

HOUSE BILL REPORT

E2SSB 5549

As Reported by House Committee On:
Commerce & Gaming

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

Brief Description: Modernizing resident distillery marketing and sales restrictions.

Sponsors: Senate Committee on Ways & Means (originally sponsored by Senators Liias, King, Hunt and Braun).

Brief History:

Committee Activity:

Commerce & Gaming: 2/20/20 [DPA].

**Brief Summary of Engrossed Second Substitute Bill
(As Amended by Committee)**

- Modifies liquor sales privileges of distilleries and craft distilleries, creates an off-site tasting room license for distilleries and craft distilleries, establishes food service requirements, and limits when minors can be on the premises.
- Authorizes co-operated off-site tasting rooms and conjoined consumption areas for distilleries, craft distilleries, wineries, and breweries.
- Eliminates the license endorsement that authorizes sales of spirits for off-premises consumption by distilleries and craft distilleries at qualifying farmers' markets.
- Authorizes the provision of branded promotional items of nominal value to 501(c)(3) nonprofit entities, and creates a Public Records Act exemption for unaggregated financial, proprietary, or commercial information submitted to or obtained by the Liquor and Cannabis Board from distilleries.

HOUSE COMMITTEE ON COMMERCE & GAMING

Majority Report: Do pass as amended. Signed by 10 members: Representatives Peterson, Chair; Kloba, Vice Chair; MacEwen, Ranking Minority Member; Chambers, Assistant Ranking Minority Member; Blake, Jenkin, Kirby, Ramel, Vick and Young.

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.

Staff: Peter Clodfelter (786-7127).

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 distilleries who sell spirits to purchasers in Washington.

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 sell or provide customers with free 0.5 ounce or less samples of spirits, or 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 2 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. 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, the Internet (if Internet-sales privileges are requested), or by similar methods, and deliver spirits to an adult age 21 years or over subject to restrictions on hours of delivery, age-verification of the recipient, and packaging and labeling requirements. When selling spirits 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.

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 (annual fee of \$75 per farmers market). Before authorizing a farmers' market to allow an approved distillery or craft distillery to sell bottled spirits at retail, 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.

Tied-House Laws and Exceptions.

Business practices and financial interests of liquor licensees are restricted by the tied-house laws. These laws generally prohibit an industry member from advancing and a retailer from receiving moneys or moneys' worth under any type of agreement, practice, or arrangement.

The 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 to include a licensed manufacturer, producer, supplier, importer, wholesaler, distributor, authorized representative, certificate of approval holder, warehouse, and any affiliates, subsidiaries, officers, agents, employees, and representatives of any industry member.

An exception to the tied-house laws authorizes a distillery to hold a spirits, beer, and wine restaurant license for the purpose of selling liquor at a restaurant premises on the property on which the primary manufacturing facility of the distillery is located or on contiguous property owned or leased by the distillery. Another exception 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(s) entitling the nonprofit to the exemption.

Summary of Amended Bill:

License Privileges of Distilleries and Craft Distilleries.

The liquor sales privileges of distilleries and craft distilleries are modified. In addition to their own spirits, distilleries and craft distilleries may sell, for off-premises consumption, spirits produced by another distillery or craft distillery licensed in Washington, and vermouth or sparkling wine products produced by a licensee in Washington. For craft distilleries, when selling spirits produced by another distillery or craft distillery for off-premises consumption, their existing exemption from the 17 percent spirits retail license issuance fee does not apply, and the craft distillery must pay the 17 percent 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 unadulterated, samples must be 0.5 ounce or less of spirits, and a person is limited to receiving or purchasing, for on-premises consumption, no more than 2 ounces total of unadulterated spirits.

Regarding sales of spirits and alcohol products for on-premises consumption, 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, 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.

However, revenue derived from the sale of spirits for on-premises consumption may not comprise more than 30 percent of the overall gross revenue earned in the tasting room during

the calendar year. A distillery or craft distillery who sells adulterated products to consumers must file an annual report with the Liquor and Cannabis Board (LCB) that summarizes the distillery's revenue sources. Also, if a distillery or craft distillery provides or sells spirits or other alcohol products that are produced by another distillery, craft distillery, or licensee in Washington, 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 5 alcohol stock-keeping units of another distillery, craft distillery, or licensee in Washington.

No person under age 21 may be on the premises of a distillery or craft distillery tasting room, including an off-site tasting room, unless they are accompanied by their parent or legal guardian. Every tasting room, including off-site tasting rooms, must include a designated area where persons under age 21 are allowed to enter. The area may be a separate room or a designated area within the tasting room separated from the remainder of the tasting room space as authorized by the LCB.

Except for an event for which a private party has secured a banquet permit, after 9:00 p.m. no person under age 21 may be in an area of a distillery or craft tasting room where alcohol is sold, sampled, or served, including off-site tasting rooms. However, persons under 21 years of age who are children of owners, operators, or managers of a distillery or an off-site tasting room may be in any area of a distillery, tasting room, or an off-site tasting room, including past 9:00 p.m., provided they must be under the direct supervision of their parent or legal guardian while on the premises.

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.

The existing endorsement authorizing sales of spirits by a distillery or craft distillery at a qualifying farmers' market is eliminated. All references to this existing privilege are removed from law.

New License for Off-Site Tasting Rooms.

A tasting room license is established and available to distillery and craft distillery licensees. The new license authorizes the operation of an off-site tasting room at which the distillery may sample, serve, and sell spirits and alcohol products to adults age 21 and over subject to the same limits applicable to these activities when conducted on the distillery production facility's premises. A distillery or craft distillery licensed production facility is eligible for up to two tasting room licenses in Washington, and each tasting room requires its own license. Tasting rooms may be indoors, outdoors, or a combined indoor-outdoor area, and are administratively tied to a licensed production facility.

The fee for each off-site tasting room license is \$2,000 per year. No separate license is required for the single on-site tasting room licensees may operate at their production facility. The number of off-site tasting room licenses that may be issued to distilleries and craft distilleries may not exceed 150 total in Washington. However, this restriction does not apply

for purposes of issuing an off-site tasting room license for a location that is also licensed as a spirits, beer, and wine restaurant. Off-site tasting rooms may have a section identified and separated as federally bonded spaces for the storage of bulk or packaged spirits. Products of the licensee's production may be bottled or packaged in the space.

New Food Service Requirements.

New food service requirements apply to off-site tasting rooms of distilleries and craft distilleries, as well as to their on-site tasting rooms. A distillery or craft distillery operating a tasting room must provide, for free or for a charge, food offerings to customers during public service hours. Food offerings are defined to include a combination of small serving food items to include a mix of hors d'oeuvre-type foods, cheeses, fruits, vegetables, deli-style meats, chips, pretzels, nuts, popcorn, crackers, or similar items.

Additionally, distilleries and craft distilleries must post, in a conspicuous place within any tasting room, a list of at least five local restaurants or food trucks where customers can purchase food for consumption in the tasting room. The list must include names, addresses, contact information, and hours of operation for each restaurant or food truck named.

Requirements for food offerings must be further defined through rules. The rules must include the ability for food to be prepackaged for individual sale and consumption, allow food offerings to be prepared off-site for plating for the customer, not require any warming, cooking, or heating off-site or on-site prior to service, and not require the installation, maintenance, or use of any food-heating device or apparatus to prepare any food offerings.

Authorization for Co-Operated Tasting Rooms and Conjoined Consumption Areas with Wineries and Breweries.

Of the authorized off-site tasting rooms, any distillery, craft distillery, domestic winery, or any combination of these licensees may jointly occupy and co-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.

Additionally, 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 a co-operated off-site tasting room or conjoined consumption area of production facilities, licensees must comply with the applicable laws and rules relating to retailers. All licensees who operate joint off-site tasting rooms or conjoined consumption areas at production facilities must share staffing resources, and all participating licensees are jointly responsible for a violation of enforcement issue 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 applies only to those identified licensees. Further, every person who participates in any manner in the sale or service of samples or servings of spirits must obtain a class 12 alcohol server permit, and every person who participates in any manner in the sale or service of samples or servings of beer and wine must obtain a class 12 or class 13 alcohol server 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 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 to exempt from disclosure unaggregated financial, proprietary, or commercial information submitted to or obtained by the LCB in applications for distillery or craft distillery licenses or in any reports or remittances submitted by a licensed distillery or craft distillery pursuant to the LCB's rules.

Amended Bill Compared to Engrossed Second Substitute Bill:

The amended bill makes the following changes to the engrossed second substitute bill:

- provides that persons under age 21 must be accompanied by their parent or legal guardian to be on the premises of a distillery's on-site or off-site tasting rooms (and may not be accompanied only by another adult who has responsibility for them but who is not a parent or legal guardian). Prohibits persons under age 21 from being on the premises of a distillery or off-site tasting room past 9:00 p.m., except for an event covered by a private banquet permit or when the person is a child of an owner, operator, or manager;
- provides that children of owners, operators, or managers of a distillery or off-site tasting room may be in any area of the distillery or off-site tasting room (including past 9:00 p.m.) if the children are under the direct supervision of their parent or guardian;
- eliminates a reference to a 42-inch barrier as one of the authorized types of separations between a tasting room space and the designated area where persons under age 21 are allowed to enter a distillery tasting room;
- requires distilleries to provide, free or for a charge, food offerings to customers during public service hours at distillery tasting rooms. Defines "food offerings" to be a combination of small serving food items to include a mix of hors d'oeuvre type foods, cheeses, fruits, vegetables, deli-style meats, chips, pretzels, nuts, popcorn, crackers, or similar items. Also requires the posting of a list of at least five local restaurants or food trucks where customers can purchase food for consumption in the tasting room. Requires the Liquor and Cannabis Board (LCB) to further determine requirements for food offerings through rule, subject to limitations;
- limits the number of off-site tasting room licenses that may be issued to 150 total licenses. Provides that this limitation does not apply to an off-site tasting room that has also been granted a license as a spirits, beer, and wine restaurant;

- modifies terminology, makes various other changes, and grants the LCB-rulemaking authority to implement the act; and
- modifies the effective date, so the creation of the off-site tasting room license, the authorization for co-operated tasting rooms and conjoined consumption areas, and the authorization for the provision of branded promotional items to nonprofits take effect on January 1, 2021, whereas the following provisions have a 90-day effective date: (1) the new privileges and limitations for distilleries to sell spirits and other products from on-site tasting rooms; (2) the elimination of existing authority for distilleries to sell bottled spirits at farmers' markets under a license endorsement; (3) the new food service requirements for distillery tasting rooms; (4) the new Public Records Act exemption related to unaggregated financial, proprietary, or commercial information; and (5) the grant of rulemaking authority to the LCB to implement the act.

Appropriation: None.

Fiscal Note: Available.

Effective Date of Amended Bill: This bill takes effect 90 days after adjournment of the session in which the bill is passed, except for sections 3, 5, 6, 7, and 10, relating to creating the new off-site tasting room license, the authorization for co-operated tasting rooms and conjoined consumption areas, and the allowance for promotional items to nonprofit entities, which take effect January 1, 2021.

Staff Summary of Public Testimony:

(In support) This will give small craft distilleries a fighting chance to market their products. Proponents have worked with legislators and stakeholders for several years to develop and refine this bill, and passing the bill is critical. Last year there were 132 craft distilleries in Washington. As of December 2019 there are only 98 craft distilleries remaining. Two thirds of craft distilleries do not have a distributor. Two thirds of them do not have products in any retail location within Washington other than at their single on-site tasting room at the distillery facility. In this bill, the distillery industry is giving up their current authorization to sell bottled spirits at farmers' markets. The industry is also agreeing to a high fee of \$2,000 per off-site tasting room license. This will help offset the Liquor and Cannabis Board's one-time information technology costs. The bill requires 70 percent of revenue from the new off-site distillery tasting rooms to be from bottle sales for off-premises consumption and the sale of products other than spirits for on-premises consumption. This will ensure off-site distillery tasting rooms do not become bars. No bar could survive by making only 30 percent of its revenue from liquor sales for on-premises consumption. Also, there are limits on the amount of products produced by other producers that distilleries may sell. No more than 25 percent of the stock-keeping units of alcohol products offered for sale by a distillery may be produced by another licensee. The bill also restricts where minors can be in tasting rooms, and imposes a 9:00 p.m. curfew for minors at tasting rooms. These are restrictions not in current law to which the industry is agreeing. Two new types of food requirements are also added by the bill to distilleries. In addition to offering food items to customers at all distillery tasting rooms, the bill requires distilleries to post a conspicuous sign identifying at

least five local restaurants where customers can purchase and return with food. The fiscal note estimates about 35 off-site distillery tasting rooms will result from this bill. Even this relatively low number is likely inflated, and there will likely be an even smaller number of off-site tasting rooms. There are currently over 4,200 liquor-licensed locations in Washington where customers may purchase alcohol, so this bill is a very small expansion of access points to alcohol. The bill will protect public health, safety, and the three-tier system.

(Opposed) Stakeholders opposed to the bill appreciate the lengths proponents have gone to address concerns and to ensure any expansion to alcohol access is done as responsibly as possible. The elimination of the existing farmers' market spirits sales is appreciated, as well as the addition of the new food service requirements and the restrictions related to minors on the premises of distillery tasting rooms. However, stakeholders who oppose any expansion to alcohol access and who focus on communicating to the public the dangers of driving while intoxicated cannot support this bill.

(Other) Stakeholders with concerns about preventing substance abuse appreciate the work done on the bill and can get to neutral with two amendments. First, an amendment should require distillery tasting rooms to close by 9:00 p.m. instead of only prohibiting minors after 9:00 p.m. If the tasting rooms are not bars it should be okay to close by then. Second, an amendment should fix an inconsistency to eliminate the provisions that allows the 0.5 ounce samples of spirits to be adulterated with other alcohol. The 0.5 ounce limit per sample of spirits is appreciated, but it seems inconsistent to then allow that sample to be adulterated with other alcohol. It is appreciated that the bill removes the current authorization for sales of bottled spirits at farmers' markets. Moving these transactions to distillery tasting rooms, like this bill does, is a better approach because, at a tasting room, customers have chosen to go to an environment where alcohol sales are normal. Also, someone in recovery is less likely to be unexpectedly offered alcohol at a tasting room than at a farmers' market. In the future, the Legislature should continue to use the approach in this bill of retracting alcohol access in some way when a proposal seeks to expand alcohol access in another way.

Persons Testifying: (In support) Jim Hedrick, Washington Distillers' Guild.

(Opposed) James McMahan, Washington Association of Sheriffs and Police Chiefs.

(Other) Seth Dawson, Washington Association for Substance Abuse Prevention.

Persons Signed In To Testify But Not Testifying: None.