

CALCPA WINE INDUSTRY CONFERENCE

WINE LAW BASICS

DECEMBER 8, 2014

BAHANEH HOBEL

SENIOR ALCOHOL BEVERAGE ATTORNEY

DICKENSON, PEATMAN & FOGARTY

T: 707.261.7070 | BHOBEL@DPF-LAW.COM



Disclaimer

This memorandum is provided by Dickenson, Peatman & Fogarty for educational and informational purposes only and is not intended and should not be construed as legal advice.

AGENDA

Licensing

-  License Types, Small Producers Tax Credit

Structural Considerations

-  Entity Types, Tied House Issues, Reportable Changes, Winery Sales

Hot Topics

-  Sponsorships & Events, Contest/ Sweepstakes, Third Party Providers

This handout is made available for general informational purposes only and none of the information provided herein should be considered to constitute legal advice.

LICENSING

WHAT TYPE OF LICENSE?

Traditional Winery: Type 02

- **Licenses:**
 - Federal Basic Permit for wine production and Bonded Winery Registration from Alcohol and Tobacco Tax and Trade Bureau (“TTB”)
 - Type 02 Winegrowers license from CA Department of Alcoholic Beverage Control (“ABC”)
 - Licensed premises for wine production required. Alternating Proprietor (AP) is an option.
- **Pros:**
 - Greater tasting privileges: Tasting permitted at licensed winery premises & one duplicate tasting room, unlicensed locations for private events, limited tastings at retail locations
 - Shipping: Approximately 40 states allow direct to consumer shipping. Various permits are required depending on the state
 - Small Producers Tax Credit
 - Tied House Exceptions: Allow investment in retail tier
- **Cons:**
 - Requires greater financial investment (facility fees, etc.) , although costs mitigated if AP
 - Slightly more complicated application process (all applications take about 90 days)
 - Required reporting and responsibility of payment for excise taxes

LICENSING

WHAT TYPE OF LICENSE?

Virtual Winery: Type 17/20

- **Licenses:**
 - Federal Wholesalers Basic Permit from TTB
 - Beer and Wine Wholesaler (Type 17) and Beer and Wine Off Sale Retail (Type 20) from ABC
- **Pros:**
 - Less financial investment upfront
 - Little reporting responsibility
- **Cons:**
 - Cannot produce wine
 - Limited tasting privileges: Type 17/20s have no tasting privileges with consumers other than at nonprofit sponsored events
 - More limited direct to consumer privileges: Only 15 states allow for direct to consumer shipping. In most states, must go through three tier system to get products to consumers legally.

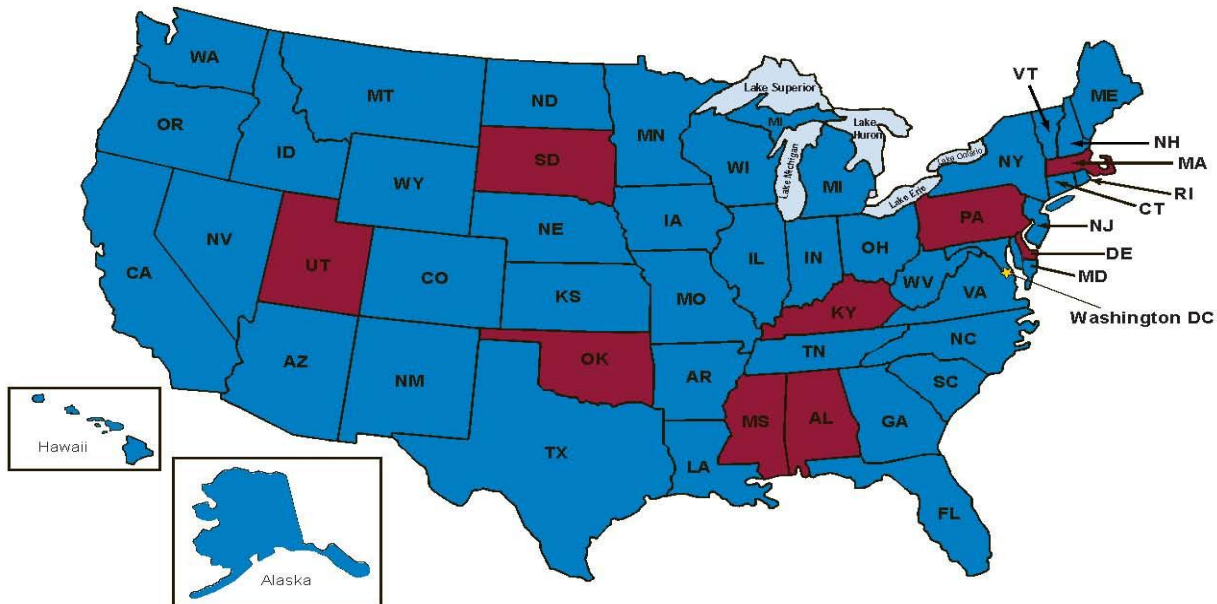
LICENSING

TYPE 02 VS. TYPE 17/20 PRIVILEGES

	Production	Tastings	DTC Shipping	Small Producer Tax Credit
Type 02	Y	Y	Y <i>*Approximately 40 States</i>	Y
Type 17/20	N	N <i>*Except nonprofit events</i>	Y <i>*Only 15 States</i>	N

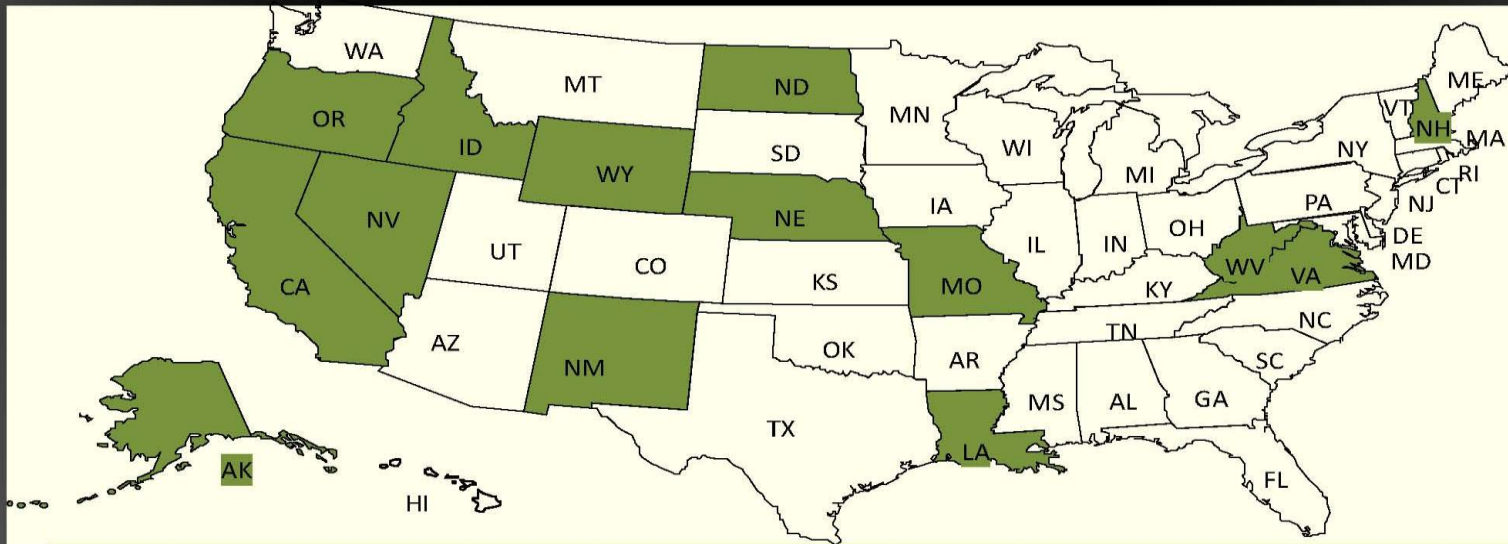
Direct Shipment Laws by State for Wineries
(Information Current as of January 24, 2014)

Contact: Wine Institute for latest updates
www.wineinstitute.org
(415) 512-0151



DTC Shipping by Out-of-State Wine Retailers

(American Wine Consumers Coalition)



Out-of-State Wine Retailer Shipments Allowed in 14 States and DC: AK, CA, DC, ID, LA, MO, NE, NV, NH, NM, ND, OR, VA, WV, WY

LICENSING

SMALL PRODUCERS TAX CREDIT

- ❑ Small Producer Tax Credit only available to holders of a Type 02/ Federal Wine Producer Basic Permit that make less than 250,000 gallons a year.
- ❑ SPTC can be applied to wines produced both by and for the small producer, so long as the producer has produced something during the year (no minimum requirements).
 - What is meant by "produced?" TTB states it is the wine produced by fermentation plus volume increases due to amelioration, wine spirits addition, sweetening, production of a formula wine, of sparkling wine, and wine produced by the same company outside the United States.
- ❑ As long as production stays under 250,000 gallons for a calendar year, a winery may remove more than 250,000 gallons of wine (wine produced in bond, plus purchased wine received in bond) from their bonded premises taxpaid and remain eligible for the small producer credit under Section 5041(c)(1).

LICENSING

SMALL PRODUCERS TAX CREDIT

- ❑ **Standard TTB Excise Tax Rates (without SPTC):**
 - **Up to 14% alcohol: \$1.07 per gallon**
 - **14.1% to 21% alcohol: \$1.57 per gallon**
 - **21.1% to 24% alcohol: \$3.15 per gallon**
- ❑ **If production is 150,000 gallons or less, the credit is \$.90 on the first 100,000 gallons (other than sparkling) taxably removed each year.**
- ❑ **If production is more than 150,000 gallons and not more than 250,000 gallons, the credit is reduced by 1% for every 1,000 gallons produced in excess of 150,000 gallons (i.e., the more wine made, the smaller the credit).**
- ❑ **SPTC can only be transferred on wines you have produced yourself. Consider complications when blending wines and taking in transfers of wine produced for you by other wineries.**

STRUCTURAL CONSIDERATIONS

WHAT TYPE OF ENTITY?

- ❑ Type of entity that holds the alcohol beverage license will affect who must be qualified with TTB and ABC (fingerprints, background check, etc.).
 - **LLC:**
 - For ABC, all members owning more than 10%, all managers, all officers.
 - For TTB, basic information on ALL members, managers, officers must be disclosed.
 - **Corporation:**
 - For both ABC and TTB, all shareholders owning more than 10%, all officers, all directors.
 - **Trusts:**
 - For ABC and TTB, only the trustee needs to be qualified.

STRUCTURAL CONSIDERATIONS

TIED HOUSE ISSUES

❑ General Tied House Principle:

- A person who has an interest (owner (including spouses) officer, director, manager, certain employees) in a licensed alcohol beverage supplier (manufacturer, wholesaler, importer, etc.) is prohibited from holding an interest in a licensed retail alcohol beverage business, unless a specific exception in the alcohol beverage code allows such an interest.

❑ Type of license held will govern applicability of tied house rules

- Type 02 – Allowed numerous exceptions to the Tied House laws and can hold interests in restaurants, retailers, etc. (subject to rules and restrictions).
- Type 17/20s: No ownership interest in restaurants and other retail licenses permitted.

❑ No minimum threshold for tied house restrictions

- Even a .01% ownership would trigger a tied house violation.
- Always need to consider what other alcohol beverage interests are held by all potential investors, owners, managers, officers and directors of licensed entities.
- Consider whether use of a trust as the owner of the interest /shares will provide tied house protection.

STRUCTURAL CONSIDERATIONS

REPORTABLE CHANGES

- ❑ **Any changes to person or entity holding license must be reported to ABC and TTB.**
 - Change in location of Licensed Premises
 - Changes in owners (regardless of percentage), managers, officers, directors, trustees, etc.
 - Change in entity that holds the license or operates the business as a result of sale or otherwise
 - Changes to way ownership interest is held (i.e., change from individual owner to trust, change from parent's trust to children's trust)
- ❑ **Changes to greater than 50% ownership interest in the license will be considered a change in control. Changes to entity holding the license considered a change in proprietorship.**
 - Must be reported to agencies within 30 days
 - TTB permits deemed terminated within 30 days of a change in control unless new application filed
 - TTB requires “new” permits in the event of change in control, although permit numbers can be retained if entity remains the same.
 - Note that even a change from an individual owner to a trust is considered a change in control, even if the same parties retain management and control of operations

STRUCTURAL CONSIDERATIONS

SALE OF WINERY OR WINERY ASSETS

- ❑ **Transfers permitted for ABC permits, not TTB permits. How do winery operations continue?**
 - If bonded winery operations need to continue, Transitional Services Agreement required.
 - If bonded winery operations not required, buyer could sell tax-paid wine under *seller's* existing federal permits and temporary ABC permit.
 - Technically buyer is not permitted to make sales under seller's basic permit if bonded winery operations are being conducted by seller.
- ❑ **Complicated to juggle federal and state transfers – disconnect between the buyer's temporary CA ABC licenses and the fact that federal permits continue to be held by the seller.**
- ❑ **Complications could be avoided by making closing contingent on issuance of licenses.**
 - In reality, most parties do not want to wait the 90 days it takes for licenses to issue to close.
- ❑ **Consider benefits of purchasing assets of existing entity vs. new entity.**
 - If existing licensed entity remains in tact, likely could retain all existing license and permit numbers.
 - From an administrative/licensing point of view, will not have to obtain new licenses in most other states (just updates), will not have to submit new label approvals to TTB (COLAs), etc.

HOT TOPICS

SPONSORSHIPS & EVENTS

- ❑ **Sponsorships by Type 02 and 17/20 Licenses are extremely limited under ABC Act**
 - **Nonprofit organizations (as long as the event does not benefit a permanent retail licensee). Both Type 02s and 17/20s can provide wine or money to nonprofits and “assist” at such events.**
 - **If clients are considering sponsoring any event, the first question should always be who they are sponsoring and whether that entity is a nonprofit. If not, the sponsorship is likely not permitted.**
 - **Contests, races, tournaments, and other similar activities which are only in the form of “monetary payments to bona fide amateur or professional organizations established for the encouragement and promotion of the activities involved”**
 - **Rule 106 contains additional restrictions on sponsorship – cannot require exclusive service of sponsors products, can’t give away free goods, etc.**
 - **ABC inconsistent in enforcement of sponsorships**

HOT TOPICS

CONTESTS & SWEEPSTAKES

Industry Advisory Overview

- Entry shall not be based on purchase of alcoholic beverages
- Must be 21 years old or above to enter
- Shall not benefit any permanent retail licenses
- Alternative means of entry that does not require visit to retailer
- Cannot give alcohol or means to obtain alcohol as a prize

In Practice

- Most frequently raised question: Can winery provide wine tastings as a prize?
 - A Type 02 winegrower should NOT provide a winetasting as a prize for any contest or sweepstakes. The Type 02 winegrower can provide a visit or tour of its winery premises as the prize. Note that Type 02 winegrower is permitted to do tastings at its premises.
 - Type 17/20 also should not provide a winetasting as a prize and does not have any tasting privileges at its licensed premises.

HOT TOPICS

THIRD PARTY PROVIDERS

❑ Industry Advisory Overview

- Winery needs to be in control and be decision-maker (pricing, products, etc.)
- All sales made must be made by winery
- Requirement for escrow account and control by winery of funds
- All deliveries must be made by winery under their license
- Licensee is ultimately responsible and same rules apply

❑ In Practice

- Many different applications of third party provider to different business models, both with respect to physical services (fulfillment) and online (marketing)
- Consider intersection with other states' rules when dealing with third party providers on the internet. Which states' rules apply?
 - New York Advisories: ShipCompliant/Lot 18 decision, Drizzly, Slingr

THANK YOU

BAHANEH HOBEL

SENIOR ALCOHOL BEVERAGE ATTORNEY

DICKENSON, PEATMAN & FOGARTY

1455 FIRST STREET, STE. 301 | NAPA, CA 94559

T: 707.261.7070 | F: 707.255.6876

BHOBEL@DPF-LAW.COM | WWW.DPF-LAW.COM