

Date of Hearing: March 22, 2023

ASSEMBLY COMMITTEE ON GOVERNMENTAL ORGANIZATION

Miguel Santiago, Chair

AB 1088 (Blanca Rubio) – As Amended March 9, 2023

SUBJECT: Licensed craft distillers: direct shipping

SUMMARY: This bill would extend a current exemption in the Alcoholic Beverage Control Act (Act) from January 1, 2024 to January 1, 2025. The exemption allows a licensed craft distiller to directly ship distilled spirits manufactured and produced by the licensee at its premises to a consumer, as specified. Specifically, **this bill:**

- 1) Reauthorizes, until January 1, 2025, a licensed craft distiller to directly ship distilled spirits manufactured and produced by the licensee at its premises to a consumer.
- 2) Provides that the amount shipped shall not exceed 2.25 liters per day and shall be solely for the consumer's personal use and not for resale.
- 3) Requires the licensee to maintain adequate records of the shipments and provide those records to the Department of Alcoholic Beverage Control (ABC) upon request.
- 4) Requires the licensee to require the common carrier to obtain the signature of any individual 21 years of age or older before delivering any distilled spirits shipped to an individual in this state.
- 5) Mandates that the containers in which the distilled spirits are shipped to be conspicuously labeled with the words: "CONTAINS ALCOHOL: SIGNATURE OF PERSON AGE 21 YEARS OR OLDER REQUIRED FOR DELIVERY."

EXISTING LAW:

- 1) Establishes the Department of Alcoholic Beverage Control (ABC) and grants it exclusive authority to administer the provisions of the Act in accordance with laws enacted by the Legislature. This involves licensing individuals and businesses associated with the manufacture, importation, and sale of alcoholic beverages and the collection of license fees for this purpose.
- 2) Provides, under the Act, for the issuance of various alcoholic beverage licenses, including the imposition of fees, conditions, and restrictions in connection with the issuance of those licenses.
- 3) Separates the alcoholic beverage industry into three separate component parts, or tiers, of the manufacturer (including, breweries, and distilleries), wholesaler/distributor, and retailer. This is referred to as the "Tied-house" law or "three-tier" system.
- 4) Provides that adults who bring alcoholic beverages into California for personal or household use do not need an alcoholic beverage license; however, some restrictions do apply, as defined. (California Business and Professions Code § 23661)

- 5) Creates the craft distillers license (Type 74), which among other things, authorizes the licensee to produce up to 150,000 gallons of distilled spirits per year and sell up to 2.25 gallons of distilled spirits directly to a consumer at the licensee's licensed premises. (California Business and Professions Code § 23502)
- 6) Creates the distilled spirits manufacturer's license (Type 04), which allows a licensee to manufacture, produce, package, mix, flavor, color, label, and export distilled spirits. (California Business and Professions Code § 25600.5)
- 7) Authorizes, until January 1, 2024, a licensed craft distiller to directly ship distilled spirits manufactured and produced by the licensee at its premises to a consumer, as defined. (California Business and Professions Code § 23504.5)
- 8) Authorizes a person licensed in California or any other state as a winegrower who obtains a wine direct shipper permit to sell and ship wine directly to a resident of California, who is 21 years of age or older, for the resident's personal use and not for resale, as specified. Current law does not limit the amount of wine that a holder of a wine direct shipper permit can ship to consumers. (California Business and Professions Code § 23661.3)
- 9) Provides that an individual or retail licensee in a state that affords California retail licensees or individuals an equal reciprocal shipping privilege, may ship, for personal use and not for resale, no more than two cases of wine (no more than nine liters each case) per month to any adult resident in this state. Delivery of a shipment shall not be deemed to constitute a sale in this state. (California Business and Professions Code § 23661.2)

FISCAL EFFECT: This bill is keyed fiscal by Legislative Counsel.

COMMENTS:

Purpose of the bill. According to the author's office, "Last year, with unanimous bipartisan support, the Legislature passed and the Governor signed AB 920 (Chapter 729). The bill allowed craft distillers to ship their products directly to in-state consumers for one year. The law is set to expire on January 1, 2024. On average, online sales and direct-to-consumer shipping now account for 30% of craft distillers' revenue. Most of California's family-owned craft distilleries are slowly recovering from the COVID-19 pandemic. AB 1088 simply extends the flexibility afforded to the aforementioned small distillers for an additional year, providing the proper opportunity for in-person tasting rooms to recover the revenue and food traffic lost during the pandemic. Additionally, it will allow for future conversations regarding the development of a permanent direct-to-consumer shipping solution that will appease the industry as a whole."

Background.

Tied-House Laws. State and federal laws generally prohibit certain relationships among those who produce, distribute, and sell alcoholic beverages. The term "tied-house" is derived from a common practice in England whereby a bar or public house was "tied"—by ownership, contractual obligations, or other influences—to a specific manufacturer. In some instances, that model encouraged intemperance in alcohol consumption. This was because retailers would offer manufacturers generous favors, such as expensive business meals and gifts. In order to recoup these costs, aggressive product promotion was needed. Manufacturers sometimes used their

influence to force tied houses to sell their products and exclude products from other manufacturers.

As a result, after the repeal of prohibition in 1933, California's current "three-tier" system was introduced. This body of law was initially created to: a) promote the state's interest in an orderly market; b) prohibit vertical integration and dominance by a single producer in the market place; c) stop commercial bribery and safeguard the public from predatory marketing techniques; d) discourage and/or prevent intemperate drinking.

DTC Shipping in California – Distilled Spirits. Today, the state boasts more than 160 craft distilleries (Type 74) licensed under the Act, giving California more distilleries than any other state. But prior to the establishment of the craft distillers license (Type 74) in 2015, no manufacturer of distilled spirits had the privilege of selling distilled spirits directly to a consumer. In 2015, AB 1295 (Levine), Chapter 640, Statutes of 2015, created the craft distillers license which, among other things, allowed a licensee to manufacture up to 100,000 gallons of distilled spirits per year and sell 2.25 liters directly to a consumer, if that consumer attended a tasting at the licensed premises. For reference, a typical bottle of distilled spirits is 0.75 liters. Therefore, a consumer can purchase three bottles of distilled spirits per day directly from a craft distiller at their licensed premises. If a craft distiller does not qualify to hold a craft distiller license, the licensee must obtain a distilled spirits manufacturer license, which does not have any off-sale privilege.

Subsequent legislation, AB 1164 (Skinner), Chapter 695, Statutes of 2018, increased the maximum production to 150,000 gallons and removed the requirement that a consumer needed to attend a tasting before being able to purchase distilled spirits directly from a licensee. Current law states that the sale of distilled spirits directly to a consumer must occur at the craft distiller's licensed premises. Thus, California law clearly states that it is prohibited for a licensed craft distiller to ship distilled spirits directly to consumers.

While a craft distiller did not have statutory authority to ship directly to consumers, at the beginning of the COVID-19 pandemic, ABC, as part of the Governor's First Notice of Regulatory Relief, temporarily allowed craft distillers to ship up to 2.25 liters per day to consumers. On June 3, 2020, the temporary privilege was extended as part of the Governor's Eighth Notice of Regulatory Relief to December 31, 2021. On December 30, 2021, as part of the Governor's Ninth Notice of Regulatory Relief, the temporary privilege was once again extended to March 31, 2022. There was no additional extension past the March 31, 2022 date. Therefore, licensed craft distillers no longer had the authority to ship directly to consumers.

In 2022, AB 920 (Aguiar-Curry, Statutes of 2022) was signed into law. Although similar to some of the prior regulatory relief that was temporarily available through March 2022 because of the COVID-19 pandemic, the bill contained key differences that will expire on January 1, 2024. The bill allowed a holder of a craft distillers license (Type 74) to directly ship distilled spirits manufactured or produced by the licensee at its premises to California consumers. The amount shipped must not exceed the equivalent of 2.25 liters in any combination of prepackaged containers per day per consumer. This quantity shall be solely for the consumer's personal use and not for resale. Additionally, the craft distiller must require the common carrier to get the signature of an individual 21 years of age or older.

AB 1088 would continue to allow, until January 1, 2025, a licensed craft distiller in California to directly ship distilled spirits manufactured and produced by the licensee at its premises to a consumer. There is no similar privilege in the bill for manufacturers of spirits distilled outside the state.

Granholm v Heald, 544 U.S. 460 (2005). In the 2005 *Granholm v Heald* case, the Supreme Court of the United States ruled that laws in New York and Michigan that permitted in-state wineries to ship wine directly to consumers but prohibited out-of-state wineries from doing so were unconstitutional. The court case, which was a consolidation of two separate lawsuits against Michigan and New York, pitted the Dormant Commerce Clause against the 21st Amendment.

Michigan and New York alcohol laws allowed in-state wineries to directly ship alcohol to consumers but prohibited such activity from out-of-state wineries. Plaintiffs argued that these laws violated the United States (U.S.) Constitution's Dormant Commerce Clause, which over the years has been interpreted to mean that states are prohibited from passing laws favoring in-state businesses over out-of-state businesses. On the other hand, the defendants argued that their laws were a valid exercise of state power under the 21st Amendment, which ended federal prohibition and allowed states to regulate alcohol importation. One of the state's justifications was that by regulating out-of-state wineries, the state might be able to hinder the shipment of alcohol to underage minors, which they believe served a valid state purpose.

After making its way through the courts, the two separate cases were ultimately decided by the U.S. Supreme Court. In a 5-4 opinion delivered by Justice Anthony Kennedy, the Court opined that both states' laws violated the commerce clause by favoring in-state wineries at the expense of out-of-state wineries. In essence, the case held that states have the burden to show that restrictions on out-of-state businesses that do not also apply to in-state businesses, need to be supported by a justifiable need to advance public health and safety, or for some other legitimate, non-discriminatory, reason. Prior to this decision, it was widely assumed that in-state manufacturers could be given more privileges compared to out-of-state manufacturers. Following the *Granholm v Heald* case, out-of-state manufacturers must generally be given the same privileges as in-state manufacturers.

AB 1088, in providing an in-state manufacturer with a privilege not given to an out-of-state manufacturer, could result in possible lawsuits under the *Granholm* decision, even if this privilege is temporary.

In support. The California Artisanal Distillers Guild writes, “AB 1088 is critical because shipping direct to consumers will allow California craft distillers to keep their businesses open, retain employees, and continue to provide tax revenue to the state. If this bill doesn’t pass, craft distillers will continue to lose employees and some will go out of business due to lost revenue combined with reduced tourism numbers and the tough economy. Many other states allow for direct to consumer shipping for alcohol products, and California already allows this for beer, wine and brandy makers. This bill will allow Type 74 craft distilled spirits licensees in California to continue to use third party common carriers to ship directly to customers within the state as they have been since March 2020. These common carriers have policies and procedures to ensure the safe and legal delivery of spirits (ID verification and in-person delivery only) to persons over age 21.”

In opposition. Alcohol Justice writes in opposition, “The three-tier system was intended to inhibit monopoly among the alcohol industry, as well as empower intentionality in alcohol purchasing and consumption. Direct-to-Consumer (DtC) makes it nearly impossible to consistently engage in responsible beverage service (RBS) practices. Delivery carriers have no RBS mandate, no ability to consistently identify and refuse service under dangerous circumstances, and both technical and economic pressures that reduce the ability to properly prevent delivery to underage recipients. Similarly, DtC sales create and nearly insurmountable enforcement challenge. The vagaries of delivery make it extremely difficult for an already overstressed ABC to conduct monitoring or stings.

Related legislation. SB 269 (Laird) of 2023. This bill would authorize the owner of a craft distilled spirits manufacturer’s license that also holds a beer manufacturer’s license, or a winegrower’s license, to have alcoholic beverages that are authorized under those licenses at the same time anywhere within the premises, and to maintain a designated area where retail sales and consumption authorized under those licenses can occur, subject to specified conditions (Senate Appropriations Committee)

Prior legislation. AB 920 (Aguiar-Curry), Chapter 729, Statutes of 2022. The bill, until January 1, 2024, allows a licensed craft distiller to directly ship distilled spirits manufactured or produced by the licensee at its premises to a consumer pursuant to specified requirements.

SB 620 (Allen) of 2022. Would have authorized craft distillers, who obtain a distilled spirits direct shipper permit, to sell and ship specified amounts of distilled spirits directly to a resident of California, who is 21 years of age or older, for the residents personal use and not for resale, as specified. (Not heard in the Assembly Governmental Organization Committee)

SB 1198 (McGuire) of 2022. Would have created a beer direct shipper permit which would authorize beer manufacturers to sell and ship beer directly to a resident of California, who is 21 years of age or older, for the residents personal use and not for resale. (Not heard in the Assembly Governmental Organization Committee)

SB 517 (McGuire) of 2021. Would have created a beer direct shipper permit which would authorize beer manufacturers, regardless of specific type of license, who obtain a beer direct shipper permit, to sell and ship beer directly to a resident of California, who is 21 years of age or older, for the residents personal use and not for resale. (Not heard in the Senate Governmental Organization Committee)

SB 1164 (Skinner), Chapter 695, Statutes of 2018. Made various changes to the craft distillers license, including eliminating the requirement that a person must attend a tasting before being able to purchase prepackaged containers of the licensee’s spirits directly from the craft distiller and increasing the maximum amount of distilled spirits that a craft distiller is permitted to manufacture from 100,000 gallons to 150,000 gallons.

AB 1295 (Levine), Chapter 640, Statutes of 2015. Created a new "craft distillers license" in the Act with specified privileges and limited to persons who manufacture less than 100,000 gallons of distilled spirits annually, exclusive of brandy production. The bill also modified an existing provision of law that allowed distillers to offer six, one-quarter ounce tastings, per individual/per day, to instead permit distillers to combine the current limitation into one single 1.5 ounce tasting that may also include a non-alcoholic mixer.

AB 933 (Skinner), Chapter 366, Statutes of 2013. Granted licensed distilled spirits manufacturers and licensed brandy manufacturers the privilege to conduct consumer tastings on their licensed premises and to charge for those tastings.

REGISTERED SUPPORT / OPPOSITION:**Support**

10th Street Distillery - San Jose
117° West Spirits
Adams Grain Company
Alchemy Distillery - Arcata
Amador Distillery
Autry Cellars - San Luis Obispo
Bethel Road Distillery - Castoro Cellars
Blinking Owl Distillery
California Artisanal Distillers Guild
Calwise Spirits Co - Paso Robles
Central Coast Distillery
Charbay Distillery - Mendocino
Clos Solene
Cutlers Artisan Spirits - Santa Barbara
Devils Creek Distillery
Distillers of Slo County
Donati Wine and Spirits
Dry Diggings Distillery
Dunning Vineyards
Essential Spirits Alambic Distillers
Golden Beaver Distillery, INC
Greenbar Distillery
Hearst Ranch Winery
Hinterhaus Distilling - Arnold CA
Home Base Spirits
Humboldt Distillery
Jetty Wave Distillery - Half Moon Bay
Krobar Craft Distillery
Los Angeles Distillery
Lxv Wine
Midtown Spirits
Napa Valley Distillery
Paris Valley Road Estate Winery
Peachy Canyon Winery
Pekut and Carwick Independent Bottlers
Pendray's Distillery
R6 Distillery - El Sugundo
RE:FIND Distillery
Ringgold Distilling
Shelter Distilling
St. George Distillery

Stark Spirits - Pasadena
Summerwood Winery
Surf City Still Works
Treecraft Distillery
Turley Wine Cellars
UPS
Ventura Spirits Distillery
Willie's Tin Shop
Willow Creek Distillery
Young and Yonder Spirits Healdsburg

Oppose

Alcohol Justice

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