

Business & Professions Subcommittee

Wednesday, October 16, 2019
12:30 AM – 2:30 PM
Webster Hall (212 Knott)

Meeting Packet

Jose Oliva
Speaker

Heather Fitzenhagen
Chair

Committee Meeting Notice

HOUSE OF REPRESENTATIVES

Business & Professions Subcommittee

Start Date and Time:	Wednesday, October 16, 2019 12:30 pm
End Date and Time:	Wednesday, October 16, 2019 02:30 pm
Location:	Webster Hall (212 Knott)
Duration:	2.00 hrs

Discussion of Florida's Alcoholic Beverage Laws

NOTICE FINALIZED on 10/09/2019 3:45PM by Rigas.Amanda

The Florida House of Representatives

Commerce Committee

Business & Professions Subcommittee

Jose Oliva
Speaker

Heather Fitzenhagen
Chair

AGENDA

Wednesday, October 16, 2019
Webster Hall (212 Knott)
12:30 PM – 2:30 PM

I. Call to Order & Roll Call

II. Welcoming Remarks

III. Discussion of Florida's Alcoholic Beverage Laws

IV. Adjournment

303 House Office Building, 402 South Monroe Street, Tallahassee, Florida 32399-1300
(850) 717-4873 Fax: (850) 413-0419

Alcohol Regulation in Florida

Division of Alcoholic Beverages and Tobacco

House Business and Professions Subcommittee
October 16, 2019

Introduction

- Division Overview
- Beverage Regulation in Florida
- Licensing Information
- Excise Tax Collection
- Compliance Activities
- Revenue Distribution

Division Overview

The Division of Alcoholic Beverages and Tobacco licenses the manufacture, distribution, sale and service of alcoholic beverage and tobacco products in Florida.

Licensing

- Processing license applications and renewals.
- Verifying an applicant's qualifications for licensure under the Beverage Law and chapters 210 and 569, Florida Statutes.

49 FTE Positions

Auditing

- Collecting and auditing of the excise tax due to the state.
- Conducting compliance audits to ensure compliance with special licensing requirements.

84 FTE Positions

Enforcement

- Conducting routine compliance inspections.
- Conducting minimum age of purchase surveys.
- Conducting criminal and administrative investigations.

188 FTE Positions

Florida dbpr Department of Business & Professional Regulation

Beverage Regulation in Florida

Florida is a Licensing State

- Predominant regulatory model
- The State of Florida is not in the business of distributing or selling alcoholic beverages.

Florida's Beverage Law Creates a Three-Tier Licensing System

- Originated from efforts to prevent pre-Prohibition practices that caused a proliferation of manufacturer-controlled saloons with aggressive marketing tactics, commonly referred to as "tied houses."
    - The term "tied house" comes from a practice in England where a bar is "tied," by ownership links or contractual obligations, to a specific manufacturer.

- Tied house legislation was intended to prevent vertical integration of ownership and, in turn, prevent intemperate consumption.

Prohibitions on Tied House Evil

- No manufacturer, distributor, importer, primary American source of supply, brand owner or registrant, broker, sales agent, or sales person shall have any financial interest, directly or indirectly, in the establishment or business of any vendor licensed under the Beverage Law, nor assist any vendor by any gifts or loans of money or property of any description or by the giving of any rebates of any kind whatsoever.

- No licensed vendor shall accept, directly or indirectly, any gift or loan of money or property of any description or any rebates from any such manufacturer, distributor, importer, primary American source of supply, brand owner or brand registrant, or any broker, sales agent, or sales person thereof.

- Industry members are prohibited from furnishing, supplying, giving, renting, or lending, to a vendor, any equipment, fixtures, furniture, furnishings, signs, supplies, credit, money, compensation, rebates, accumulated rebates, fees of any kind including slotting fees, services, property, or other thing of value of any description not included in the exceptions specified by rule or specifically authorized by statutes to vendors or their employees or agents acting within their scope of employment. Vendors are similarly prohibited from accepting such

Exceptions to Three-Tier System

- *Licensing of manufacturers and distributors as vendors and of vendors as manufacturers; conditions and limitations.*

Manufacturers of Wine:

Authorized to own, manage, operate, or control no more than three vendor's licenses in the state.

Manufacturers of Malt Beverages:

Authorized for up to (8) eight vendor licenses at a brewery/vendor properties consisting of a single complex divided by no more than one public street or highway
Authorized to transfer malt beverages to a licensed facility in an amount up to the yearly production at the receiving facility (subject to limitations in law).

- *Distilleries and craft distilleries*

Craft Distillery (Manufacturer of Distilled Spirits Producing 75,000 or fewer gallons per calendar year):

Authorized to sell to consumers, at its souvenir gift shop, branded products distilled on its premises in factory-sealed containers that are filled at the distillery for off-premises consumption

Local Government Authority

- The Florida Constitution states that the status of a county with respect thereto shall be changed only by vote of the electors in a special election called upon the petition of twenty-five per cent of the electors of the county, and not sooner than two years after an earlier election on the same question. Where legal, the sale of intoxicating liquors, wines and beers shall be regulated by law.

- The standards and procedures for local option elections are established in Chapter 567, Florida Statutes.

- Nothing contained in the Beverage Law shall be construed to affect or impair the power or right of any county or incorporated municipality of the state to enact ordinances regulating hours of business, location of place of business, sanitary regulations, type of entertainment and conduct permitted (consumption on premises) of any licensee under the Beverage Law within the county or corporate limits of such municipality.

- No tax on the manufacture, distribution, exportation, transportation, importation, or sale of such beverages shall be imposed by way of license, excise, or otherwise by any municipality, anything in any municipal charter or special or general law to the contrary notwithstanding. However, a portion of state license tax revenue is returned to the county or incorporated municipality where collected.

Licensing Information

In FY18-19, the Division administered approximately 50,000 alcoholic beverage licenses, with a staff of 49 dedicated Bureau of Licensing employees across 11 district offices.

In FY18-19, the Division collected approximately $46,000,000 in fees for the issuance or renewal of alcoholic beverage licenses or permits. Licenses are renewed annually.

Licenses are categorized by tier, then further categorized, in most instances, depending on their particular business model.

Licensing fees are generally based on the scope of the activities permitted and the population of the county where the license is located.

Tier	Annual Fee Range	Number of Licensees
Manufacturer	$500-$4000	453
Distributor	$1000-$4000	904
Vendor	$25-$2500	48,926

FY 2018-19 Growth Points:

- 13% Increase in Malt Beverage Manufacturer Licenses
- 16 % Increase in Distilled Spirits Manufacturer Licenses

Florida dbpr Department of Business & Professional Regulation

Licensing Information

Quota Limitations on Liquor Licenses

Section 561.20(1), F.S., limits the number of licenses authorized for the sale of liquor – by the package or for consumption on the premises – to:

1 License Per 7,500 Residents (by county)*

Limitation by population does not apply to numerous special license types, including:

- Hotels/Motels
- Condominium
- Food Service Establishment
- Caterer
- Culinary Education Program
- Public Fair/Expo
- Civic Center/Sports Arena
- Performing Arts Center
- Golf Clubs
- Tennis Clubs
- Fraternal Associations
- and others....

Licensing Information

Quota Limitations on Liquor Licenses

Section 561.19, F.S., governs procedures for issuance of new licenses when determined to be available by increases in county population:

1 License Per 7,500 Residents (by county)*

Based on Population Estimates supplied by
Office of Economic and Demographic Research

Annual Entry Period - 45 days beginning on the third Monday in August
One entry per interested party per county - $100 fee per entry

2019 Drawing Entry Period

More than 24,000 entries for 51 quota beverage licenses in 27 counties.

Drawing date to be announced upon final validation of entries.

Excise Tax Collection

Tax is collected at intervals of one month, on or before the 10th of each month, and the tax payment is accompanied by the statutorily required report of alcoholic beverages manufactured, sold, imported or exported.

Tax rates are dependent on the type of alcoholic beverage being sold.

Tax is generally assessed on the distributor tier at the time the alcoholic beverages are sold to vendors for the purpose of retail sale, unless otherwise specified by statute to be assessed on a manufacturer.

In FY18-19, the Division collected over $300,000,000 in excise tax on alcoholic beverages, with a staff of 84 dedicated Bureau of Auditing employees across 6 district offices.

Beer		Wine		Liquor	
Pints or Less	$0.06 each	Less than 17.259% ABV*	$2.25 per Gallon	Less than 17.259% ABV*	$2.25 per Gallon
Quarts	$0.12 each	17.259% or more	$3.00 per Gallon	17.259% to 55.780% ABV*	$6.50 per Gallon
Gallons	$0.48 each	Natural Sparkling	$3.50 per Gallon	More than 55.78% ABV*	$9.53 per Gallon
		Cider	$0.89 per Gallon		

*ABV: Alcohol by Volume

The Division maintains an electronic report filing system.

- Approximately 90% of tax remitting licensees are currently reporting electronically

Florida dbpr Department of Business & Professional Regulation

Compliance Activities

In FY 18-19, the Division performed over 52,000 alcoholic beverage and tobacco inspections, with a staff of 188 dedicated Bureau of Enforcement employees across 12 district offices.

- 107 FTE positions are sworn, and 81 FTE positions are non-sworn.

- Routine compliance inspections resulted in an approximately 64% compliance rate at the time of inspection.

In FY18-19, the Division performed over 3,300 alcoholic beverage compliance surveys to determine whether licensees were complying with minimum age of purchase restrictions in Florida law.

Nearly 89% of the alcohol-related compliance surveys resulted in vendor compliance.

Revenue Distribution

Alcoholic Beverage License Fees:

8 % Service Charge to General Revenue, after payment the balance is distributed as follows:

- 38% of each license fee to the city where the license is physically located;
- 24 % of each license fee to the county where the license is located; and
- The remaining balance to the ABT Trust Fund.

Catering (13CT) License Fees:

- First $300,000 in fees collected is deposited in the DCF Operations and Maintenance Trust Fund to be used only for alcohol and drug abuse education, treatment, and prevention programs;
- All fees in excess of the initial $300,000 collected is deposited in the Hotel and Restaurant Trust Fund.

New Quota License Fee:

- $10,750 fee deposited in DCF Operations and Maintenance Trust Fund to be used only for alcohol and drug abuse education, treatment, and prevention programs.

Alcoholic Beverage Excise taxes:

- 2% of the excise taxes on alcoholic beverages and the tax on alcoholic beverages, cigarettes, and other tobacco products for passenger vessels is deposited in the ABT Trust Fund to meet the division's appropriation for the state fiscal year;
- 50% of excise tax on domestic wine is transferred to the Department of Agriculture's Viticulture program;
- The remainder of the excise taxes collected on alcoholic beverages and for passenger vessels are deposited into the General Revenue Fund.

The unencumbered balance in the ABT Trust Fund at the close of each fiscal year may not exceed $2 million. These funds shall be held in reserve for use in the event that trust fund revenues are unable to meet the division's appropriation for the next fiscal year. Any unencumbered funds in excess of reserve funds shall be transferred unallocated to the General Revenue Fund by August 31 of the next fiscal year.

Florida dbpr Department of Business & Professional Regulation

Contact Information

Gabe Peters
Legislative Affairs Director
gabe.peters@myfloridalicense.com
850-487-4827

The Alcohol Regulation Dilemma: Maintaining Public Health and Safety as the Overarching Priority While Accommodating Business Needs

Pamela S. Erickson, President/CEO Public Action Management and former Director of the Oregon Liquor Control Commission

Before the Business and Professions Subcommittee, Commerce Committee, Florida House of Representatives, Tallahassee, Florida.

October 16, 2019

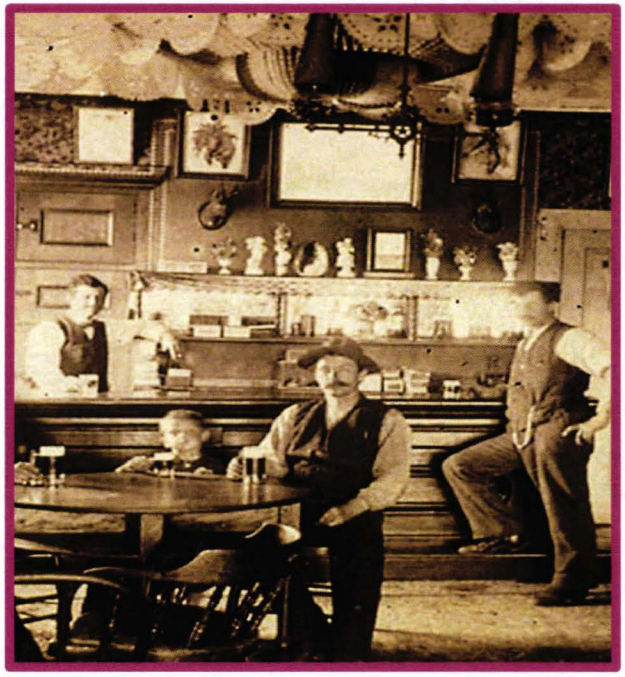
Alcohol regulation is a difficult and complex task.

- To regulate a product that is potentially dangerous, your regulations must be tight enough to curtail practices that can increase harm, but loose enough to allow large and small businesses to be profitable.
- Enforcement is key to ensuring that regulations will be effective in ensuring public health and safety.
- The best regulatory systems, according to the World Health Association, are those that use scientific evidence "… and multiple policies are implemented in a systematic way. Complementary system strategies that seek to restructure the total drinking environment are more likely to be effective than single strategies."
- Measures should be in place to prevent local markets from domination of large, out-of-state businesses. A brief history lesson will help explain this.



U.S. alcohol regulation was designed to prevent the market conditions which created major public health and safety issues before Prohibition.

- Before Prohibition, national alcohol companies dominated sales in local markets by owning saloons which was the only place alcohol was usually sold.
- 70% were vertically integrated Tied Houses and they saturated local communities.
- They used aggressive sales, inducements, and illegal activity to boost sales. Often workers would "drink up their pay check" leaving the family in dire straits.
- These companies were "absentee owners" who took profits out of state and cared little about community problems they engendered.



When states were given the primary responsibility for alcohol regulation via the 21st Amendment, the objectives were designed to prevent both local market domination by large companies as well as curtailing business practices which promote over-consumption.

- Because corporations are made up of investors, the priority is invariably profits, not public health and safety. Therefore, some regulations were designed to **reduce the adverse impacts of "the profit motive"** such as price wars, incentives to consume in high volume.
- **Reduce the opportunity for local market domination by preventing "vertical integration"** or financial arrangements which tied manufacturers to retailers.
- Curtail public order problems created by saloons by **outlet density restrictions**, limits on days/hours of sale and measures to encourage less drinking in public.
- **Greater restrictions on high alcohol content products;** make "lighter alcohol content" products more widely available. By making light beer more available, it encouraged the drinking public to consume less potent products.
- **These things worked and they still work today** although there are efforts to tear the system down and allow alcohol to be sold in a "free market."
- Most of these measures have now been confirmed to be effective based on the results of credible research.

The problem of the "absentee owner" (Justice William O. Douglas comment):



"Local leadership is diluted. He who was a leader in the village becomes dependent on outsiders for his action and policy." (*Standard Oil Co. v. U.S.*, 337 U.S. 293 (1949)

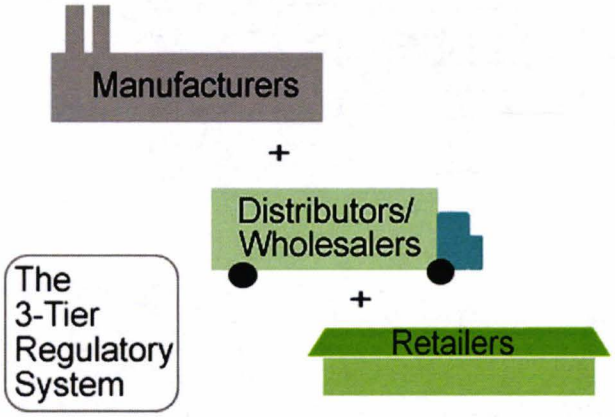
The U.S. alcohol regulatory system is organized into three tiers with various requirements for each tier to be independent. All states and the federal government have similar systems.

Three tier laws prevent a form of monopoly known as **vertical integration** by prohibiting ownership, financial dependence, exclusive arrangements between tiers.

Trade practice laws provide an **even playing field** so small and large companies can operate. They also increase competition since products are not pushed on customers, but succeed if the customer likes them.

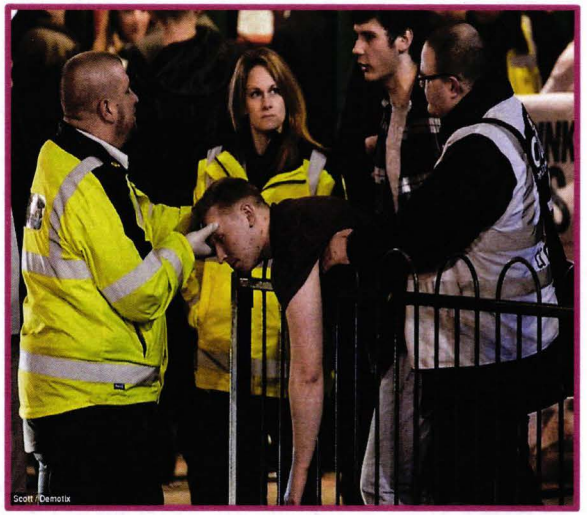
Examples of **trade practice laws are** those that prohibit financial ties, exclusive contracts, commercial bribery and consignment sales. (Many of these practices are legal in other countries and in the U.S. for other commodities.)

Each tier has **tax collection duties** (federal tax, state excise tax and sales tax) and the middle tier tracks all bottles and cans allowing for **safe products** and rapid recall when necessary.



But does alcohol regulation really work? We only need to look at the UK to see what can happen when alcohol is deregulated.

- At one time, the UK had a model regulatory system. But, they deregulated over 50-60 years.
- Big box grocery chains are "vertically integrated" and dominate local markets with cheap alcohol available 24 hours a day, 7 seven days a week.
- The UK experienced a major increase in consumption and "out-of-control" bar sales that reached epidemic proportions with high rates of underage drinking, public drunkenness and over 1 million alcohol related hospital admissions.
- Three of the four recent prime ministers have proposed a major strategy to address this issue only to be thwarted by a strong industry that opposes the population-based "strong strategies" preferring "personal responsibility" measures.



Strong policies make a difference according to the first study of multiple policies.

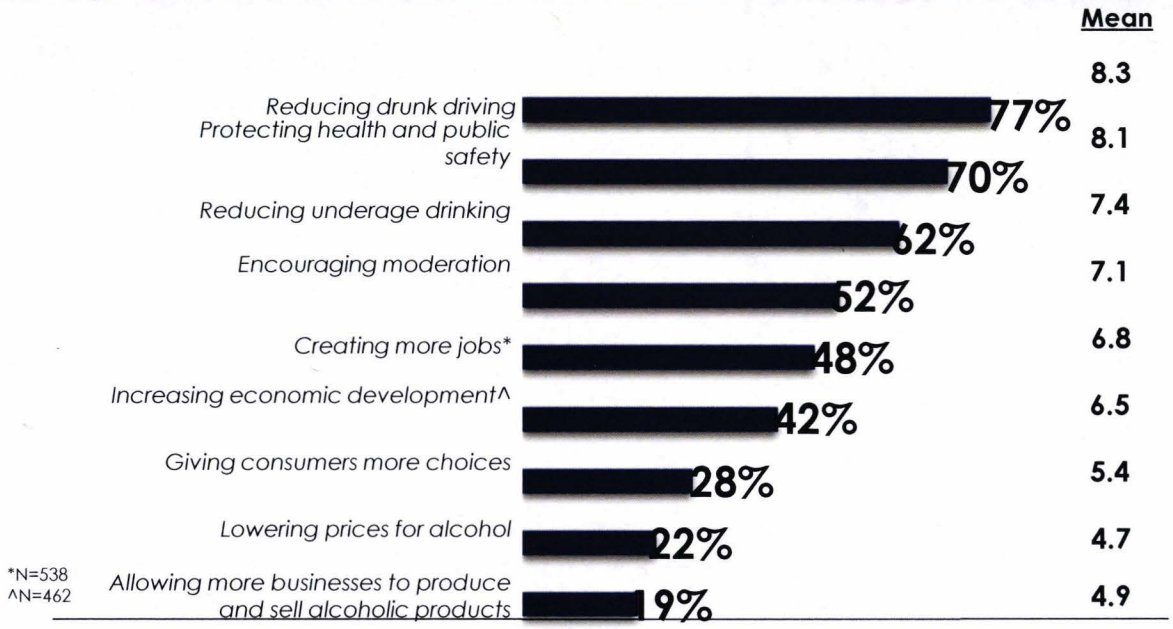
- Dr. Tim Naimi, Boston University, and colleagues created an alcohol policy score and ranked each state based on their policies.
- **"We found that states with stronger and more effective alcohol policies had less binge drinking than states with weaker alcohol policies."**



The Public is With You!!!

A recent survey indicates high levels of support for alcohol regulation. When asked about setting alcohol policies, the results show a strong priority for public health and safety. *Source: Center for Alcohol Policy 2017 survey.*

***The question**: "As you may know, states do regulate alcohol by crafting rules that are unique to their state. Sometimes changes are considered. The following is a list of concerns some people say that lawmakers should consider when setting alcohol regulations. Using a scale of 0 to 10, please indicate how important each of these considerations should be when deciding alcohol regulations: 10 is very important, 0 is not at all important and 5 is a neutral rating."*



*N=538
^N=462

Recent issues:

- **The US alcohol manufacturing sector has experienced a gargantuan change**: In 1961 there were 230 breweries in the US, now we have over 7,000 plus over 9,000 wineries and 1500 distilleries. The vast majority are tiny operations.
- **Small suppliers want to operate outside the three-tiered system to retail their product and self-distribute**. Many states have allowed exemptions, but only for small operators (based on volume produced). This requires a separate tax collection process, different types of licenses, new enforcement tasks, and does not result in tracking products.
- **Some states have granted small suppliers retail privileges** that include food and beverage service without the requirements placed on regular on-premise licensees. In states where licenses are bought and sold, on-premise licensees have raised the issue of financial unfairness.
- **More states and local jurisdictions are granting more alcohol licenses, some in non-traditional locations, as more businesses want more profits.** Yet, at the macro level there is no new demand for alcoholic beverages. According to economist, Lester Jones, "The pie is not growing, just shared across more occasions, more outlets and more products." This presents potential public safety problems as research has shown a relationship between high outlet density and problems. In addition, it dilutes enforcement resources.
- There is a **demand for home delivery** of alcohol by small suppliers, by large chain liquor companies and by connoisseurs of fine wine. Many states allow home delivery, especially for wine…but there seems to be a general lack of compliance with requirements. Enforcement of safe-guards for home delivery are very difficult to enforce.



Recommendations

- **Remember that public health and safety is the priority** when considering changes to alcohol regulation. The deaths, injuries and social problems affect a substantial portion of Florida's citizens.
- Your effort to **invite prevention and public health officials to brief you periodically** on progress with alcohol problems should continue. Prevention programs have been successful in reducing underage drinking and drunk driving and should be continued and strengthened.
- Businesses of all sizes need to be able to operate profitably, yet not contribute to alcohol involved harms. To strike the right balance, the current system curtails the chances for local market domination and bans/limits business practices which can lead to abuse. **These benefits are worth maintaining.**
- **Go slow** when considering marketplace regulation changes as it is very hard to predict the impact and reversing the change is extremely difficult. It is also important to consider the harm that might occur for current licensees and the needs for effective enforcement.

or more information: contact Pamela Erickson, pam@pamaction.com or visit website www.healthyalcoholmarket.com.



Website has:

- **Monthly newsletter, educational pieces, PowerPoint presentations from conferences. (These are free!)**
- **Recent reports available: "Special Rules for Small Brewers, Wineries and Distillers" and "Fair Trade Practice Regulations." (Free download)**
- **Issue Briefs has simple explanations of alcohol regulatory issues as well as citations for research and more information.**

Economics Perspectives on Alcohol Beverage Industry

Economics Perspectives on Alcohol Beverage Industry

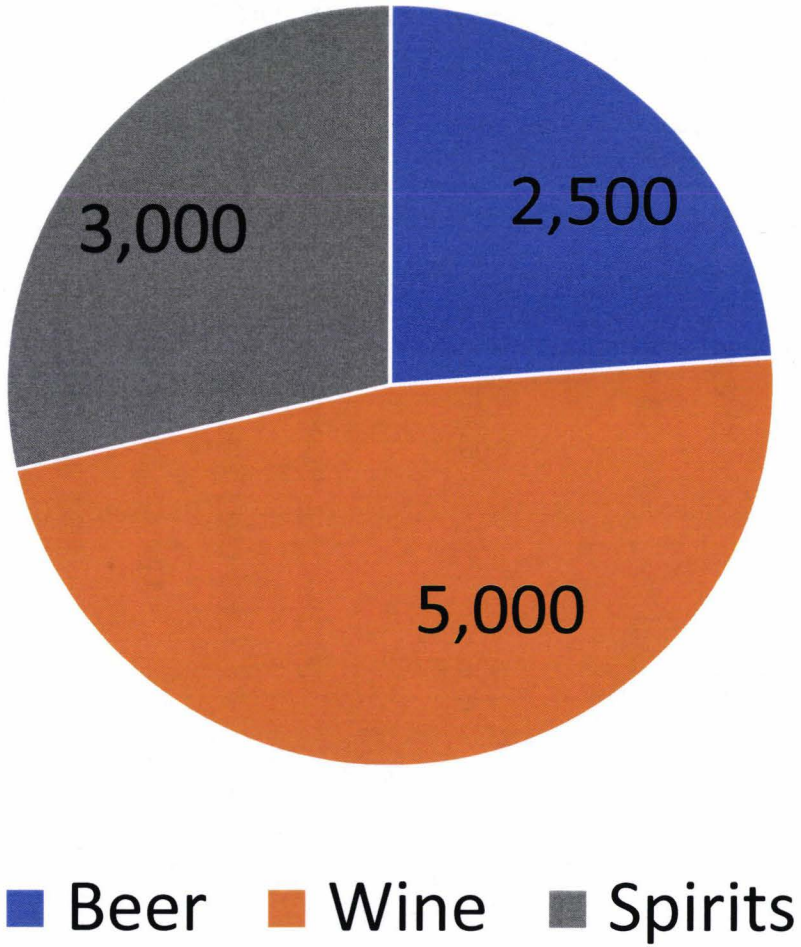
Lester Jones
Chief Economist
National Beer Wholesalers Association
Alexandria, Virginia





The three tier system for alcohol beverages provides today's consumers with more choices and variety than most other consumer package goods segments

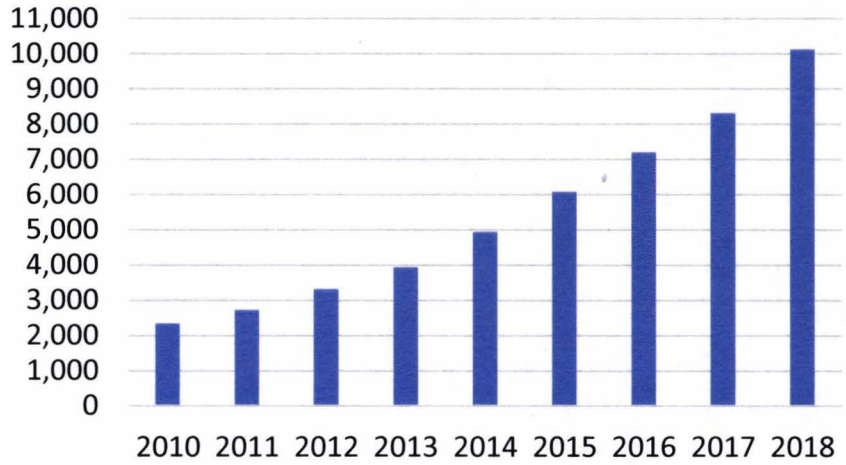
Market Availability of Brands In One Single Florida Retailer



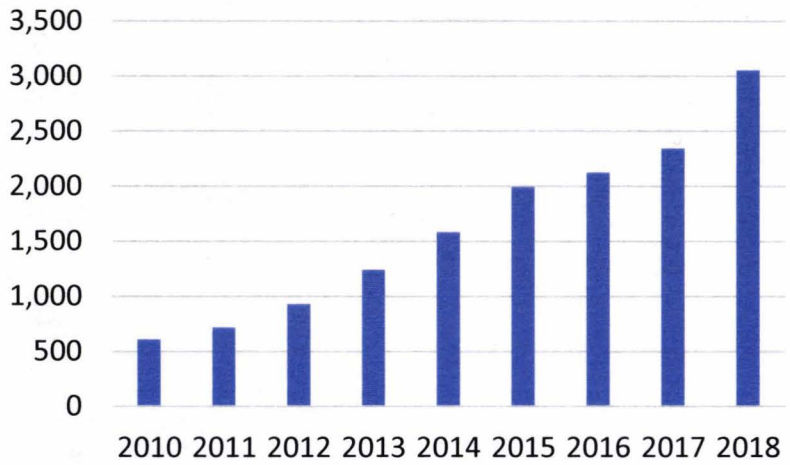
Source: FBWA and NBWA, 2019

Alcohol Permits Grow Across All Segments
Total U.S. 2010 to 2018

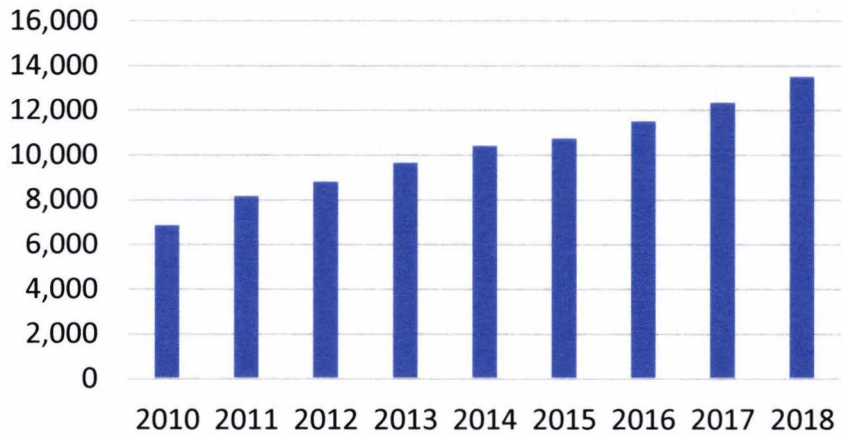
Brewery Permits



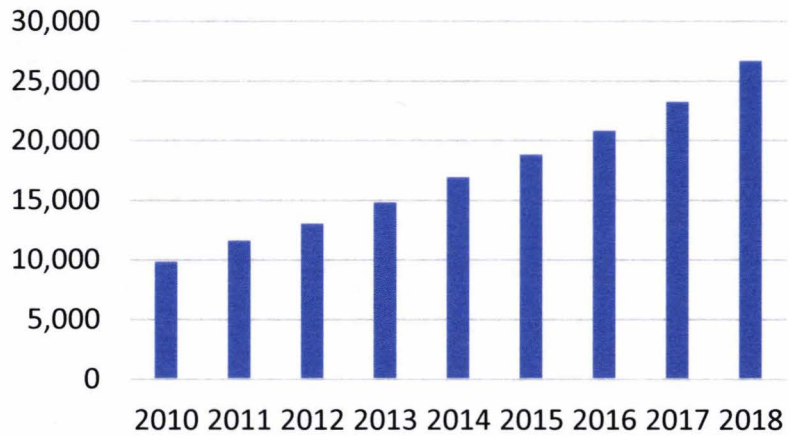
Distillery Permits



Winery Permits

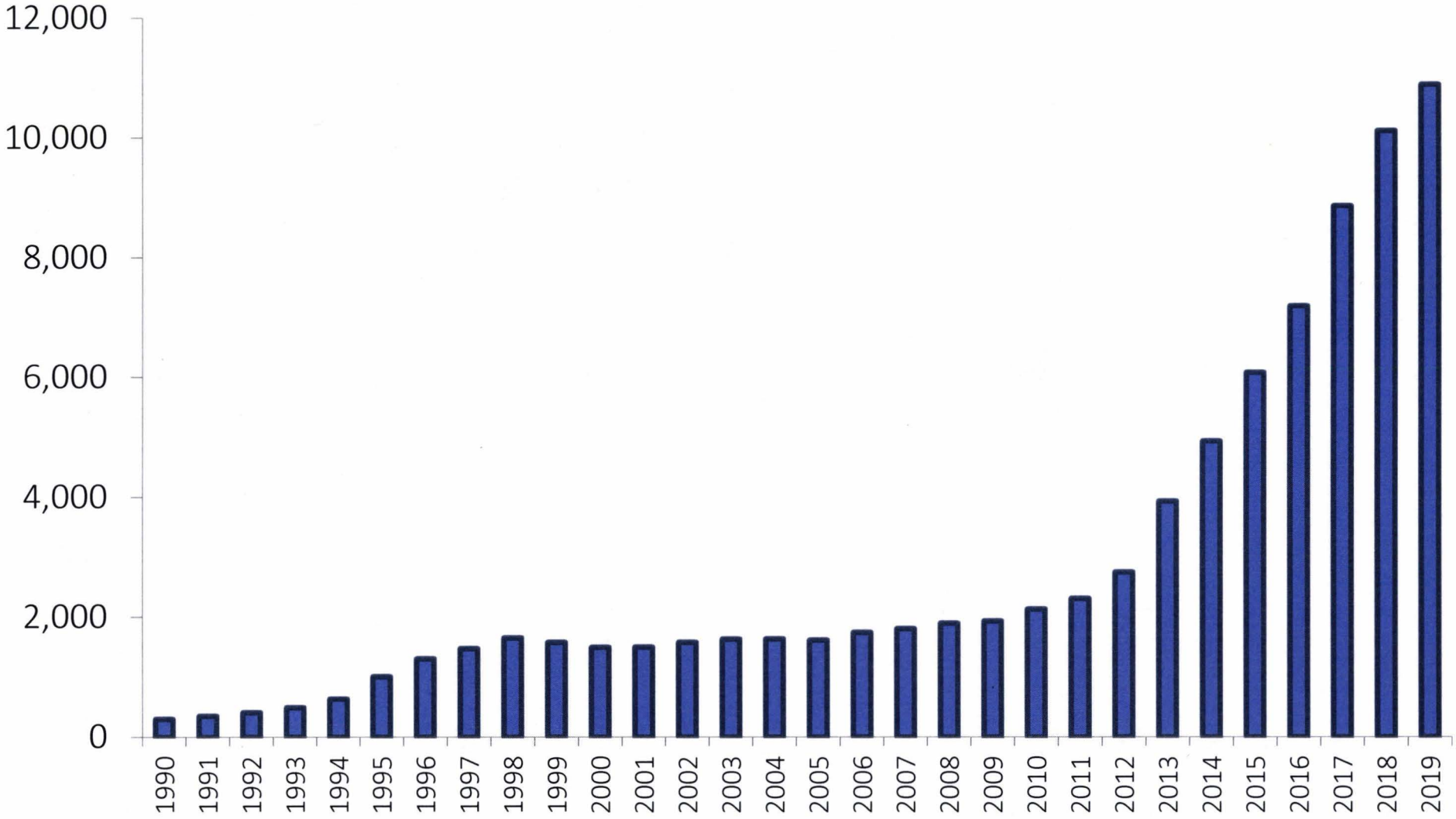


Total Permits



Source: NBWA and U.S. TTB, 2019

Number of Breweries in U.S. 1990 to YTD June 2019



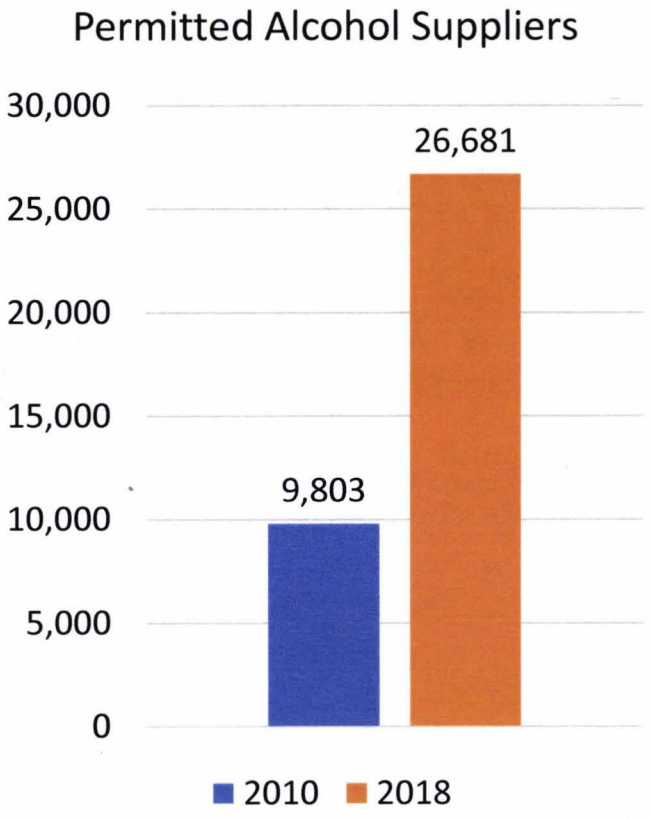
Source: NBWA and U.S. TTB, 2019

TTB Permitted Brewery Count
10,887 Total Permits June 2019

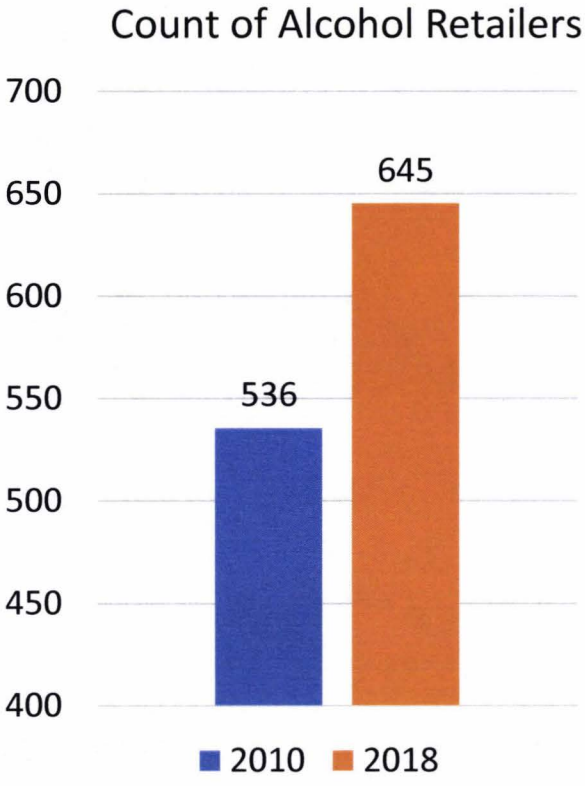
State	Count	State	Count	State	Count
Alabama	55	Kentucky	86	North Dakota	26
Alaska	51	Louisiana	47	Ohio	377
Arizona	146	Maine	165	Oklahoma	55
Arkansas	53	Maryland	141	Oregon	386
California	1,236	Massachusetts	230	Pennsylvania	472
Colorado	500	Michigan	510	Rhode Island	33
Connecticut	124	Minnesota	239	South Carolina	94
Delaware	38	Mississippi	19	South Dakota	35
DC	13	Missouri	168	Tennessee	140
Florida	386	Montana	108	Texas	387
Georgia	121	Nebraska	60	Utah	46
Hawaii	38	Nevada	50	Vermont	90
Idaho	87	New Hampshire	106	Virginia	328
Illinois	338	New Jersey	146	Washington	540
Indiana	234	New Mexico	124	West Virginia	32
Iowa	125	New York	532	Wisconsin	303
Kansas	64	North Carolina	387	Wyoming	44

Source: NBWA and TTB, 2019.

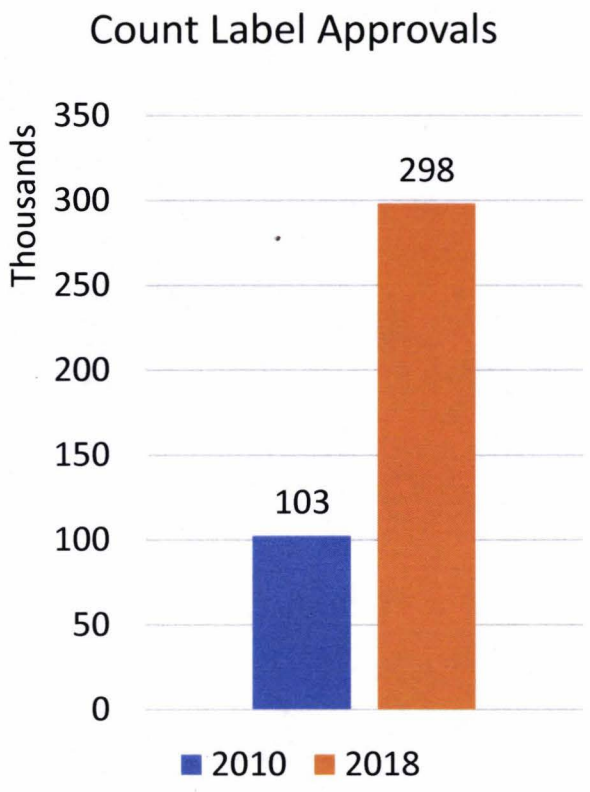
More Suppliers, More Places, More Products 2010 vs 2018



Source: U.S. TTB

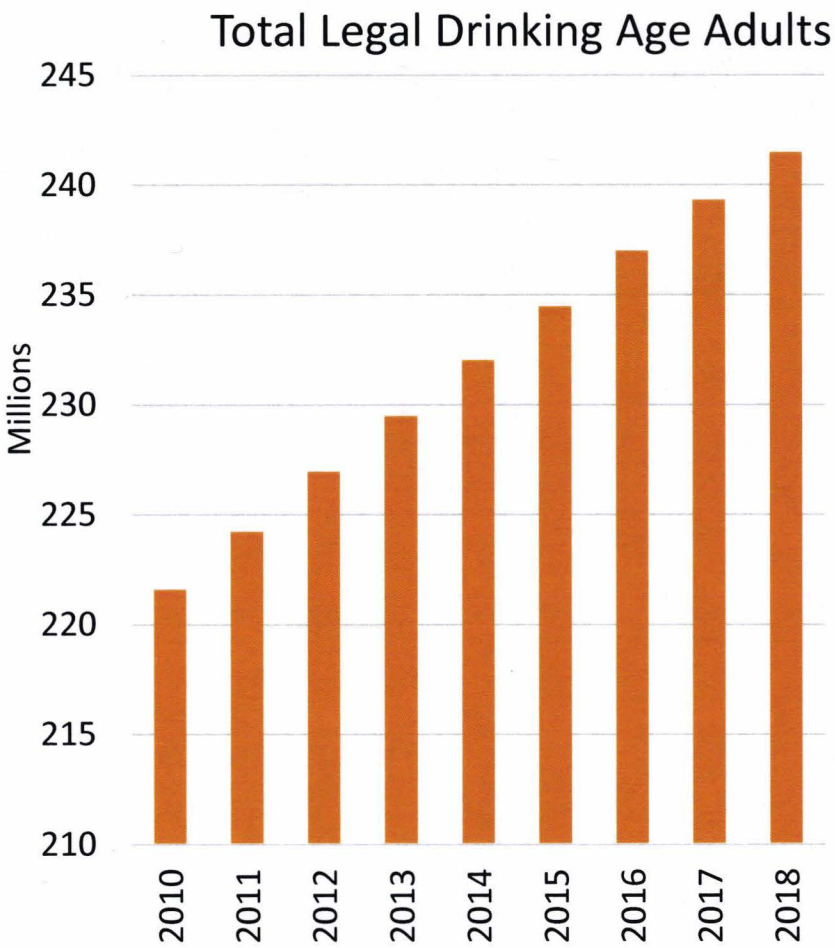


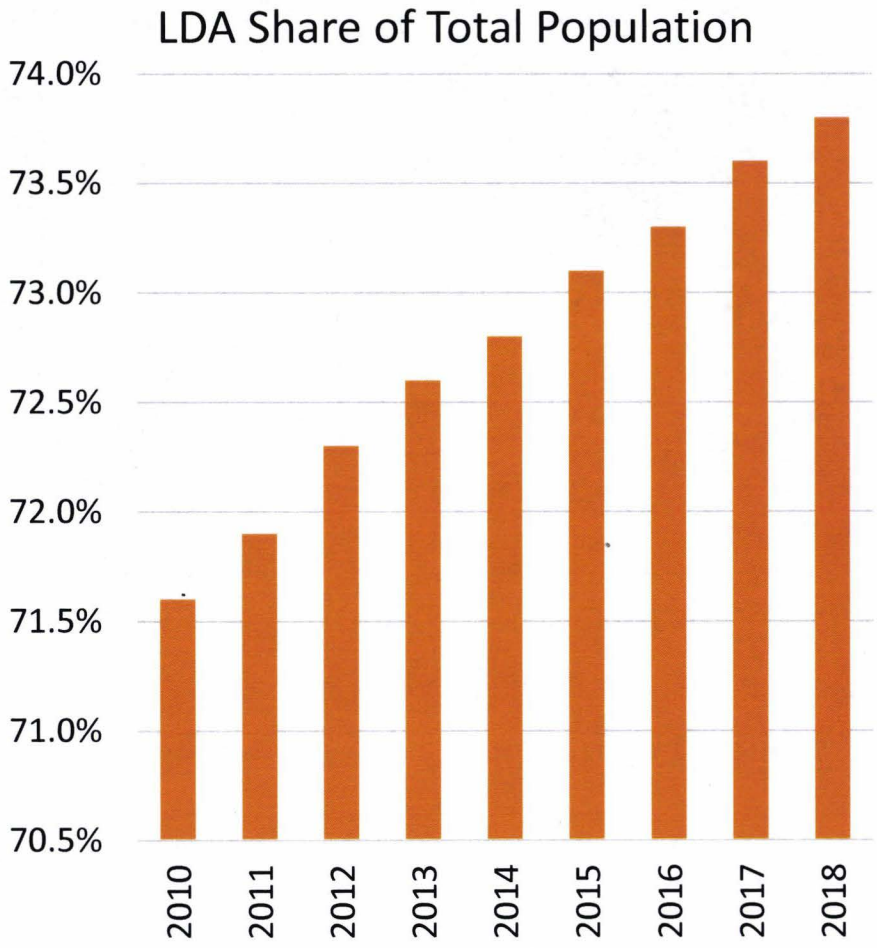
Source: TDLinks™



Source: U.S. TTB

US Demographics
Legal Drinking Age Adults (21+ / LDA)



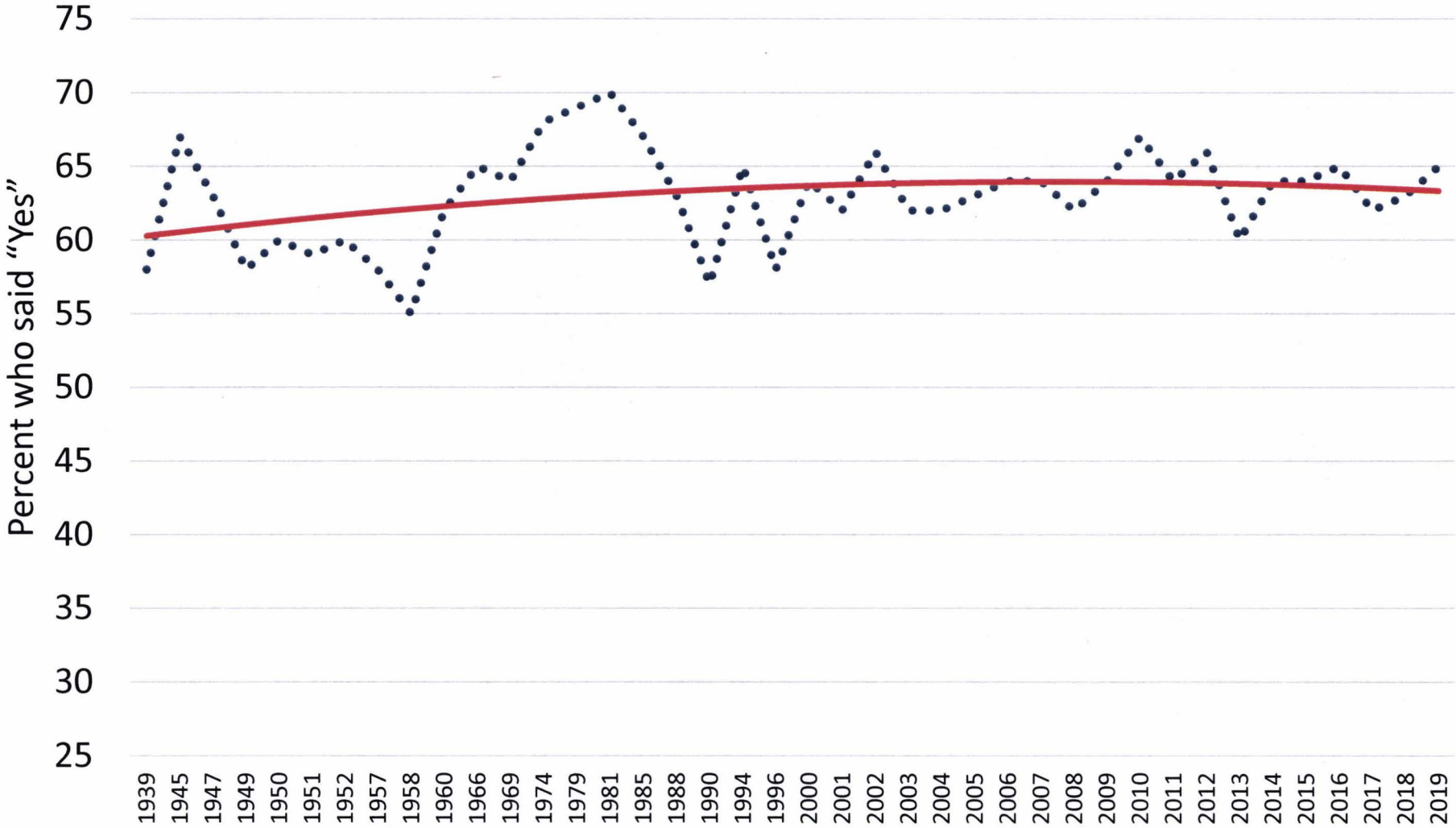


US Fertility Rates Have Plummeted Into Uncharted Territory. 60.2 babies were born in 2017 for every 1,000 women of 'childbearing' age (15-44) – a low not seen in the US since officials began charting.

Source: Compiled by NBWA from U.S. Census Bureau 2018

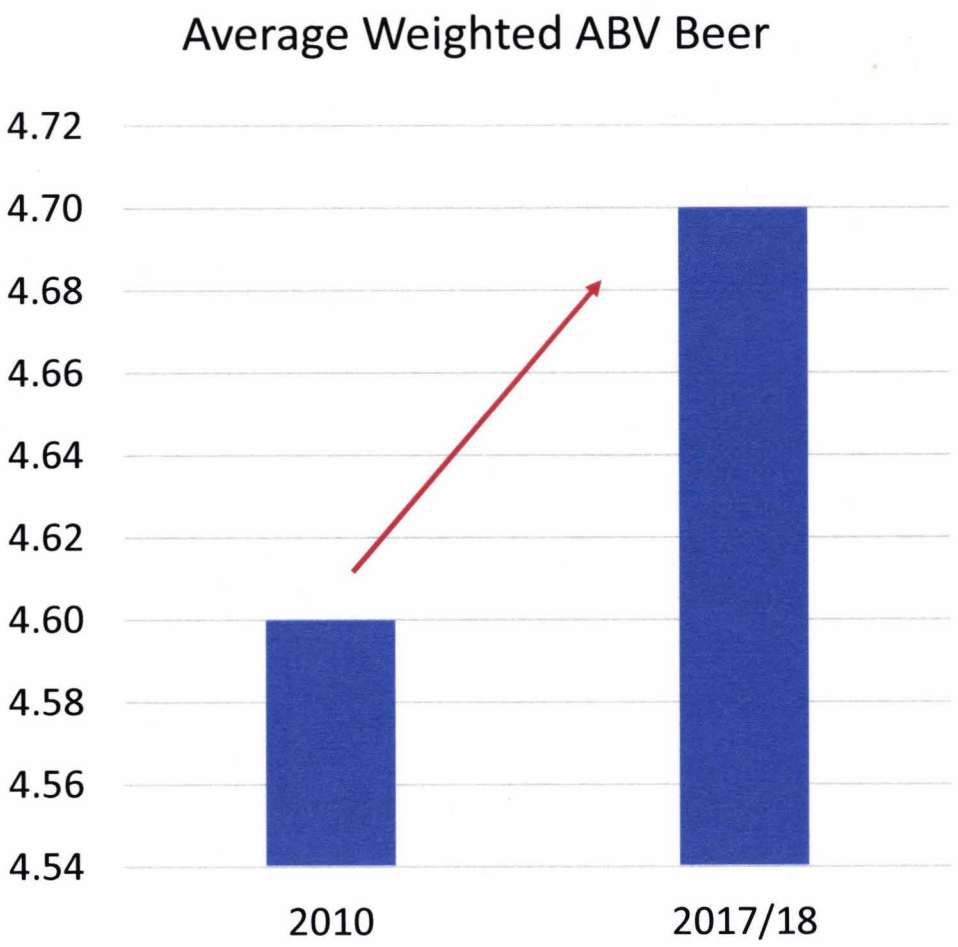
Alcohol Consumption Over Time

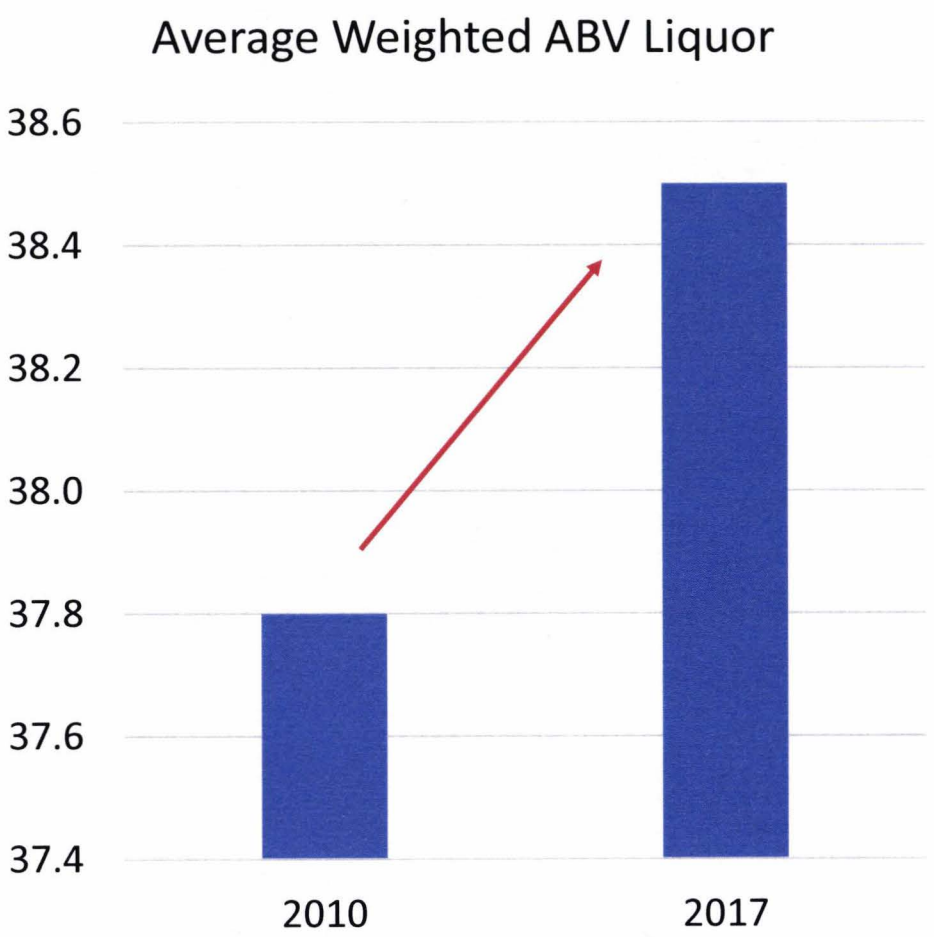
Do You Have Occasion to Drink Alcohol?



Source: Gallup Poll, 2019.

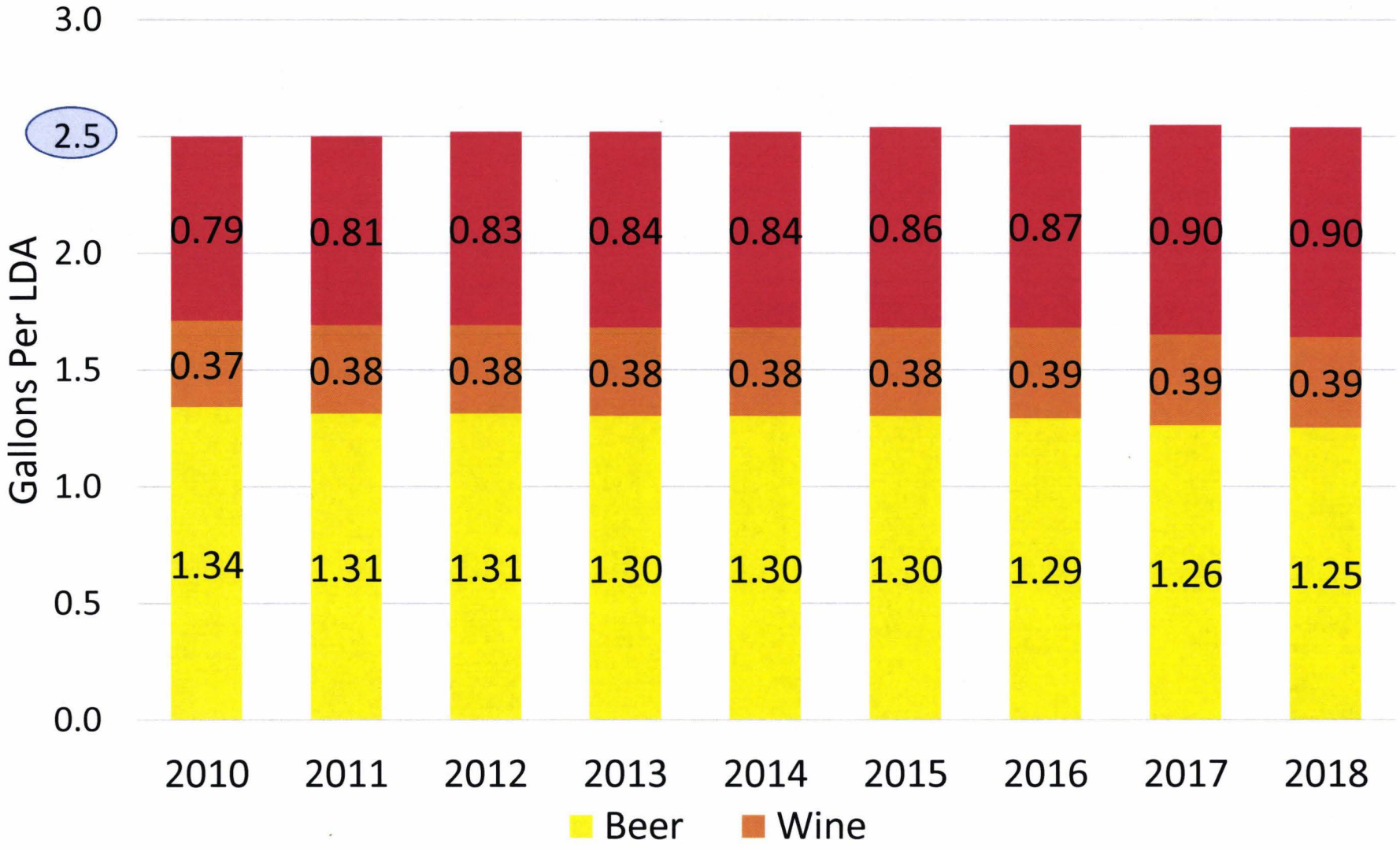
Growth in ABV for Beer and Liquor
2010 vs 2017





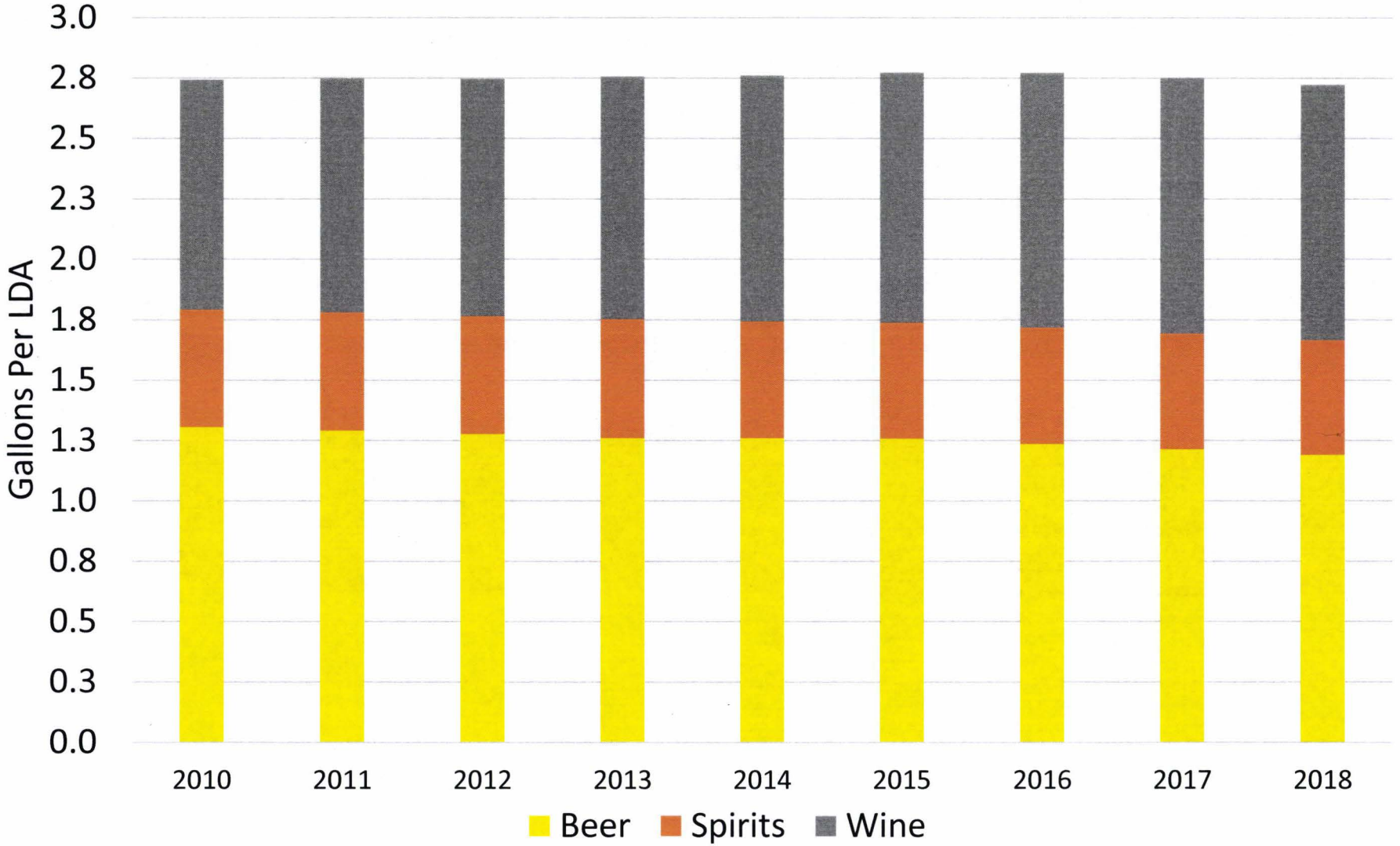
Source: NBWA, Industry Affairs – Calculated on average weighted ABV across top 100/150 brands

Total U.S. Ethanol Per Capita
2010 to 2018



Source: Compiled by NBWA from TTB, Discus and BIG, 2019 (2018 wine volumes estimated by NBWA)

Florida Ethanol Per Capita
2010 to 2018

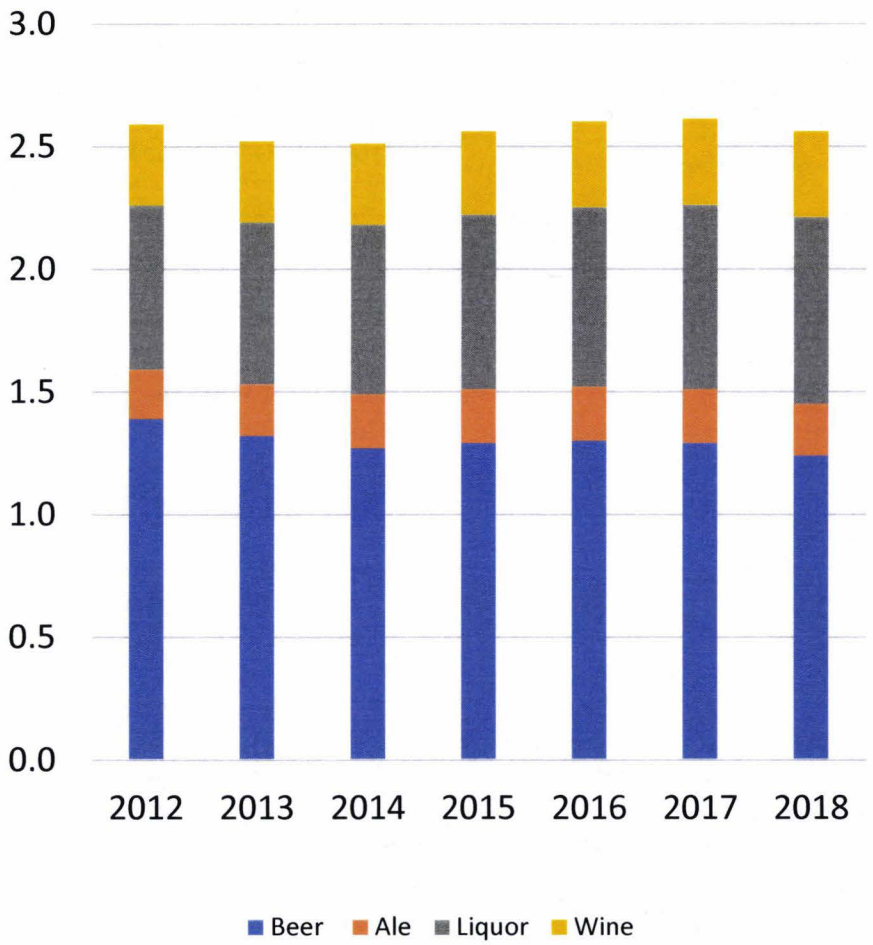


Source: Compiled by NBWA from Beer Institute, Discus and BIG, 2017

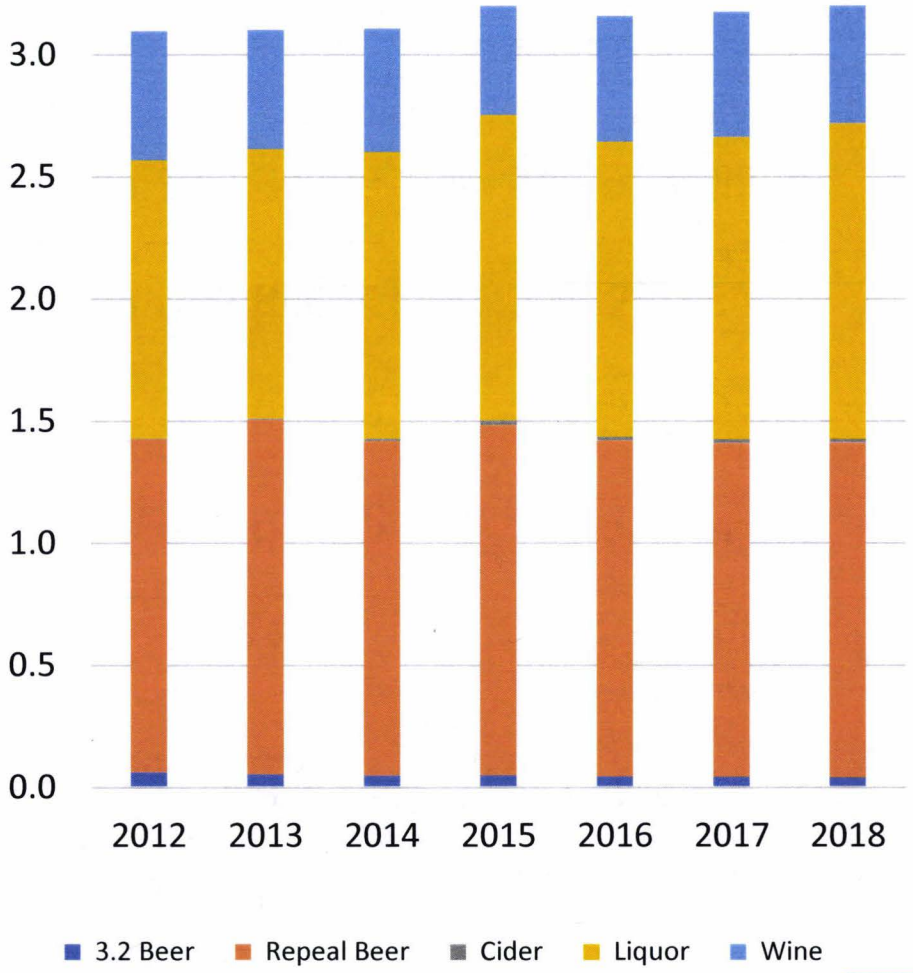
Texas vs Colorado

Total Per Capita Ethanol Consumption

Texas (TABC)



Colorado (Dept of Revenue)



2018 Economic Impacts

Florida Beer, Wine and Spirits Industries

Florida	Jobs	Wages	Output/Impact
Direct Impact	170,771	$5.426 Billion	$14.549 Billion
Supplier Impact	55,834	$3.936 Billion	$14.540 Billion
Induced (multiplier)	87,142	$3.936 Billion	$12.540 Billion
Total Impacts	313,747	$3.673 Billion	$10.937 Billion

Business Taxes (Licenses, Property, FUTA, SUTA)	$5.610 Billion
Consumption Taxes (FET, SET, Sales Taxes)	$2.610 Billion

Source: John Dunham & Associates: New York, 2019



The Current Three Tier System for Alcohol Beverages maintains an orderly and effectively regulated market for all industry players

- More choice and variety.
- Adapting to economic and demographic change
- Provide meaningful jobs, wages and tax benefits


Lester Jones, Chief Economist
National Beer Wholesalers Association
ljones@nbwa.org
Twitter @joneslester

Federal Unfair Trade Practices & the Three-tier System

Federal Unfair Trade Practices and the Three-tier System: Framework of a Federal and State Partnership and 2018-19 Investigations Approach Under the Federal Alcohol Administration Act

Robert M. Tobiassen, President, National Association of Beverage Importers, Inc. (NABI), Washington, DC and Former Alcohol and Tobacco Tax and Trade Bureau Chief Counsel, United States Treasury Department

Subcommittee on Business and Professions
Florida House of Representatives – October 16, 2019

Alcohol Beverage Law Trade Practices

The National Association of Beverage Importers, Inc. (NABI) was founded in 1935 and is the leading public policy advocacy group in Washington, DC for the importers of distilled spirits, wine, and beer/malt beverages.

Members of NABI operate within the traditional three-tier system and fully support that system which ensures consumers receive authentic brands of the alcohol beverages. NABI fully supports enforcement of unfair trade practice laws to ensure a level playing field in the distribution of these products.

Historic Perspective
And
Goals of Federal Enforcement
In Partnership With the States

Alcohol Beverage Law Trade Practices

The Historical "Why" Background?

- Prevention of the recurrences of the "social and political evils" giving rise to Prohibition. (S. Rep. No. 1215, 74th Cong., 1st Sess., Federal Alcohol Control Act, pages 6 -7.)
- National regulation of interstate commerce where States were unable or limited in regulation: "(W)e must do something to supplement legislation by the States to carry out their own polices. The liquor industry is too big and the constitutional and practical limitations on the States are so considerable that they alone cannot do the whole job." (79 Cong. Rec. 12178.)
- Public Policy Goals: Prevent excess consumption; protect the consumer; level playing field among industry members; and prevent monopolistic control and undue influence over retailers (and wholesalers in the areas of commercial bribery and consignment sales).

Evolution of Federal Unfair Trade Practices:

- 1840s to 1918 – Social & Political Evils
- 18th Amendment – "the manufacture, sale, or transportation of intoxicating liquors within, the importation thereof into, or the exportation thereof from the United States and all the territory subject to the jurisdiction thereof for beverage purposes is hereby prohibited"
- Prohibition Experience (1920 – 1933)
- Repeal (21st Amendment) in December 1933 resulted in concurrent jurisdiction at Federal and State levels

Evolution of Federal Unfair Trade Practices (cont.)

- *Codes of Fair Competition* under National Industrial Recovery Act (NIRA) from 1933 to 1935 – Self- regulation by industries via Presidentially approved Codes for wholesalers, importers, distillers, wineries, and breweries

- NIRA declared unconstitutional in May 1935 by Supreme Court in *Schechter Poultry Corp. v. United States*, 295 *U.S.* 495 (1935). Reason for detailed interstate commerce language in FAA Act.

- Federal Alcohol Administration Act in August 1935 (same month as social security enactment)

27 U.S.C. 201 *et seq.* – Key Goals of FAA Act:

- Keep criminal element out of alcohol industry using basic permit system (Sections 203 and 204)
- Regulate formulation, labeling, and advertising of alcohol beverages (Section 205(e) and (f))
- Regulate promotional and marketing trade practices that might lead to corruption or excessive consumption (Sections 205 (a) through (d)
- "Pull" and not "Push" system of consumer demand for retailer selection of brands of alcohol beverages

Alcohol Beverage Law Trade Practices

Importance of Three-tier System

- Federal trade practice provisions under the Federal Alcohol Administration Act and regulation of the alcohol beverage tax paying industry under the Internal Revenue Code of 1986 do not mandate the three-tier system **but** are structured to recognize its existence under State law.
- The absence of the three-tier system in a State would force TTB to revamp and reorganize its administrative, investigative, and enforcement models.
- Each tier is a check and balance on the other.

The Four TTB Unfair Trade Practices

Exclusive Outlet

Tied-house – Our Focus Today

Commercial Bribery

Consignment Sales

Alcohol Beverage Law Trade Practices

Tied-house (27 USC 205(b) and 27 CFR Part 6).

"To induce through any of the following means:"

1. Interest in license;
2. Interest in real or personal property;
3. Furnishing, giving, renting, lending or selling any equipment, fixtures, signs, supplies, money, services, or other thing of value SUBJECT to regulatory exceptions in Subpart D of Part 6 of Title 27, CFR (including recordkeeping requirements under section 6.81(b));
4. Paying or crediting for advertising, display or distribution service ("slotting fees");

Alcohol Beverage Law Trade Practices

5. Guaranteeing any loan or repayment of financial obligation;

6. Extending credit in excess of usual and customary credit period prescribed by regulations (27 CFR sections 6.65 (30 days)-6.67);

7. Quota sale ("Tie-in sales")

- Retailer
- Exclusion, in whole or in part, of products sold or offered for sale by others in interstate or foreign commerce. ("Primary Clause")
- One of three interstate or foreign commerce jurisdictional clauses

Alcohol Beverage Law Trade Practices

Indirect Inducements through Third Party Arrangements (Section 6.42, Tied-house; Section 8.23, Exclusive Outlet)

- Ballparks, Stadiums, Arenas (Industry Circular 75-16 (September 22, 1975)) https://ttb.gov/industry_circulars/archives/1975/75-16.html

- Las Vegas Cases TTB Press Release 11-4 (May 10, 2011)

Alcohol Beverage Law Trade Practices

Similar State Law (Section 205(f) often referred to as the penultimate paragraph)— In the case of *malt beverages (beer)*, there must be a similar State law.

- Similar means similar, not same or identical
- Broad interpretation of similarity

Is there any State law that applies to alcohol beverages under which the State could take action based on this set of fact?

Repeal of Tied-house law by Florida would hinder Federal enforcement for malt beverages.

Alcohol Beverage Law Trade Practices

"In the case of malt beverages, the provisions of subsections (a), (b), (c), and (d) shall apply to transactions between a retailer or trade buyer in any State and a brewer, importer, or wholesaler of malt beverages outside such State only to the extent that the law of such State imposes similar requirements with respect to similar transactions between a retailer or trade buyer in such State and a brewer, importer, or wholesaler of malt beverages in such State, as the case may be. In the case of malt beverages,..."

See also, Title 27, Code of Federal Regulations, Section 6.4(b) – for expanded application of section 205(f).

Alcohol Beverage Law Trade Practice

Current TTB Trade Practice Investigations and Enforcement Across the United States in Partnership with the State Alcohol Agencies

Alcohol Beverage Law Trade Practices

Action Forcing Event: Appropriations for FY 2017 and 2018, now extended through Fiscal Year 2019 (September 30, 2019)

"That of the amount appropriated under this heading, $5,000,000 shall be for the costs of programs to enforce trade practice violations of the Federal Alcohol Administration Act, (27 U.S.C. 201 et seq."

Fiscal Year 2020 Language – Pending

Evidences strong intent of Congress in trade practice enforcement to level playing field among industry members.

Enforcement Activities

Joint State/TTB efforts in Florida, Illinois, and California based on Press Releases. Activities in other States at least by TTB.

Florida *"Pay to play"* - https://ttb.gov/news/ttb-florida-authorities-conduct-joint-trade-practice-investigations.shtml

Illinois *"Pay to play"* - https://ttb.gov/press/press-release-fy-17-09-illinois-auth-conduct-joint-tp-invest.shtml

California *"Consignment Sales"* - https://ttb.gov/press/press-release-fy-18-03-joint-operation.shtml

Other States – TTB is conducting joint investigations without a press release.

Alcohol Beverage Law Trade Practices

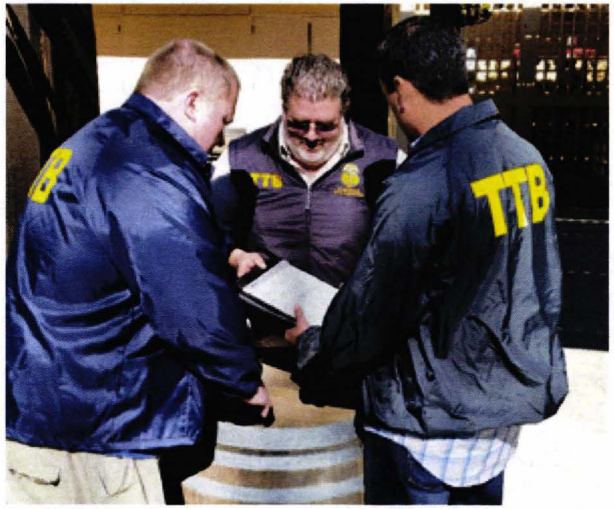
TTB Education Efforts

Sixteen trade practice seminars held in 2018 and 2019 in eight cities around the United States.

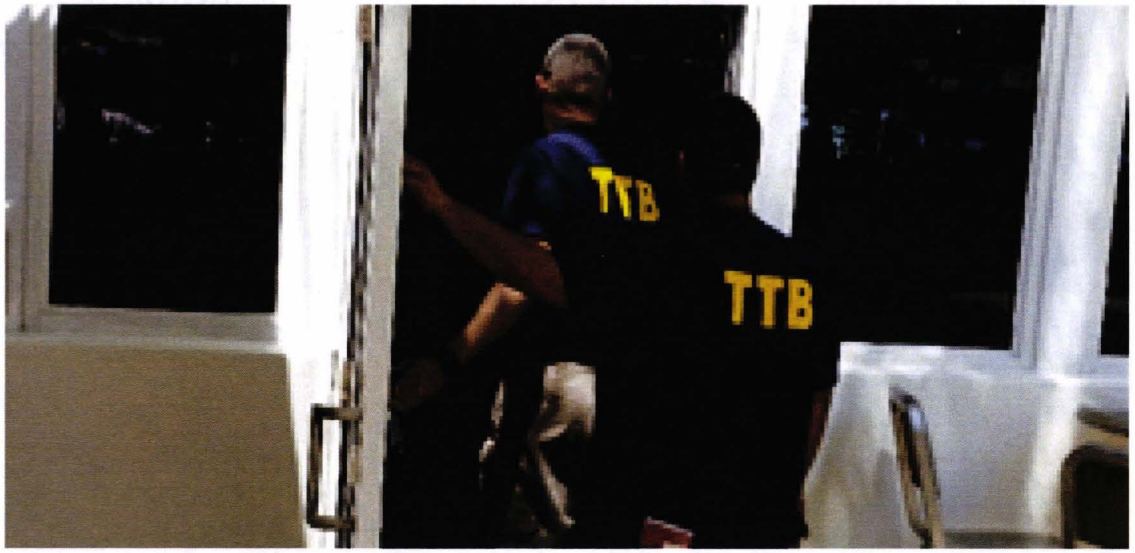
Themes from seminars:

- Joint investigations with State alcohol enforcement agencies are essential component of an effective and efficient trade practice investigation, especially State authority over retailers.
- Industry ignored previous enforcement efforts in 2009 and 2011, plus more recent OICs
- Stronger sanctions are appropriate to get the attention of the industry
- Higher dollar value OICs and administrative action against basic permits for suspensions. No suggestion of revocations yet
- These are "real investigations," not like a tax audit or a product integrity investigations (e.g., label integrity)
- Cadre of Special Operations Investigators (SOIs) recruited from Tobacco Smuggling and Diversion criminal investigations.

Alcohol Beverage Law Trade Practices







Alcohol Beverage Law Trade Practices

- **TTB Accepts Record $900,000 Offer in Compromise for Trade Practice Violations**
- FY-18-06
- Washington, D.C. — The Alcohol and Tobacco Tax and Trade Bureau (TTB) has accepted a $900,000 offer in compromise from Warsteiner Importers Agency Inc. for alleged violations of the trade practice provisions of the Federal Alcohol Administration (FAA) Act. This is the largest single offer in compromise for trade practice violations accepted by TTB to date.
- Warsteiner Importers Agency Inc. is alleged to have engaged in Tied House, Commercial Bribery, and Exclusive Outlet violations that either placed, or had the potential to place, the retailer's independence at risk. This offer in compromise was submitted to settle all possible alleged violations.
- TTB remains committed to actively enforcing the trade practice provisions of the FAA Act so that consumers can continue to enjoy a wide selection of products and that industry members can compete for those consumers in a fair and open marketplace.
- Please visit www.ttb.gov for additional information on prohibited trade practices or to see this and other offers in compromise that have been accepted.

Alcohol Beverage Law Trade Practices

TTB Accepts $325,000 Offer in Compromise for Tied House Violations

FY—19—04

Washington, D.C. — TTB has accepted a $325,000 offer in compromise from Elgin Beverage Co., a wholesaler in Bartlett, Illinois, for alleged violations of the tied house provisions of the Federal Alcohol Administration Act (FAA). This case developed out of the joint operation that TTB conducted with the Illinois Liquor Control Commission in September 2017.

Specifically, TTB alleges that Elgin aided and abetted another industry member in the use of a third party to pay retailers to carry and promote their products to the exclusion of competing products, which gave Elgin an unfair advantage over law-abiding competitors and ultimately limited consumer choice,

TTB remains committed to putting an end to anti-competitive practices that hurt law-abiding businesses and prevent consumers from enjoying a wide selection of products.

Please visit www.ttb.gov for additional information on prohibited trade practices or to see this and other offers in compromise that have been accepted.

Alcohol Beverage Law Trade Practices

TTB Accepts $1.5 Million Offer in Compromise for Trade Practice Violations FY—19—09

Washington, D.C. — TTB has accepted a $1.5 million offer in compromise from QAC, LLC (d/b/a Eagle Brands), a wholesaler in **Miami, Florida**, for alleged violations of the trade practice provisions of the Federal Alcohol Administration Act (FAA). This case developed out of the joint operation that TTB conducted with Special Agents from the Florida Division of Alcoholic Beverages and Tobacco (ABT), Miami District Office, targeting alleged "pay to play" schemes in the greater Miami area. This is the largest single offer in compromise that TTB has ever accepted, surpassing the Warsteiner case, which also resulted from the Miami joint operation.

Specifically, TTB alleges that Eagle Brands paid retailers to carry and promote its products to the exclusion of competing products and hid those payments as banquet events, credit card payments for rebates, or consumer samplings. TTB also alleges that Eagle Brands employees provided retailers with draft systems that were to be used exclusively for Eagle Brands products.

This case serves as an example of the types of unlawful activity that TTB highlighted in Industry Circular 2018-7. TTB remains committed to putting an end to anti-competitive practices that hurt law-abiding businesses and prevent consumers from enjoying a wide selection of products.

Please visit www.ttb.gov for additional information on prohibited trade practices or to see this and other offers in compromise that have been accepted.

Alcohol Beverage Law Trade Practices

TTB Trade Practice Investigation Results in Permit Suspension
FY—18—07 (August 23, 2018)

Washington, D.C. — On August 21, 2018, Modus Operandi Cellars, LLC, a bonded winery in St. Helena, California, served a one day suspension of its basic permit. This latest enforcement action clearly demonstrates TTB's determination to put an end to anti-competitive practices that hurt law-abiding businesses and prevent consumers from enjoying a wide selection of products.

Specifically, over the course of almost two years, Modus Operandi Cellars, LLC, engaged in consignment sales of wine to wholesalers who were not obligated to pay for the wine until after it had been sold to retailers. Consignment sales arrangements, like other unlawful trade practices, are used to gain an unfair advantage over law-abiding industry members and ultimately limit consumer choice.

The Modus Operandi Cellars, LLC, investigation was part of the joint operation that TTB conducted with the California Department of Alcoholic Beverage Control in March 2018.

TTB remains committed to actively enforcing the trade practice provisions of the Federal Alcohol Administration Act. TTB will continue to assess ways that enforcement actions can encourage voluntary compliance and discourage noncompliant industry members from treating those enforcement actions as a simple cost of doing business.

Thank you

What is the use of living, if it be not to strive for noble causes and to make this muddled world a better place for those who will live in it after we are gone?

Winston Churchill,
prime minister

Modernization in the Craft
Distilling Industry

House Business & Professions Committee
October 16, 2019
The Testimony of Robert Cassell,
Advisory Board Member-American Distilling Institute,
President-PA Distillers Guild,
Co-Founder of New Liberty Distillery,
Co-Founder-Connacht Whiskey Co. (Ireland)

Modernization in the Craft Distilling Industry

Good afternoon Representative Fitzenhagen, Representative Newton and distinguished members of the House Business and Professions Committee.

I am grateful for the time and opportunity you have granted me to discuss the craft segment of the Distilled Spirits Industry, and the impact of modernization on our business models.

The manufacturing segment of the distilled spirits industry has seen exponential growth of federally licensed distilleries in the craft segment in the last 15 years. When I opened one of the early US craft distilleries in 2005, there were approximately 40-50 licensed facilities in the entire country. That number is now closer to the 2,000 mark and continues to climb. The trend we are seeing mimics the same growth trajectory previous seen in the craft beer movement. All being part of the greater trend of consumers seeking and supporting artisanal purveyors, and the expectation of an experience at the point of manufacture. While these trends and consumer interest abound, the capital-intensive nature and route to markets create a unique risky challenge to a small business owner in the spirits industry.

As part of this growth the segment is booming in job creation. Statistically, the trend of craft distilling has also triggered a growth in Full Time Employee jobs by 50% over three years. Approximately 66% of these jobs are created from the production facility and tasting room staff. Statistically a craft distillery gets 34% of their total sales from direct to consumer activity through their tasting rooms, etc. These tasting rooms have the dual purpose of brand home, and sales channel. In this capacity it allows the business owner to provide the consumer with a brand-centric experience in their facility. Providing the unique platform from which to create consumer champions of your brands through focused communication of your points of differentiation. This is an imperative marketing tool for small craft spirits companies. At the end of the consumer experience, the business needs the means to convert that experience to a sale. This sale represents the contribution a distillery can bring to agricultural tourism.

The spirits industry has a proud heritage and symbiotic ties to the agricultural industry, and on a Federal Department of Agriculture level are recognized as "agricultural processors". The effect of the micro-distilling trend is an agricultural asset, and a key component of the value-add supply chain. As agricultural processors, we are proving to be an economic engine of regional agriculture. We create our product differentiation through

the feature and use of local ingredients. This results in a small farmers crop being purchased at prices benefiting both the farmer and the distiller: defining the value add supply chain. With the thousands of acres of crops turned into spirits, distillers are supporting and showcasing each respective states beautiful agricultural diversity and terroir.

Behind all of this excitement and potential lies a heavily regulated sector. Federally, a distiller in the United States in monitored and each product vetted through a series of submissions, standards, and testing. A federally licensed distillery is required to monitor and report all aspects of it spirits production to the hundredth of a gallon (0.01 gallons/ 37mL). All our products are dictated by the Code of Federal Regulations, subject to formula approval through the federal government as well as label approvals. Ingredients used must comply with US Department of Agriculture GRAS standards (Generally Recognized As Safe). As a distilled spirits manufacturer you are required by law to submit three separate detailed operational reports each month demonstrating your raw material usage rates, yields, in progress inventory, finished goods inventory, and removed from bond spirits (Taxable spirits). In short, product safety and tax liability are being continually monitored by the federal government. Before a bottle ever gets filled or a label applied, it has been thoroughly vetted by the Federal Government and held to well established published standards. Upon completion of the licensing and approval processes, a distiller is now able to bring a product to market.

A small business in the distilling industry is not much different than many other small consumer goods businesses looking to sell their products. We look to test market our products in a small area with minimal capital exposure, and upon success, scale the business and our outlets and means for sales opportunities. Traditionally, that has been the three tier means of distribution. The three tiers consist of the producer, distributor, and retailer. This model can work, and has worked. But as with anything, times change. Lets explore the current three-tier marketplace, from the small producers perspective.

A distributor acting as the middleman *can* serve many key roles to the producer. They have sales team covering large geographic regions, buyer relationships at the retail accounts, as well as strong logistics systems. All of this being dependent on your distributor taking on your brands, and your means of access to that sales force. Gaining mindshare of those sales representatives is key to scaling your business in the 3 Tier model. Consolidation and vast portfolios has made access through the three tiers challenging for an upstart distillery. As of Monday October 14th, Southern-Glazers Florida segment of their website shows they carry 14,538 SKUs. The people who own and work at that company are hard working people, but that is a lot of SKUs to take care of. They can't support the needs of a small in state craft distiller when they have that many SKUs, most of ground level sales people can't even keep track of that many products. The inventory levels they need to carry to support possible sales of those SKUs are staggering. And adding another small brand to the mix, is a nettle in the haystack but with a financial burden of purchased inventory. Frankly, the owners of these houses are right not to focus sales forces on a small, emerging, and unproven brands, because it makes fiscal sense for their respective companies. Wholesalers and retailers can't afford the excess inventory of an

unproven, unknown brand. It represents one of the most common reasons for a retailer or wholesaler to not take on a new brand. When given the option, as business owners, we have to have to ability to make smart fiscal decisions, but decisions require options. However, that is also more reason why existing codes need modernized to permit a proof of concept business model before entering the three-tier marketplace.

As in any business, the ability to demonstrate a successful proof of concept is imperative to the ultimate success of the business as well as determining the full capital requirements to scale the business in a meaningful manner. Due to the capital required in equipment, regulatory environment, and tax structure, the spirits industry has many barriers to being able to demonstrate Proof of Concept. An established proof of concept mitigates financial risk for all parties involved. It also allows a brand owner to convey to their wholesale partner where and to whom the brand can work. Together with this information, they can best identify the potential market share and targets for success.

This direct to consumer capability is a key sales channel for a startup company in any industry, and the craft spirits industry is no different. In some states, like my home state of Pennsylvania, we have been fortunate to see modernization take hold and allow for this to be possible. We have been able to test brands and products within our brand home before bringing to market. Not having to do work arounds of constant new label creations but instead focusing efforts on meaningful brand elements.

As distillers and brand owner, once we have established financially sustainable proof of concept businesses, we need the traditional 3-tier system. As mentioned earlier, the system then provides a means to scale a brands distribution, sales, and logistics footprint. Ultimately a distillers brand success is measured by it ability to have product that works through the 3 tier system. All of this begins with a successful proof of concept.

In my home state of Pennsylvania we have been granted many of the liberties that small breweries and wineries have, with some exceptions. Within my state, we call a craft distillery a "Limited Distillery" defined as and permitted the following:

-produce and sell up to 100,000 gallons
-sell direct to consumer on site by the glass, cocktail, and bottle (9am-11pm)
-ship direct to consumer within the commonwealth via licensed carrier
-sell PA made beer & wine, by the glass
-5 satellite locations permitting us the same abilities as our Tasting Room
-limited to 50,000 gallons of sales direct to on premise
-ability to setup and sell at farmers markets
-exposition permits up to 30 days
-10 store listing, upon request
-pay a 6% sales tax, as well as 10% drink tax in Philadelphia & Allegheny counties
-all licensing capabilities are non-transferrable and contingent on the manufacture of distilled spirits occurring on-site.

Of note, once a distillery exceeds the 100,000 gallon threshold, they lose the satellite location right, but still maintain ability to sell direct to consumer at their brand home/distillery. In working with the legislators, the goal of this was to allow a business

owner the runway to create a sustainable business in a proof of concept environment and build the necessary capital to get into a 3 Tier distribution system with meaningful consumer awareness. Our mutual goal was to create an environment to expose consumers to our brands, tell them our story, and unique selling points. As would be standard in the sales of any consumer product. The business's goal is to create brand champions who would continue to buy in the regular 3 Tier marketplace.

While still emerging in years since this key legislation passed, we have seen the fruits of our labor in Pennsylvania. By the means of quality legislation, and the industry it created, the result was a ground swell of new skilled manufacturing and service jobs. I sit here before you today to emphatically state we went from three to 134 licensed distilleries in Pennsylvania in 7 years. The result was a creation of nearly a thousand new jobs, as well as a value add to the local agricultural supply chain and tourism. As shown in the public domain of the Pennsylvania Liquor Control Boards website, sales of distilled spirits within the state have grown, not decreased, with the proliferation of these craft distilleries. With the result being more tax revenue for the state and continued increased deposits into the state's general fund.

In any debate on modernization, there is always the fear that change will be bad. As we have demonstrated in Pennsylvania, by working with our brokers and stakeholders we created a system that is mutually beneficial and granted the appropriate freedoms for a business to incubate in a manner that is respectful and not taking revenue away from our future distribution partners. Ultimately allowing a consumer to make the choice. For example, in Pennsylvania a Limited Distillery could be exclusively an online retailer and ship bottle by bottle to a consumer's doorstep, up to the 100,000 gallon limit. However, that is unlikely to happen given the basic economics incurred by the consumer. While shipping a bottle at a time is a means for us to get our unique offerings to a consumer, the consumer is unlikely to continue purchasing in that manner due to the shipping cost relative to the purchase price. This is not a long-term economically solid business model for a distiller. While it permits proof of concept, a traditional retail footprint is necessary, as this model does not permit volume due to the incremental shipping costs. It is at this point, that fiscal sense would drive a distiller to have partners in the 3 Tier system, as partnering with them and utilizing their robust logistics capabilities enables us to deliver a better fully loaded price to the consumer and ultimately build a brand in the marketplace. But it all starts with the ability to sell that first bottle, then graduating to the 3 Tier system.

The intent is not to undercut or to take business away from I view as my partners in any state (the wholesalers, retailers, restaurants, and bars), and particularly here is Florida. I feel this could turn into positive opportunity for the state to demonstrate its forward direction and modernization of liquor code as it pertains to the manufacture and retail sales of distilled spirits. Selling on site is a privilege and responsibility, which we take seriously. As a distilled spirits manufacturer we strive to perform those actions in a controlled and respectful manner as a business goal.

I thank the committee for its time and consideration today and am happy to take any questions.

Florida Craft Beer Modernization

Florida Craft Beer Modernization

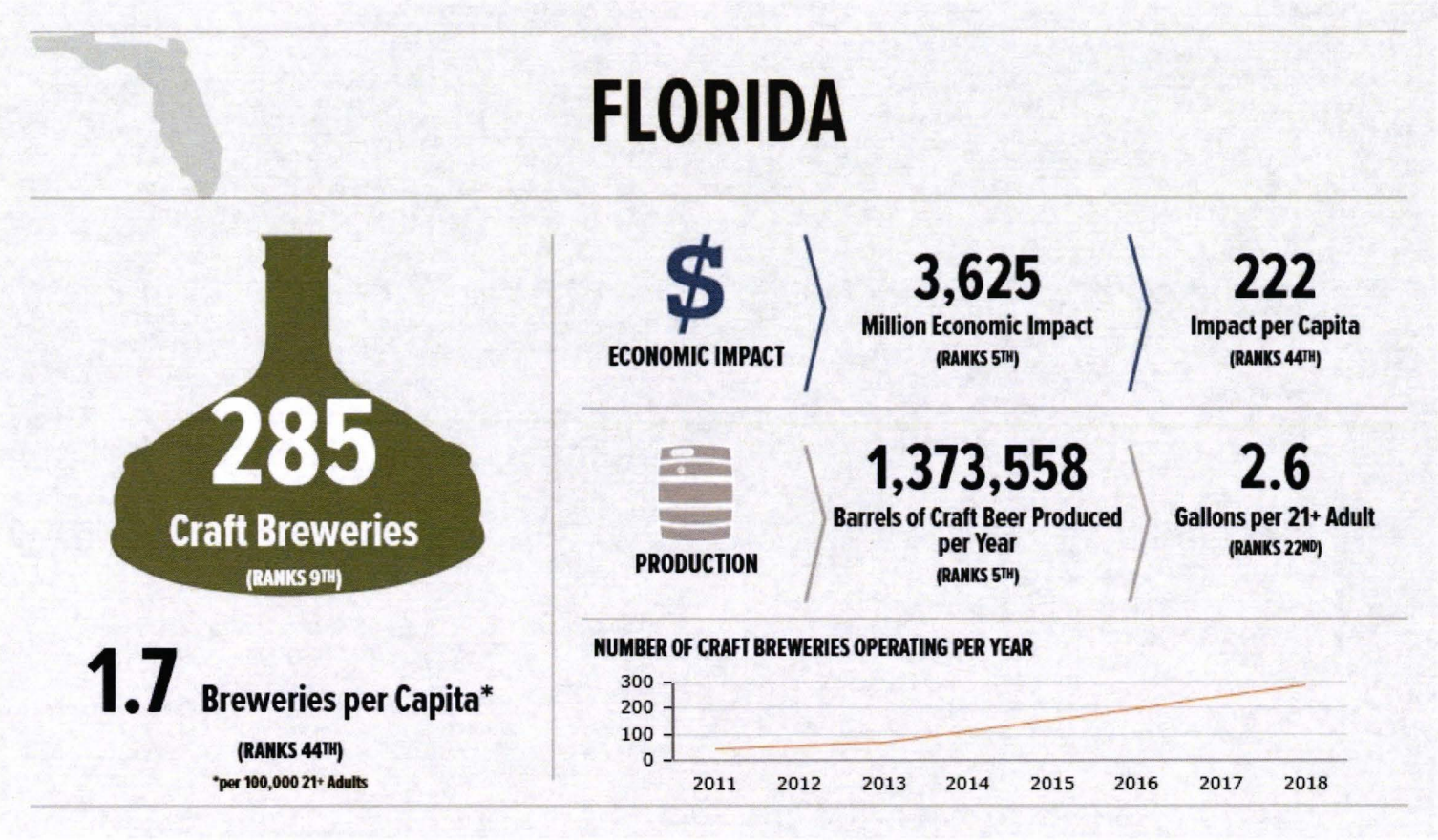
Josh Aubuchon

October 16, 2019

Holland & Knight

Copyright © 2019 Holland & Knight LLP. All Rights Reserved

Florida Facts and Figures (2018)*



*Data from the Brewers Association

Holland & Knight

Self-Distribution

- What is it?
  - The ability of a brewery to sell and deliver beer directly to a licensed vendor without the necessity of a distributor.
  - Usually limited by either the production amounts of the brewery or limited by the amount which may be distributed by the brewery.
- Currently, 37 states allow some form of self-distribution:
  - Texas: up to 125,000 barrels
  - North Carolina: up to 50,000 barrels
  - Arizona: up to 40,000 barrels
  - Indiana: up to 30,000
  - Iowa: unlimited
  - California: unlimited

Beer Franchise Laws

- Found in Section 563.022, F.S.
  - Enacted in 1987. (Ch. 87-63, Laws of Florida)
  - Provides a brewery's rights may be sold, assigned, or purchased *without compensation to the brewery.*
  - Contracts are perpetual and subject to the whim of the distributor (they may terminate at any time).
  - Requires exclusive territory agreements.
- Gives distributor's a 120-day period for any noncompliance:
  - 30 days to submit plan of corrective action.
  - 90 days to cure.
- In contrast, wine and spirits *do not* have franchise laws similar to beer.
- Termination by a manufacturer is extremely difficult.
- Breweries required to sign with a distributor in order to get their products into the market.

Franchise Reform | Free Market Distribution

- **North Carolina** (2019): Breweries producing less than 25,000 barrels can terminate with five day's notice and paying "fair market value."

- **Maine** (2019): Breweries may terminate so long as they are less than 3% of a distributor's sales, give 90 days' notice, and pay "fair market value." (1x or 2x gross profits)

- **Maryland** (2019): Breweries producing less than 20,000 barrels may terminate without cause after providing 45 days' notice and paying "fair market value" and repurchase inventory.

Franchise Reform | Free Market Distribution

- **Vermont** (2018): Breweries may terminate so long as they are less than 3% of a distributor's sales by volume, produce less than 50,000 barrels per year.

- **New York**: Breweries may terminate so long as they are less than 3% of a distributor's sales and produce less than 300,000 barrels per year and pay fair market value.

- **Washington**: Franchise laws do not apply to breweries producing less than 200,000 barrels annually; termination upon 60 days' notice

- Currently, **Alaska**, the **District of Columbia**, and **Hawaii** do not have beer franchise laws.

Craft Beer Modernization in Florida

- *Self-Distribution*
  - Permitted up to a certain barrel production. (50,000 to 120,000 barrels)
  - Territories determined by the brewery.
  - May sign with a distributor in other territories.
  - May sell their distribution rights.
  - Limited "hot-shot" delivery for breweries that have already signed with a distributor in a brewery's home territory.
- *Free Market Distribution (Franchise Reform)*
  - Termination with or without cause.
  - Brewery must be under a certain percentage of a distributor's sales.
  - Definition of "fair market value."
  - Franchise exemption for breweries below a certain barrel production amount.
  - Prohibition on the sale, assignment, or transfer of a brewery's rights without their express consent; brewery entitled to percentage of the sales and right of first refusal.

Questions?

Josh Aubuchon
joshua.aubuchon@hklaw.com

Thank you!