Alcoholic Beverage Control Laws

The Year That Was Foreshadows the Year That Will Be

Stephen G. Amato

The state of alcoholic beverage control in the 2015 Kentucky General Assembly was a tale of three bills: HB 168—a bill that closed a loophole in state law that allowed malt beverage producers to distribute their own products—became law, upholding the structure of the three-tier system in Kentucky; SB 81—which would have benefited many craft producers and made a host of changes to alcohol regulations across the board—failed to pass; and HB 423—which would have allowed small farm wineries to make use of or sell the unmarketable byproducts of winemaking—also failed.

Although the latter two bills failed to reach the governor's desk, they provided a crystal ball of sorts into the upcoming session of the General Assembly as the distillers, brewers and small farm wineries press legislators to expand opportunity for Kentucky's burgeoning alcohol production industry.

The Year That Was

HB 168 was passed by the General Assembly on March 4, 2015 and was then signed by the governor after a contentious debate that often spilled into the public eye. The law created a class of incompatible licenses, preventing brewers from also holding licenses as distributors. The objective of the law was to close a loophole that allowed brewers to own and operate in-state distributors, unlike distillers and wineries. Under a three-tier system, producers are prohibited from also owning a distributor, as this leads to vertical integration.

The case of *Kentucky Alcoholic Beverage Control Board v. Anheuser-Busch* solidified this loophole in 1978, allowing Anheuser-Busch to purchase a distributor in Louisville. The controversy came to a head after the brewer purchased another distributor in Owensboro. The new law now prohibits the collapse of the production and distribution tiers with regard to malt beverages.

Senate Bill 81 would have brought a multitude of changes to Kentucky's ABC laws, such as several "local option" provisions that would have allowed a local vote for package sales at distilleries and small farm wineries. Of particular note is the fact that SB 81 would have expanded sampling privileges at distilleries, allowing up to three ounces of samples per visitor, per day. These sampling privileges would have allowed visitors to try a wider variety in types and ages of distilled spirits than is available under current law, bringing them more in line with privileges at breweries and small farm wineries.

Small farm wineries under SB 81, meanwhile, would have been able to enter into "custom crush" agreements with other wineries. They would also have been able to sell unmarketable wine products such as pomace to distillers to make brandy, and HB 423 would have allowed those small farm wineries to create brandy from pomace themselves for the purposes of fortifying dessert wine or selling to distillers.

The Year That Will Be

Legislation has a metaphorical twin in the distillation process of Kentucky bourbon. Both start out in vast quantities that become distilled into a final product through a multistep process. That process for the upcoming 2016 General Assembly began in earnest for the alcohol industry already, as groups representing Kentucky's alcohol producers have already presented their legislative wish list for the coming year to Kentucky's legislators.

The Kentucky Guild of Brewers (KGB) advocated on behalf of two proposed measures to the Interim Joint Committee on Licensing and Occupations ("the Committee") to further the aims of the craft beer industry in Kentucky. The first proposal seeks to raise the cap on production from 25,000 barrels per year to 50,000. Under the current system, microbreweries—defined as those with a production limit of 25,000 barrels—can open taprooms and sell malt beverages as a retailer both by the drink and by the package. As those brewers approach production limits, however, they must choose between curtailing production growth and closing their taprooms altogether. The taprooms generate significant revenue for microbrewers, and for the KGB members approaching production limits in the coming years, the decision could be daunting.

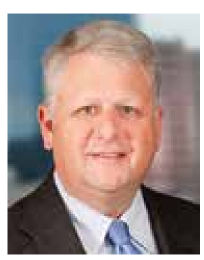
The second proposal KGB advanced, requests that microbreweries be put on similar footing to small farm wineries with respect to retail sales and sampling events off-premises. Under current law, microbreweries may provide samples and direct retail sales on premises only. KRS 243.155 allows small farm wineries to provide both samples and retail sales both by the package and by the drink at off-premises retail sites, fairs, festivals and other events as long as these locations are in wet territory. These same privileges for microbrewers would be a boon to an industry that already contributes $495 million to the Kentucky economy, according to the KGB.

The Kentucky Wineries Association (KWA) asked the Committee for the same legislative language in support of small farm wineries as found in SB 81 and HB 423. This legislation, again, would allow small farm wineries to enter into custom crush agreements with other wineries, sell or distill unmarketable byproducts and store wine in offsite bonded storage facilities. As with the KGB, the KWA asked that the cap of 50,000 gallons that separates small farm wineries from larger producers under the law be raised to 100,000, as at least five Kentucky wineries are coming close to those production limits.

The Kentucky Distillers' Association (KDA) presented five general legislative propositions to the Committee. As a way of bolstering and capitalizing on alcohol tourism in Kentucky's bourbon industry, the KDA suggested that distillers should be allowed to sell alcohol by the drink, expand bottle limits for visitors and provide larger sample sizes for visitors. The KDA also asked for local option precinct elections for distilleries, as well as permission to sell antique spirits at retail.

Several of these proposals represent a request for equalization among the various producers: the microbrewers want the same off-premises sales and sampling privileges as the small farm wineries, the small farm wineries want the ability to store product in off-site bonded storage similar to distillers, and the distillers would like the same general sampling and on-premises retail privileges as the microbrewers and small farm wineries. In sum, all Kentucky alcohol producers are asking the legislature for the opportunity to produce more alcohol and create more avenues in which to sell it.

What remains to be seen is whether this amassed combination of legislative requests will be answered with separate bills for each production segment or whether all these "asks" will be combined into an omnibus bill for passage as a package, much like SB 81 in 2015. With the Kentucky alcohol industry growing at a prodigious rate, it will be hard for the General Assembly to table requests by producers to capitalize on this growth, especially when there is a corresponding increase in wholesale, excise and sales tax revenue entering public coffers.



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