

SENATE BILL REPORT

SB 5549

As Reported by Senate Committee On:
Labor & Commerce, February 20, 2019
Ways & Means, March 21, 2019

Title: An act relating to modernizing resident distillery marketing and sales restrictions.

Brief Description: Modernizing resident distillery marketing and sales restrictions.

Sponsors: Senators Liias, King, Hunt and Braun.

Brief History:

Committee Activity: Labor & Commerce: 2/18/19, 2/20/19 [DPS-WM].
Ways & Means: 3/14/19, 3/21/19 [DP2S, DNP, w/oRec].

Brief Summary of Second Substitute Bill

- Modifies on-premises and off-premises liquor sales privileges of distilleries and craft distilleries.
- Limits the percent and number of other producers' products that distilleries and craft distilleries may offer for sale to customers, relative to their own products.
- Establishes an off-site tasting room license available for distilleries and craft distilleries, to operate up to two off-site tasting rooms, with a license fee of \$2,000.
- Requires the tasting room sales to be at least 70 percent from the sales of products for off-premises consumption and includes an annual report on the source of sales revenue.
- Allows the sale of adulterated spirits sold for on-premises consumption, without the 2-ounce limit that is imposed on unadulterated samples.
- Authorizes distilleries, craft distilleries, and wineries to jointly operate off-site tasting rooms, and authorizes conjoined consumption areas for distilleries, craft distilleries, wineries, and breweries whose production facility property is in direct physical proximity to each other.
- Authorizes distilleries, craft distilleries, and spirits certificate of approval holders to provide branded promotional items of nominal value to nonprofit entities.

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.

- Prohibits anyone under the age of twenty-one from entering or remaining on the distillery's premises in an area where alcohol is sampled, sold, or served, or on the premises of an off-site tasting room.
- Exempts certain unaggregated financial, proprietary, or commercial information obtained from distillery applicants and licensees from disclosure under the state Public Records Act.

SENATE COMMITTEE ON LABOR & COMMERCE

Majority Report: That Substitute Senate Bill No. 5549 be substituted therefor, and the substitute bill do pass and be referred to Committee on Ways & Means.

Signed by Senators Keiser, Chair; Conway, Vice Chair; King, Ranking Member; Saldaña, Walsh and Wellman.

Staff: Richard Rodger (786-7461)

SENATE COMMITTEE ON WAYS & MEANS

Majority Report: That Second Substitute Senate Bill No. 5549 be substituted therefor, and the second substitute bill do pass.

Signed by Senators Rolfes, Chair; Frockt, Vice Chair, Operating, Capital Lead; Braun, Ranking Member; Brown, Assistant Ranking Member, Operating; Honeyford, Assistant Ranking Member, Capital; Bailey, Becker, Billig, Conway, Hasegawa, Hunt, Keiser, Liias, Pedersen, Schoesler, Wagoner and Warnick.

Minority Report: Do not pass.

Signed by Senators Darneille and Van De Wege.

Minority Report: That it be referred without recommendation.

Signed by Senator Carlyle.

Staff: Alia Kennedy (786-7405)

Background: License Privileges of Distilleries and Craft Distilleries. The Liquor and Cannabis Board (LCB) licenses people engaged in distilling—which is deemed an agricultural practice—under different license types, including the following:

- Distiller License—the license is for a person engaged in distilling, including blending, rectifying, and bottling. The license fee is \$2,000 per year, unless a person meets a different specific category.
- Craft Distillery License—the license is for distillers producing 150,000 gallons or less of spirits with at least half of the raw materials in the production grown in Washington. The license fee is \$100 per year.

The LCB also licenses commercial chemist stills, stills for educational purposes at universities, and fruit and wine distilleries. A person may alternatively manufacture spirits

under a separate manufacturer's license, and a certificate of approval is available for out-of-state distillers who sell spirits to purchasers in Washington State.

A distillery or craft distillery may sell spirits of its own production for consumption off the premises. A distillery or craft distillery may also contract distilled spirits for, and sell contract distilled spirits to, holders of distillers' or manufacturers' licenses, or for export. Additionally, distilleries and craft distilleries may (1) sell or provide customers with free 0.5 ounce or less samples of spirits, which may be adulterated, or (2) sell adulterated samples of spirits of their own production, water, and/or ice to persons on the premises of the distillery. A person is limited to sampling no more than a total of two ounces of spirits on the distillery premises per day.

Any distillery or craft distillery may act as a retailer and distributor of spirits of its own production to retailers. Generally, a distillery or craft distillery acting as a distributor and retailer must comply with laws and rules applicable to distributors and retailers. A distillery or craft distillery may accept orders for spirits from customers in person at a licensed location, by mail, telephone, or the Internet—if Internet-sales privileges are requested, or by similar methods, and deliver spirits to an adult age twenty-one years or over subject to restrictions on hours of delivery, age-verification of the recipient, and packaging and labeling requirements.

A distillery or craft distillery may apply to the LCB for an endorsement to sell bottled spirits of its own production at a qualifying farmers market. No sampling of spirits is authorized at a farmers market. Before authorizing a farmers market to allow to sell bottled spirits at its farmers market location, the LCB must notify appropriate local governments and certain nearby entities and public institutions. The LCB may withdraw any farmers market authorization for any violation of liquor laws or rules.

When selling spirits in bottles to consumers for off-premises consumption, the 17 percent spirits retail license issuance fee applies to spirits sales by distilleries, but not to spirits sales by craft distilleries.

Tied House Laws and Exceptions. Business practices and financial interests of liquor industry businesses are restricted under the so-called tied house laws. Tied house laws generally prohibit an industry member from advancing and a retailer from receiving moneys or moneys' worth under an agreement, written or unwritten, or by means of any other business practice or arrangement. Tied house laws also generally prohibit one industry member from having a direct or indirect financial interest in another industry member or retailer, except for specific exceptions. The term "industry member" is defined as a licensed manufacturer, producer, supplier, importer, wholesaler, distributor, authorized representative, certificate of approval holder, warehouse, and any affiliates, subsidiaries, officers, directors, partners, agents, employees, and representatives of any industry member.

An exception to the tied house laws authorizes a distiller to hold a spirits, beer, and wine restaurant license for the purpose of selling liquor at a spirits, beer, and wine restaurant premises on the property on which the primary manufacturing facility of the distiller is located or on contiguous property owned or leased by the distiller. A similar exception exists for breweries and wineries.

Another exception to the tied house laws authorizes industry members to provide retailers branded promotional items that are of nominal value, singly or in the aggregate. Promotional items must be used exclusively by the retailer or its employees and may not be passed along to customers or be targeted to or appeal principally to youth. Also, domestic wineries and microbreweries may provide branded promotional items that are of nominal value, singly or in the aggregate, to a nonprofit charitable corporation or association exempt from taxation under Section 501(c)(3) of the Internal Revenue Code, for use consistent with the purpose or purposes entitling the nonprofit to the exemption.

Public Records Act. The Public Records Act (PRA) requires state and local agencies to disclose requested written records to the public for inspection and copying upon request, unless the information fits into one of the various specific exemptions under the PRA or as otherwise provided in law. For example, certain financial, commercial, and proprietary information is exempt from public inspection and copying. The stated policy of the PRA favors disclosure and requires narrow application of the listed exemptions.

Summary of Bill (Second Substitute): License Privileges of Distilleries and Craft Distilleries. In addition to their own spirits, distilleries and craft distilleries may sell, for off-premises consumption, spirits produced by another distillery or craft distillery, or vermouth or sparkling wine products produced by a licensee in Washington State. For craft distilleries, when selling bottled spirits produced by another distillery or craft distillery for off-premises consumption the craft distillery must pay the 17 percent license issuance fee on sales of these products.

Distilleries and craft distilleries may serve samples of spirits, free or for a charge, and sell servings of spirits, vermouth, and sparkling wine to customers for on-premises consumption, at the premises of the distillery indoors, outdoors, or in a combined indoor-outdoor area, and at the distillery's off-site tasting rooms. When spirits samples are served unadulterated, samples must be 0.5 ounces or less of spirits, and a person is limited to receiving or purchasing, for on-premises consumption, no more than two ounces total of spirits that are unadulterated.

Distilleries and craft distilleries may sell servings of spirits of the distillery's own production or spirits produced by another distillery or craft distillery licensed in Washington State, which must be adulterated with water, ice, other alcohol entitled to be sold or served on the licensed premises, or nonalcoholic mixers. Also, servings of vermouth and other sparkling wine products may be sold for on-premises consumption at a distillery or craft distillery.

If a distillery or craft distillery provides or sells spirits or other alcohol products authorized to be sold or provided to customers for on-premises or off-premises consumption that are produced by another distillery, craft distillery, or licensee in Washington State, then at any one time no more than 25 percent of the alcohol stock-keeping units offered or sold by the distillery or craft distillery at its distillery premises and at any licensed off-site tasting rooms may be vermouth, sparkling wine, or spirits made by another distilled spirits producer or licensee. If a distillery or craft distillery sells fewer than 20 alcohol stock-keeping units of products of its own production, it may sell up to five alcohol stock-keeping units of another distillery, craft distillery, or licensee in Washington State.

No person under age twenty-one may enter or remain on a distillery or craft distillery's premises in an area where alcohol is sampled, sold, or served, or on the premises of a distillery's licensed off-site tasting room unless they are attending a private party secured by a private banquet permit. Any person serving or selling spirits or other alcohol authorized to be served or sold by a distillery or craft distillery must obtain a class 12 alcohol server permit. A distillery or craft distillery may also sell nonalcoholic products at retail.

A distillery or craft distillery may no longer apply to the LCB for an endorsement to sell bottled spirits of its own production at a qualifying farmers market.

New License for Off-Site Tasting Rooms. A tasting room license is established that authorizes the operating of up to two off-site tasting room at which the distillery may sample, serve, and sell spirits and alcohol products. Tasting rooms may be indoors, outdoors, or a combined indoor-outdoor area, and are administratively tied to a licensed production facility. At least 70 percent of the sales revenue from each tasting rooms must be from off-premises—bottles—sales and on-premises—beverages—are limited to no more than 30 percent of sales. Distillers with an off-site tasting room must file an annual report regarding its revenue sources.

The fee for each off-site tasting room license is \$2,000. No separate license is required for the one on-site tasting room licensees may operate at their distillery production facility. Except for an event in which a private party has secured a private banquet permit, after 9:00 p.m., no person under age twenty-one may enter or remain on the premises of a tasting room. Any person serving or selling spirits or other alcohol authorized to be served or sold by a craft distillery must obtain a class 12 alcohol server permit.

Authorization for Jointly Operated Tasting Rooms and Conjoined Consumption Areas with Wineries and Breweries. Of the off-site tasting rooms authorized under law, any distillery, craft distillery, domestic winery, or any combination of these licensees may jointly occupy and operate up to two off-site locations, which may be indoors, outdoors, or in a combined indoor-outdoor location, at which the licensees may sample, serve, and sell products of their own production and products authorized to be sampled, served, and sold under the terms of their licenses. The licensees must maintain separate storage of products and separate financials.

Any domestic brewery, microbrewery, domestic winery, distillery, or craft distillery, or any combination of these licensees, whose property parcels or buildings are located in direct physical proximity to one another may share a standing or seated tasting area for patrons to use, which may be indoors, outdoors, or a combined indoor-outdoor area. Each licensee may sample, serve, and sell products the licensee is authorized to sample, serve, and sell under the terms of their respective licenses, for on-premises consumption, in the jointly operated consumption area. Each licensee must use distinctly marked glassware or serving containers to identify the source of any product being consumed.

When operating any jointly operated off-site tasting room or conjoined consumption area of production facilities, licensees must comply with the applicable laws and rules relating to retailers. Licensees must also comply with all applicable laws and rules relating to sampling

and serving, as may be allowed by their license type. All licensees who participate in the authorization for joint off-site tasting rooms or the authorization for conjoined consumption areas at production facilities, must share staffing resources. All participating licensees are jointly responsible in the event of any violation or enforcement issues, unless it can be demonstrated that the violation or enforcement issue was due to one or more licensee's specific conduct or action, in which case the violation or enforcement shall apply only to those identified licensees.

For the jointly operated off-site tasting room or conjoined consumption areas, every person who participates in the sale or service of samples or servings of spirits must obtain a class 12 alcohol server permit and if serving beer and wine must obtain either a class 12 or class 13 permit.

Tied House Laws and Exceptions. It is established that nothing in the "moneys' worth" prohibition in the liquor industry tied house laws prohibits a distillery, craft distillery, or spirits certificate of approval holder from providing branded promotional items which are of nominal value, singly or in the aggregate, to a 501(c)(3) nonprofit charitable corporation or association, for use consistent with the purpose or purposes entitling the nonprofit to the exemption.

Public Records Act. A new exemption is added to the Public Records Act that protects unaggregated financial, proprietary, or commercial information submitted to or obtained by LCB in applications for distillery or craft distillery licenses, or in any reports or remittances submitted by licensees.

EFFECT OF CHANGES MADE BY WAYS & MEANS COMMITTEE (Second Substitute):

- Prohibits anyone under the age of twenty-one from entering or remaining on the distillery's premises in an area where alcohol is sampled, sold, or served, or on the premises of an off-site tasting room.
- Exempts certain unaggregated financial, proprietary, or commercial information obtained from distillery applicants and licensees from disclosure under the state Public Records Act.
- Changes "unadulterated" to "adulterated" when referring to certain sales of spirits for on-premises consumption.

EFFECT OF CHANGES MADE BY LABOR & COMMERCE COMMITTEE (First Substitute):

- Limits distilleries to two off-site tasting rooms.
- Removes farmers' markets entirely, including current law provisions.
- Raises the licensing fee to \$2,000 for each off-site tasting rooms.
- At least 70 percent of the sales revenue from each tasting rooms must be from off-premises—bottles—sales; limited to no more than 30 percent of sales from on-premises sales.
- Requires an annual report of revenue sources for distillers who sell adulterated beverages—that are limited to 30 percent of sales.

- Makes clarifying changes to the enforcement provision for jointly operated consumption areas.
- Changes the effective date to January 1, 2020.

Appropriation: None.

Fiscal Note: Available.

Creates Committee/Commission/Task Force that includes Legislative members: No.

Effective Date: Ninety days after adjournment of session in which bill is passed.

Staff Summary of Public Testimony on Original Bill (Labor & Commerce): *The committee recommended a different version of the bill than what was heard.* PRO: There are 133 craft and general distillers in Washington State. Half of the craft distillers only sell their products from their tasting rooms. The four tasting rooms are the same amount allowed for wineries. This bill will be a lifeline for those small distillers who are struggling to stay in business. The fiscal note indicates the LCB only expects 35 additional tasting rooms under this bill. When compared to the 7141 other businesses licensed to sell alcohol, this bill is not a big expansion. The authorized cross-sales are very limited, with only 25 percent of the sales allowed for other producers' products and will not operate as a retail outlet. The cross-sales will include the license issuance fee of 17 percent. Lifting the cap on unadulterated beverages will make the provisions consistent with the craft beer and winery laws. Sixty-five percent of the craft distillers do not have a distributor and with many of the former liquor stores closed, we have limited marketing abilities that are away from high traffic and tourism areas. Distillers have the lowest percent of licensing violations compared to the other industries.

CON: We find the tasting room provisions to be less objectionable to the expansion of spirits sampling at farmers markets. The markets are family oriented events and are often held on Sunday mornings, which is an awkward time for serving spirits. While we support Washington branded spirits, we believe there should be uniform requirements for the service of alcohol in on-premises and off-premises sales and consumption.

OTHER: We are concerned about the lack of requirements similar to those required for service of alcohol at restaurants and night clubs. Our businesses must serve extensive meals for long periods of time and are limited in the amount of floor space we can dedicate. The bill will allow the service of mixed drinks without the requirement of a tavern license or the additional associated licensing requirements. This will allow the creation of a bar-like environment where minors will be present. It creates new disparities that other licensees will now seek.

Persons Testifying (Labor & Commerce): PRO: Senator Marko Liias, Prime Sponsor; Jim Hedrick, Washington Distillers Guild; Justin Stiefel, Heritage Distilling.

CON: Seth Dawson, Washington Association for Substance Abuse Prevention; Brad Tower, Washington Liquor Store Association.

OTHER: Zachary Lindahl, Washington Hospitality Association; Chris Thompson, LCB.

Persons Signed In To Testify But Not Testifying (Labor & Commerce): No one.

Staff Summary of Public Testimony on First Substitute (Ways & Means): *The committee recommended a different version of the bill than what was heard.* PRO: Washington's distilleries are struggling. Distilleries make up less than 1 percent of the 18,000 liquor licenses in the state and less than 2 percent of the spirits licenses. Average distillery revenue in Washington compares poorly to the national average. Local businesses are serving local distillery products. The bill does not allow distilleries to act as a bar or as a retail outlet for another producers' product. This bill gives distilleries the ability to grow their business by increasing visibility of their products.

CON: There is no shortage of opportunities for people to obtain and consume alcohol in this state. It is a broken message to tell people to not drink and drive but then make alcohol available for consumption virtually anywhere they drive. Alcohol is inherently unhealthy so there is concern with legislation that promotes this product.

Persons Testifying (Ways & Means): PRO: Jim Hedrick, Washington Distillers Guild; Mhairi Voelsgen, Brovo Spirits; Jeff Robinette, Chambers Bay Distillery.

CON: James McMahan, Washington Association of Sheriffs and Police Chiefs; Seth Dawson, Washington State Association for Substance Abuse Prevention; Zachary Lindahl, Washington Hospitality Association.

Persons Signed In To Testify But Not Testifying (Ways & Means): No one.