in e-commerce to date. The barriers to entry for illegal actors and their products are high. Therefore, it is expected that reports of fake and counterfeit products are minimal under the current alcohol regulatory system and tend to arise from secondary market sales. It is simple to assume that an increased presence in e-commerce will result in a similar presence of fakes or counterfeits as is the experience with the myriad of other consumer goods. Treating alcohol as just another good in the stream of general commerce without regulation will result in a large increase in fake and counterfeit alcohol.

Fake alcohol is not a problem in the United States because of the three-tier system. The three-tier system varies from state to state and is no monolith, but its consistent theme is that it is a closed distribution system. While access to market is robust, unfettered and unregulated access is not. Why? Because the three-tier system regulates those who manufacture, distribute and sell alcohol. The normal theme among all these systems is that federally licensed producers of alcohol sell to federally and state-licensed wholesalers who sell to state-licensed instate retailers who are the point of contact for the consumer. The lack of effective government regulation on alcohol production, distribution channels and sale around the world is a significant public health problem, except in the United States.



United States Three-Tier System of Alcohol Distribution

Reports have shown that illicit alcohol product sales include those that do not comply with regulations and taxes in the countries where they are consumed.

²² See footnote 10.

Those illicit alcohol beverage products are “responsible for hundreds of cases of death and illness due to accidental methanol intoxication, millions of dollars used to fund other criminal activities, and the fiscal loss of billions of dollars in unpaid taxes. Health risks affect the poorest and most vulnerable consumers by contributing to widening health inequalities.”²³

E-commerce of alcohol beverages is slowly expanding both as a result of consumer demand for convenience, pressures of large retailer interests and litigation against traditional state alcohol laws relying on “modern” judicial views of the 21st Amendment.²⁴ The challenge here is for the states to have the ability to evaluate the risks of fake or counterfeit alcohol products by these types of interstate sales in e-commerce and mitigate those circumstances. Because of the serious public health, safety and economic harms from fake and counterfeit alcohol products, the states need to be ready to articulate basic regulatory concerns often lost in the rush to embrace changes in technology. Past experience shows that e-commerce has moved faster than regulators can address in the context of myriad counterfeit products or consumer fraud.

Proper restrictions and regulation of the entire alcohol industry is key in preventing fake alcohol from reaching consumers with its deleterious health effects posing serious public health and safety challenges. Fake alcohol or illicit alcohol encompasses surrogate alcohol where industrial alcohol is improperly and illegally put to a commercial beverage use, moonshine and similar home-made products and counterfeit alcohol including the refilling of brand name bottles with other products.²⁵ More and more look-alike brands of products are appearing as counterfeit goods. Terms such as “unrecorded alcohol” are also used to describe these products.²⁶

A major focus of this report is the issue of whether increased remote sales from retail outlets combined with removal of state laws that prevent counterfeit/fake alcohol will ultimately lead to a situation similar to the offerings of fake and counterfeit consumer goods so widely prevalent in today’s online markets.

²³ Euromonitor International (2018), *Size and Shape of the Global Illicit Alcohol Market*. https://www.tracit.org/uploads/1/0/2/2/102238034/illicit_alcohol_-_white_paper.pdf

²⁴ Chrum A. (2018). *The Online Opportunity for Alcohol Sales*. <https://www.onespace.com/blog/2018/10/online-opportunity-alcohol-sales/>

IBISWorld (2019, July). *Online Beer, Wine & Liquor Sales Industry in the US - Market Research*. <https://www.ibisworld.com/united-states/market-research-reports/online-beer-wine-liquor-sales-industry/>

IWSR (2019, July 2). *The Impact of Ecommerce on Alcohol Trading*. <https://www.theiwsr.com/wp-content/uploads/Press-Release-IWSR-Impact-of-Ecommerce-on-Beverage-Alcohol-July2019.pdf>

²⁵ For purposes of this limited report we will not address the issue of gray market alcohol. Gray markets are situations where a product may in fact be legally produced but created for a different market or under different standards. For example, Corona beer sold in the United States is made in Mexican breweries by Constellation Brands. Corona sold in Europe could be made in InBev breweries in Europe so if those Corona Europe products were resold here, they would be a form of gray market alcohol. Various regulatory restrictions and lower tax rates between countries often create a large incentive for gray market activities across various consumer products.

²⁶ World Health Organization (2018). *Global Status Report on Alcohol and Health*. See generally, Alcohol-Global Status Report on Alcohol and Health 2018 (World Health Organization) at:

<https://apps.who.int/iris/bitstream/handle/10665/274603/9789241565639-eng.pdf?ua=1> The WHO notes the challenge in quantifying and measuring just how bad the fake/counterfeit alcohol market is; “Assessment and monitoring of unrecorded alcohol consumption continues to be a challenge for national monitoring systems.”

This report does not examine in great detail issues of tax compliance with remote sales of alcohol beverage products or how alcohol sales outside the system have potential to create anticompetitive harm to legitimate businesses.²⁷

Having said this, states may, as some have, decide to adopt laws allowing these types DTC shipments of some products by out-of-state retailers and thereby assume the risks from the high propensity of fake products marketed online.²⁸

Good public policy practices should lead those same states to undertake follow up reviews of how well those new legal DTC shipments comply with all state laws. However, states that decide not to enact such laws should not be compelled by the courts to allow DTC shipments because there are sound public policy reasons not to allow these out-of-state shipments to consumers in order to prevent fake or counterfeit alcohol beverages from entering the stream of commerce. This holds true even where in-state retailers are allowed to make deliveries to local consumers.

SHIFTING SUPREME COURT SANDS?

The recent U.S. Supreme Court decision in *Tennessee Wine and Spirits Retailers Association v. Thomas*²⁹ is cited by proponents of DTC retail sales as a green light to allow for the opening e-commerce and online ordering world to alcohol beverages.³⁰ The Supreme Court's holding that a two-year durational residence requirement and other onerous requirements for Tennessee retailers violates the dormant commerce clause because the state failed to prove public health and safety grounds has little to no bearing on whether the state may protect its citizens from the risks of fake or counterfeit alcohol beverages. The deaths reported from incidents around the world from fake alcohol clearly evidences the public health dangers of these products.

²⁷ National Beer Wholesalers Association (2009, March). https://www.nbwa.org/sites/default/files/NBWA_Report_2009.pdf

²⁸ National Association of Wine Retailers (2019, June 6). *Connecticut Consumers Celebrate New Wine Shipping Law*. <https://nawr.org/press-releases/connecticut-consumers-celebrate-new-wine-shipping-law/>

Kostrzewa, D. (2019, June 13). *Connecticut Will Permit Direct Shipping of Wine by Retailers in July*.

<https://www.shipcompliant.com/blog/2019/06/13/connecticut-will-permit-direct-shipping-of-wine-by-retailers-in-july/>

Sovos (2019, September 5). *Out-of-State Wine Shipping Options Expand in Florida*.

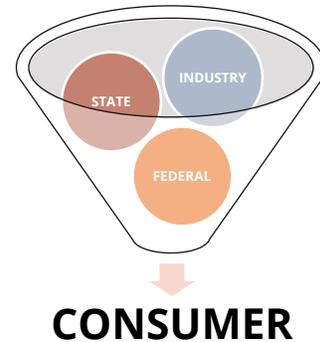
<https://www.shipcompliant.com/blog/2019/09/05/out-of-state-wine-shipping-options-expand-in-florida/> These articles list for wine: Alaska, Connecticut, Florida, Louisiana, Nevada, Nebraska, New Hampshire, North Dakota, Oregon, Virginia, West Virginia, and Wyoming. California, New Mexico, and Idaho are listed as having reciprocal retailer sales arrangements for wine.

²⁹ 139 S. Ct. 2449 (2019).

³⁰ National Association of Wine Retailers (2019). *Tennessee Wine v Thomas*. <https://nawr.org/issues/tennessee-v-byrd/>

CURRENT FEDERAL AND STATE ALCOHOL LAWS THAT HELP PREVENT FAKE/COUNTERFEIT ALCOHOL FROM ENTERING THE MARKETPLACE IN THE UNITED STATES

There are various tools that a state regulator may utilize to help prevent fake and counterfeit alcohol from reaching the consumer. The first step is to have responsible industry members. In the alcohol business that would mean those who abhor the black market and value a controlled and orderly market that supports public policy goals of temperance, orderly markets and tax collection. Without responsible industry members, preventing fake alcohol sales becomes an impossible task.



However, as James Madison once noted, “If men were angels, no government would be necessary.”³¹ The alcohol industry is a great example of that. The regulated alcohol industry operates within a system of defined rules of “do’s and don’ts” because of a historical lack of angels. The black market and bootleggers and fraudsters need to be identified and their illegal activities stopped in order to protect the public health and the legitimate alcohol industry. The regulated industry needs to know the government will assist in stomping out illegal actors. The responsibility put on industry by law helps public health. For example, if a wholesaler observes alcohol they did not provide in a retail account, they can report this violation to the state regulator who would issue a citation to that retailer for a violation of state sourcing laws. Because of the work of government regulations in the United States, the global problems mentioned earlier in this report and previous CAP studies have not happened here.

The federal and state governments are two key gatekeepers and provide protection for the public by regulating the alcohol industry. Their regulatory regimes seek to provide sunshine on the products and the business operators profiting from the sale of alcohol and protect public interests in fair, stable markets that collect taxes while limiting excessive sales and consumption.

Some examples of federal laws that help combat the availability of fake/counterfeit alcohol products include:

- Must have a federal permit to make wine or distilled spirits. Federal Alcohol Administration Act 27 USC 203 (b)
- Must have a federal permit to import alcohol. 27 USC 203(a)
- Must have a federal permit to wholesale/purchase for resale any form of alcohol. 27 USC 203(c)

³¹ The Federalist #51

- Must comply with bottling, packaging and label regulations for each product. 27 USC 205(e)³²
- Must pay federal alcohol excise taxes. 26 USC 5001, et.seq.
- Suppliers and wholesalers cannot have interest in retailer tier. 27 USC 205 et. seq.
- Identity, ownership, management and control of permit holders must be disclosed. 27 CFR 1.20 et. seq.
- A federal permit is required for each individual plant or premises where any business is conducted. 27 CFR 1.29
- A federal permit must be filed with the U.S. Treasury Department's Alcohol and Tobacco Tax and Trade Bureau for each change of address or business name of the permit holder. 27 CFR 1.40 and 1.41
- Disclosure of producer and place of production regulations. 27 CFR 5.42

Some examples of state laws that help combat the availability of fake/counterfeit alcohol products include:

- Must have license to produce, wholesale or retail alcohol in the state. For example – CO Section 44-3-901(1)(h), C.R.S.
- State law bans one retailer selling to another retailer. For example – AR Admin. Code Title 3, Subtitle C, Section 3.7; CO – Section 44-3-409(2), C.R.S.
- Must have label pre-approval before product being sold. For example – NJ Administrative Code 13:2-33.1; CO Regulation 47-904(F), 1 C.C.R. 203-2.
- Registration of products prior to sale in the state. For example – CO Regulation 47-924, 1 C.C.R. 203-2; N.J.S.A. 33:1-2; N.J.A.C. 13:2-33.
- Alcohol must come to rest in an in-state warehouse before being sold at in-state retailers. For example – CO Sections 44-3-402(1)(b), C.R.S. and 44-3-407(d), C.R.S.
- Must register the sole source of alcohol from importers. For example – CO Section 44-3-901(4)(c)
- Parties must pay state excise tax. For example – CO Section 44-3-503, C.R.S.
- State laws and regulations that ban the sale of certain alcohol products. For example – VA Administrative Code Title 3 Agency 5 Chapter 70 §200; PA Liquor Control Board Regulations Title 40 PA CODE §11.3 A; CA. Bus. & Prof. Code § 23403; FL Code Title XXIV Alcohol Beverages and Tobacco Chapter 565.07; MN. Stat. § 340A.506
- Must file territories and areas of primary responsibility which helps with product recalls. For example – VA Code 4.1-503

³² “In order to prevent the sale or shipment or other introduction of distilled spirits, wine, or malt beverages in interstate or foreign commerce, if bottled, packaged, or labeled in violation of the requirements of this subsection, (1) no bottler of distilled spirits, no producer, blender, or wholesaler of wine, or proprietor of a bonded wine storeroom, and no brewer or wholesaler of malt beverages shall bottle, and (2) no person shall remove from customs custody, in bottles, for sale or any other commercial purpose, distilled spirits, wine, or malt beverages, ... **unless**, upon application to the Secretary of the Treasury, **he has obtained and has in his possession a certificate of label approval** covering the distilled spirits, wine, or malt beverages, issued by the Secretary in such manner and form as he shall by regulations prescribe” 27 USC 205(e)(5)

- Producers must file wholesaler contracts with state. For example-CO. Stat.44-3-402(5), C.R.S.
- State can conduct testing on product. For example – TX Administrative rule 45.85
- Retailer must obey trade practice laws. For example – CO Stat.44-3-308, C.R.S.; CO Regulation 47-322, 1 C.C.R. 203-2.
- Pricing laws regulating what wholesalers and retailers can charge. For example – CT 30-63 et. seq.
- Some states require each truck transporting alcohol to pay a fee, receive and display an insignia. For example – NJ Revised Statute § 33:1-28 (2013)
- Pricing regulations. For example – CT Statute 30-64b; FL Regs. 61A-4.013; CO Section 44-3-409(2), C.R.S.; CO Regulation 47-322(A), 1 C.C.R. 203-2.

Providing exceptions to the three-tier system for certain industry participants (DTC sales from retailers) creates an opportunity for evasion of these protections.

RETAILERS IN-STATE AND RETAILERS OUTSIDE THE STATE – REGULATORY CHALLENGES THAT INCREASE RISK TO PUBLIC HEALTH AND SAFETY OF IN-STATE CONSUMERS AND THE ORDERLY MARKETPLACE

The CAP report from 2017, titled “Combating Fake, Counterfeit, and Contraband Alcohol Challenges in the United Kingdom through the Alcohol Wholesaler Registration Scheme (AWRS)”³³ highlights the fact that off-premises retailers are a source problem for consumer exposure to fake products. A principal purpose of the AWRS is not to question the regulatory integrity of the UK wholesaler distributors but to restrain the sourcing activities of UK retailers to ensure that only authentic and safe products enter the UK retail marketplace that are “duty paid” in the UK (terminology equivalent of tax-paid in the terminology in the United States).

In looking more closely at features of the closed, three-tier distribution system of alcohol beverage commerce, the 2017 report noted retail sales activities are the weakest links that could expose U.S. consumers to these fake alcohol and illicit alcohol products because they are the connection point with consumers in commercial transactions, that is, the final point of distribution. How retailers source their products controls the risk exposure to consumers from fake alcohol or illicit alcohol products. In turn, how well local regulators can regulate the alcohol industry and keep out unlicensed actors directly controls the likelihood of risk of consumers being exposed to unsafe products.

³³ Tobiassen, R. (2017, September). *Combating Fake, Counterfeit, and Contraband Alcohol Challenges in the United Kingdom through the Alcohol Wholesaler Registration Scheme(AWRS)*. (<https://www.centerforalcoholpolicy.org/wp-content/uploads/2017/09/Combating-Fake-Counterfeit-and-Contraband-Alcohol-Challenges-in-the-United-Kingdom.pdf>)

A sale and delivery of alcohol beverages through a fulfillment center business has a higher risk of being a fake or counterfeit product than does a delivery from an in-state alcohol beverage retailer from its inventory that has been acquired through a closed distribution system monitored by the state regulator. The former is a range of product offerings that may be sourced by the seller from many other parties whereas the latter is a retailer-controlled and possessed inventory.

A collateral issue of consumer confusion arises from being able to recognize whether a website offering is from a legitimate retailer given the numerous secondary market sales or offerings within online vendor platforms.³⁴ This challenge confronts state alcohol regulators as well. It has been suggested that providing state regulators a copy of the website seller's retail alcohol license from other states provides adequate protections.

But how does a state alcohol regulatory agency monitor every website accessible to consumers in the state in order to determine whether it is an alcohol beverage seller or a retailer that has complied with the state law? It cannot. And a state is powerless to regulate in another state. However, a state can regulate within its borders where it has access to product inventory, sales records and inspections of wholesale businesses. In addition to responding to complaints from licensees that observe illegal activity in the marketplace, the state regulator is able to conduct inspections of any licensed premises in the state to look for compliance issues.

Setting up a business outside of a state regulator's control is an invitation for law evasion. State regulators have zero to minimal authority or jurisdiction over businesses located in another state. The regulator can send a letter demanding the retailer cease and desist but has no teeth to enforce the demand. In some cases, the challenge for regulators is establishing the true identity of the online retailer. If the online retailer is identified and provided with a cease and desist demand, that seller could start a new website with a different name creating additional struggles to enforce DTC laws. Regulators would be frustrated by a constant "whack-a-mole" enforcement effort.

In-state retailers have licensed premises with inventory to be inspected. This is the reason why the refill violations are uncovered at on-premises locations. A common example of a refill violation is when the on-premises retailer fills an empty alcohol bottle with a less expensive product of the same type of alcohol in order to increase profit. The in-state retailer inventory obtained through the three-tier system is a "closed system" and, therefore, reduces the likelihood of fake and counterfeit products entering the commercial channels. State alcohol regulators do not have this ability to inspect and determine the sources of alcohol beverages sold by out-of-state retail sellers. And even if they did, the sheer magnitude of the number of out-of-state retailers that would need to be monitored would create an enforcement nightmare.

³⁴ The National Association of Attorneys General (2019, October 22). The National Association of Attorneys General recently issued a letter signed by 46 State and Territory Attorneys General to Facebook, Craigslist, and e-Bay seeking their assistance to prevent illegal sales of alcohol beverages in violation of State laws. See, [https://www.naag.org/assets/redesign/files/sign-on-letter/NAAG%20Letters%20Combined%20-%20Online%20Sale%20of%20Alcohol\(1\).pdf](https://www.naag.org/assets/redesign/files/sign-on-letter/NAAG%20Letters%20Combined%20-%20Online%20Sale%20of%20Alcohol(1).pdf)
Distillery Trail (2019, December 23). *Attorneys General Across the U.S. Cracking Down on Illegal Secondary Market Online Sales of Alcohol*. <https://www.distillerytrail.com/blog/attorneys-generals-across-the-u-s-cracking-down-on-illegal-secondary-market-online-sales-of-alcohol/>
See footnote 10; "The Fight Against Fakes" at pages 8, 11, and 86.

U.S. Supreme Court Justice Samuel Alito in his majority opinion in the recent Tennessee Wine and Spirits Retailers Association case noted that states should be able to conduct onsite inspections: “In this case, the argument is even less persuasive since the stores at issue are physically located within the State. For that reason, the State can monitor the stores’ operations through on-site inspections, audits, and the like. See §57–3–104. Should the State conclude that a retailer has ‘fail[ed] to comply with state law,’ it may revoke its operating license.”³⁵

Importantly, the point here is not suggested that alcohol retailers are somehow more inclined to deal with fake alcohol products than sellers of other consumer goods; rather, it is to point out that alcohol beverages in e-commerce are susceptible to fakes and counterfeits much like other commodities because of the way the product offering is sourced. But in terms of public health and safety concerns, fake alcohol products can pose a greater danger to a consumer than a fake or counterfeit designer bag.

For that latter reason, e-commerce in alcohol beverages merits different treatment and under the authority of the 21st Amendment, the states have greater deference in addressing these dangers to protect consumers, collect taxes and maintain an orderly marketplace.

As recent litigation shows, the avenues for consumer options for purchasing alcohol beverage products are being challenged by various business entities in order to add new sales streams not previously available due to laws and rules. The trend toward e-commerce is driving this push in many respects. However, the issue of DTC sales from out-of-state retailers is one of increasing concern for state regulators. Simply put, e-commerce and online orders of alcohol beverages increase the risks of fake or counterfeit products entering distribution channels to consumers. The question is whether certain types of e-commerce and online orders pose greater risks and ones that the states, under their 21st Amendment rights, may prevent in order to ensure an orderly marketplace and mitigate dangers to public health and safety. The 21st Amendment puts alcohol beverages in a completely separate and unique commodity category than any other consumer goods sold in e-commerce and online.

EVALUATING STATES’ ABILITY TO ENFORCE ALCOHOL LAWS IN AN E-COMMERCE WORLD – THE PUBLIC SAFETY ISSUES AND RESOURCES TO COMBAT NON-COMPLIANCE OF STATES’ LAWS AND RULES

The main topic of this report does not detail several other enforcement challenges on public policy issues facing state alcohol regulators from the advent of interstate e-commerce. However, as a former regulator, I would be remiss not to include some of these concerns in this report. Other public safety concerns facing state regulators include underage access to alcohol beverages, trade practice law violations and recalls for defective alcohol beverage products.

³⁵ *Tennessee Wine & Spirit Retailers Association v. Thomas*, 139 S. Ct. 2449, 2475 (2019).

Access to alcohol for consumers under 21 years of age is a serious concern as outlined by the 2018 “Report to Congress on the Prevention and Reduction of Underage Drinking.”³⁶

The report to Congress states, “Underage alcohol consumption is a persistent and serious public health challenge, resulting in thousands of deaths each year through motor vehicle crashes, violence, suicide, alcohol poisoning, and other causes. Underage drinking is also implicated in sexual assault and other crimes, impaired brain function, decreased academic performance, and the increased risk of developing an alcohol use disorder later in life.”

In 2012, a study was published that evaluated alcohol sales to minors through the Internet.³⁷ Results showed of the 100 orders that were placed by underage purchasers, 45 percent were successfully received. The study also revealed the “age verification at delivery was inconsistently conducted and, when attempted, failed about half of the time.” The study showed that concerns about underage alcohol access (via the Internet) was present, even eight years ago. That concern should be even more heightened in our present age.

Some states continue to litigate their right to regulate out-of-state retail e-commerce sales of alcohol differently than in-state retailers. One example is in the state of Michigan that has over 16,000 licensed alcohol retailers within the state and potentially faces 388,000 retailers nationwide.³⁸ Another is in the state of Mississippi where a sting operation involved online alcohol purchases that were delivered to a minor (under 21 years of age) and to the state’s regulatory agency office while not paying the appropriate tax.³⁹ This is an example where access to alcohol beverages for consumers under the age of 21 is expected to increase with the onslaught of DTC retail businesses.

Another data source is retailer data from Nielsen which indicates that there are over 643,000 alcohol retail establishments in the United States.⁴⁰ The resources needed to investigate compliance of alcohol through a fully developed retail e-commerce model are potentially staggering. Most states’ alcohol law enforcement efforts are already stretched to their limits and if they must now attempt to regulate an exponential increase in out-of-state retailers, public health and safety will surely suffer.

³⁶ Substance Abuse and Mental Health Services Administration (2018). *Report to Congress on The Prevention and Reduction of Underage Drinking*. https://www.stopalcoholabuse.gov/media/ReportToCongress/2018/report_main/stop_act_rtc.pdf

³⁷ Williams, R. and Ribisl, K. (2012, September). *Internet Alcohol Sales to Minors*. <https://jamanetwork.com/journals/jamapediatrics/fullarticle/1149402>

³⁸ *Lebamoff Enterprises, Inc., et al. v. Snyder, et al.*, United States Court of Appeals for the Sixth Circuit, No. 18-2199 Brief for Defendants-Appellants, filed October 3, 2019, at pages 7 and 20. It is not clear whether these retailers are both on-premises and off-premises though it is likely they are off-premises retailers who would be positioned to sell to consumers for off-premises consumption.

³⁹ WLBT News (2018, August 14). *Mississippi Cracks Down on Illegal Wine Shipments*. <https://www.wlbt.com/story/37354878/mississippi-cracks-down-on-illegal-wine-shipments/>

⁴⁰ National Beer Wholesalers Association (NBWA) (2018). *The U.S. Beer Industry in 2018*. Nielsen data from the website of the National Beer Wholesalers Association (NBWA) at <https://www.nbwa.org/resources/industry-fast-facts> It is not stated whether these retailer establishments are on-premises and off-premises establishments.

There is an average of 44.3 enforcement agents per state who enforce state liquor laws.⁴¹ If half of the 643,000 retailers in the United States were off-premises retailers, each state would average one agent per 7,257 retailers to enforce the laws and regulations of their state concerning retail DTC purchases. This would add an impossible increase to the states' regulatory responsibility without allocating a substantial increase to resources, which is not always met with open arms from policymakers and legislative bodies.⁴²

One group has suggested that interstate DTC wine shipments are a simple matter.⁴³ According to them, all that is needed to protect consumers in the receiving state, is the filing of a copy of an out-of-state retail license and minimal procedures on the delivery and shipment of the wine to the consumer. Nothing in their proposal addresses the source of supply by the out-of-state retailer or the use of third-party merchandisers to fill the order.

The experience with e-commerce is actually more complicated. Once you move away from e-commerce by the actual producer or manufacturer of the commodity, the likelihood of fake and counterfeit products increases and, as other consumer goods in e-commerce show, are prevalent. The economic incentives and brand protection concerns for a small winery selling a fake version of its own wine are completely different than a retailer's concerns. State alcohol regulators can address or mitigate these inventory risks with in-state retailers. State regulators' hands are tied enforcing laws beyond their borders and have faced industry pushback for attempts to do so.⁴⁴ Such preventative measures are much more difficult when dealing with e-commerce retailers who have no connection with the state of the consumer. State alcohol regulators should be able to exercise this "risk protectionism" in regulating online commerce of alcohol beverages. This is not the same as "economic protectionism."

Most states have laws prohibiting unlawful trade practices in line with federal tied-house laws and rules. In Colorado, wholesalers are prohibited from selling a product to a retailer below the actual proportionate invoice price and freight charge to that wholesaler or distributor, plus applicable state and federal taxes of any given product.⁴⁵ To monitor compliance of this regulation, the state regulator has the ability to demand records of entities that hold a wholesale license in Colorado. If e-commerce for retailers was broadened to allow retailers throughout the United States to sell DTC in Colorado, then the wholesalers in other states that sell to each retailer would need to be open for inspection to ensure that Colorado law is being followed. However, regulating entities across state lines would be cost-prohibitive, impractical and almost impossible.

⁴¹ National Alcohol Beverage Control Association (2018). NABCA survey of state regulatory agencies.

⁴² The Center for Alcohol Policy has previously provided research on the funding challenges of state alcohol agencies. https://www.centerforalcoholpolicy.org/wp-content/uploads/2013/03/The_Need_for_State_Alcohol_Regulatory_Funding.pdf

⁴³ National Association of Wine Retailers (2019). *Draft Wine Retailer Shipping Legislation*. <https://nawr.org/wp-content/uploads/2019/03/MODEL-WINE-RETAILER-SHIPPING-BILL.pdf>

⁴⁴ Healy v. The Beer Institute 491 U.S. 324 (1989)

⁴⁵ Colorado Liquor Rules, Regulation 47-322(A) (4), 1 C.C.R. 203-2 <https://www.sos.state.co.us/CCR/GenerateRulePdf.do?ruleVersionId=8436&fileName=1%20CCR%20203-2>

Trade practice laws and rules (upholding the three-tier model of alcohol distribution) are important to public health and safety as they combat exclusive arrangements, financial ties (tied-house), commercial bribery and consignment sales. These laws and rules are ultimately aimed to provide for a level playing field and to address harmful sales practices. “Because greater sales of alcohol increase consumption, social problems get worse...more impaired driving, more underage drinking, more alcohol-related disease and greater addiction.”⁴⁶

The three-tier model creates a system to quickly and easily identify alcohol beverage products subject to recalls.⁴⁷ Since all three tiers have detailed records of sales within the tiers, the ability to identify the location and availability of recalled products in order to remove them from the market is substantially more effective than locating every retailer that conducted DTC sales in each state.

Past studies from CAP establish that the absence of fake and counterfeit alcohol products from the United States domestic market is directly related to the closed system of alcohol distribution and sale.⁴⁸ Will movement away from that distribution system introduce fake and counterfeit products to U.S. consumers, causing an increase in public health and safety issues?

REGULATORY APPLES TO APPLES COMPARISON

There is no real federal alcohol regulation of alcohol retailers. Producers are more highly regulated at both the state and federal levels than are retailers. In U.S. Supreme Court case *Granholm v. Heald*, 544 U.S. 460 (2005), Justice Anthony Kennedy’s opinion stressed that producers hold a federal basic permit issued under the Federal Alcohol Administration Act⁴⁹ that, in turn, gives the states additional protection against out-of-state wineries failing to comply with the laws of the state of the purchasing consumer.⁵⁰ This is not true for retailers, retail activities by third-party merchandisers or brewers since there is no federal permit to revoke.

⁴⁶ Erickson, P. (2019, January). *Why is a “level” playing field” for local alcohol markets an important goal for public health and safety?* <http://campaign.r20.constantcontact.com/render?m=1113321512460&ca=87b7f902-bbdb-459e-8312-caaa475776ab>

⁴⁷ Goodison, D. (2008, April 7). *Samuel Adams beer maker issues recall due to glass in bottles.* <https://www.bostonherald.com/2008/04/07/samuel-adams-beer-maker-issues-recall-due-to-glass-in-bottles/>

Ford, D. (2016, March 10). *Corona beer recalled because bottles may contain glass particles.* <https://www.cnn.com/2016/03/10/health/corona-beer-recall-glass-particles/index.html>

⁴⁸ See footnotes 10 and 33.

⁴⁹ Title 27, United States Code, Section 203.

⁵⁰ “Michigan and New York benefit, furthermore, from provisions of federal law that supply incentives for wineries to comply with state regulations. The Tax and Trade Bureau (formerly the Bureau of Alcohol, Tobacco, and Firearms) has authority to revoke a winery’s federal license if it violates state law. BATF Industry Circular 96–3 (1997). Without a federal license, a winery cannot operate in any State. See 27 U. S. C. §204. In addition, the Twenty-first Amendment Enforcement Act gives state attorneys general the power to sue wineries in federal court to enjoin violations of state law. §122a(b).

HIGHER DEFERENCE TO STATES ON REGULATORY CONTROLS OVER PROVEN DISTRIBUTION SYSTEMS

Forty years ago the U.S. Supreme Court said that the 21st Amendment “[g]rants the States virtually complete control over whether to permit importation or sale of liquor, and how to structure the liquor distribution system.”⁵¹ Unlike other commodities and with full knowledge of the large amount of fake alcohol prevalent in other countries, the states should be given deference under the 21st Amendment to set up an orderly marketplace within the alcohol distribution framework inside their borders to best protect consumers and responsible industry members from risks that include differentiating between sales by in-state retailers and out-of-state retailers directly to consumers.

There are far less wineries, distilleries and beer producers in the United States in comparison to the total number of retail sellers (consider both brick and mortar and online or virtual retail sellers) in any one state. This makes identifying remote legitimate retailers far more challenging to regulators.⁵²

CONCLUSION

It is hard to prove the negative. The World Health Organization estimates that one quarter (25.5 percent) of all alcohol consumed worldwide is in the form of unrecorded alcohol – i.e., alcohol that is not accounted for in official national statistics on alcohol taxation or sales as it is usually produced, distributed and sold outside the formal channels under governmental control.⁵³ There is no known U.S. measure, but I believe the U.S. marketplace is close to 100 percent recorded alcohol due to the government regulations designed to limit the marketplace to responsible actors, and with full transparency of the entire industry.

The worldwide scourge of fake and counterfeit alcohol stops at our borders due to federal and state laws designed to protect consumers. Efforts to eliminate this time-tested and working system will harm legitimate alcohol businesses, increase the risks to public health and safety, increase tax evasion due to sales outside the regulated system and introduce fake and counterfeit alcohol into the important, profitable U.S. market.

“The worldwide scourge of fake and counterfeit alcohol stops at our borders.”

⁵¹ Cal. Retail Liquor Dealers Ass’n v. Midcal Aluminum, Inc., 445 U.S. 97, 110 (1980)

⁵² There are also numerous unresolved and potential federal preemption claims that could hamper state’s ability to seek to monitor goods flowing in from other states.

⁵³ World Health Organization (2018). *Global Status Report on Alcohol and Health*.

https://books.google.com/books?id=qnOyDwAAQBAJ&pg=PA43&lpg=PA43&dq=2.5%25+of+all+alcohol+consumed+worldwide+is+in+the+form+of+unrecorded+alcohol&source=bl&ots=a0snNEnjbr&sig=ACfU3U04FLFfdge-jfPpdZC_tSqsonzEg&hl=en&sa=X&ved=2ahUKEwjnvLGX_eDnAhWHoJ4KHdG_CrcQ6AEwC3oECAwQAQ#v=onepage&q=2.5%25%20of%20all%20alcohol%20consumed%20worldwide%20is%20in%20the%20form%20of%20unrecorded%20alcohol&f=false

The expansion of online orders of alcohol beverages shipped to consumers by out-of-state retailers has a greater potential to expose consumers to fake alcohol products which, in turn, poses health and safety risks to the public.

To protect public health, tax coffers and economic development, regulators should fight to prevent fake alcohol from negatively disrupting the United States alcohol market. Efforts to weaken or repeal important laws and regulations that help combat fake and counterfeit alcohol in the U.S. should be strongly resisted by the responsible alcohol industry and public health advocates, as well as by policy makers who consider these proposals.

ABOUT THE AUTHOR

Patrick Maroney is the President of Maroney Consulting Services LLC, and provides consulting related to liquor laws, rules, liability, training and compliance for liquor licensees and stakeholders. Patrick has over 33 years of experience in law enforcement and regulatory compliance. In June 2019, Patrick retired from the state of Colorado where he served as the Director for the Colorado Liquor Enforcement Division (LED) since 2013. For over two years previously, Patrick served as the Chief of Investigations for the LED. He has also worked for other government agencies including the Colorado Lottery, Colorado Bureau of Investigation, Arapahoe County Coroner's Office and the Larimer County Sheriff's Office.

Patrick is a former board member of the National Conference of State Liquor Administrators (NCSLA) and has served on several panels during NCSLA conferences as well as hosted the 2017 National Conference in Denver.

During his tenure as Director of the Colorado LED, Patrick saw several changes in liquor law, policy, rules and industry practices. He worked closely with liquor stakeholders in 2016 and 2018 to implement two bills passed by the Colorado legislature that brought about the most significant changes to Colorado's liquor laws since Prohibition. He understands the importance of strengthening America's strong alcohol regulatory system and its relevancy to protecting public health and safety.

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