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# SENATE COMMITTEE ON GOVERNMENTAL ORGANIZATION

Senator Bill Dodd

Chair

2023 - 2024 Regular

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<b>Bill No:</b>	AB 1088	<b>Hearing Date:</b>	6/27/2023
<b>Author:</b>	Blanca Rubio		
<b>Version:</b>	3/9/2023 Amended		
<b>Urgency:</b>	No	<b>Fiscal:</b>	Yes
<b>Consultant:</b>	Felipe Lopez		

**SUBJECT:** Licensed craft distillers: direct shipping

**DIGEST:** This bill extends a current exemption that allows a licensed craft distiller to directly ship distilled spirits manufactured by the licensee to a consumer from January 1, 2024, to January 1, 2025.

## **ANALYSIS:**

Existing law:

- 1) Establishes the Department of Alcoholic Beverage Control (ABC) and grants it exclusive authority to administer the provisions of the ABC 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 ABC 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) 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.

- 5) Authorizes an individual or retail licensee in a state that affords California retail licensees or individuals an equal reciprocal shipping privilege, to ship, for personal use, no more than two cases (no more than nine liters each case) per month to any adult resident in this state. Winegrowers are not considered a “retail licensee” therefore, the two cases per month to any adult resident does not apply to a holder of a wine direct shipper permit.
- 6) Creates the craft distillers license, 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.
- 7) Creates the distilled spirits manufacturer’s license, which allows a licensee to manufacture, produce, package, mix, flavor, color, label, and export distilled spirits.
- 8) Authorizes, until January 1, 2024, a licensed craft distiller to directly ship distilled spirits manufactured or produced by the licensee at its premises to a consumer only if they comply with the following requirements:
  - a) The amount shipped does not exceed the equivalent of 2.25 liters and is solely for the consumer’s personal use.
  - b) The licensee maintains adequate records of the shipments and provides those records to the Department of ABC upon request.
  - c) The licensee requires 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.
  - d) The container in which the distilled spirits are shipped be conspicuously labeled with the words: “CONTAINS ALCOHOL: SIGNATURE OF PERSONS AGE 21 YEARS OR OLDER REQUIRED FOR DELIVERY.”

This bill extends the above-described exemption that allows a licensed craft distiller to directly ship distilled spirits manufactured by the licensee to a consumer from January 1, 2024, to January 1, 2025.

## **Background**

*Author Statement.* According to the author’s office, “there are over 200 craft distillers in California, the vast majority being family owned small businesses that significantly impact local economies. Direct to consumer shipping provided a lifeline for these distillers since the onset of the pandemic, which now account for significant portions of their revenue. AB 1088 simply extends flexibilities

afforded to the aforementioned small distillers for one additional year, providing the proper opportunity for in person tasting rooms to recover the revenue and food traffic lost during the pandemic while also allowing conversations regarding a permanent direct to consumer shipping solution be developed which appeases the industry as a whole.”

*Tied-House Laws.* The "tied-house" or "three-tier" system, separates the alcoholic beverage industry into three component parts of the manufacturer (the first tier), wholesaler (the second tier), and retailer (the third tier). In its simplest of forms, this set of laws is designed to separate manufacturers, distributors, and retailers of alcoholic beverages.

The original policy rationale for this body of law was to: (1) promote the state's interest in an orderly market; (2) prohibit the vertical integration and dominance by a single producer in the marketplace; (3) prohibit commercial bribery and protect the public from predatory marketing practices; and, (4) discourage and/or prevent the intemperate use of alcoholic beverages.

Thus, under a strict “three-tier” system, manufacturers would have no privilege to sell alcoholic beverages directly to consumers. Over the years however, the Legislature has expanded the privileges of manufacturers to include, among other things, the ability to sell alcoholic beverages directly to consumers. Some, like winegrowers enjoy not only the ability to sell alcoholic beverages directly to consumers at their licensed premises, but also the ability to ship directly to consumers. Though a one-year exemption currently exists to this prohibition, craft distillers are currently only statutorily allowed to sell directly to consumers at their licensed premises.

*Current Exemption.* After a comprehensive solution failed to materialize, last year the legislature passed and the Governor signed AB 920, which temporarily allows craft distillers in California to ship distilled spirits directly to consumers away from their licensed premises. Under the bill, the shipment could not exceed 2.25 liters and only for the consumer’s personal use. The licensee is required to maintain adequate records and provide those records to the Department of ABC upon request by the department. The licensee must require the common carrier to obtain the signature of an individual who is 21 years of age or older and the package must be properly labeled as containing alcohol. This authorization is set to expire on January 1, 2024. This bill would extend the provisions of AB 920 by one year to January 1, 2025.

*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 21<sup>st</sup> 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 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 21<sup>st</sup> 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 state's 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.

This bill, by continuing to allow an in-state manufacturer a privilege not given to an out-of-state manufacture could result in possible lawsuits under the *Granholm* decision, even if this privilege is temporary.

*Direct to Consumer Shipping in California – Distilled Spirits.* Prior to the creation of the craft distillers license in 2015, no distilled spirits manufacturer 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 manufacturer 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, normally a bottle of distilled spirits is 0.75 liters, meaning a consumer can purchase three bottles of distilled spirits per day directly from a craft distiller at their licensed premises.

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. Other than the exemption under AB 920, current law is clear that the sale of distilled spirits directly to a consumer must occur at the craft distiller's licensed premises.

While a craft distiller does not have statutory authority to ship directly to consumers, at the beginning of the COVID-19 Pandemic, the Department of 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. As such, the Legislature passed AB 920 as an urgency bill to allow for a one year extension of the regulatory relief.

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. As with beer, there is no statutory authority for out-of-state distilled spirits manufacturers to sell, ship, or deliver distilled spirits directly to consumers in California.

*DTC Shipping in California - Wine.* As exceptions to the "three-tier" system have been enacted and laws have evolved to allow for additional direct to consumer privileges, differences between wine, beer, and distilled spirits have been created. For California wineries, the ability to sell and ship wine bottles directly to consumers has been a privilege that has been enjoyed for a number of years.

Even prior to the Granholm decision in 2005, California law made it clear that California wineries had the authority to sell fully sealed bottles to consumer at their licensed premises. While the law did not specifically authorize California wineries to ship directly to consumers, the privilege to sell directly to consumers was understood to also allow California wineries to deliver wine produced by that winery to consumers in California away from their licensed premises.

In 2005, following the Granholm decision, the Legislature passed, and the Governor signed SB 118 (Chesbro, Chapter, Statutes of 2005) which created the wine direct shipper permit, allowing a licensed winegrower to sell and ship wine directly to consumers. The wine direct shipper permit allows both in-state and out-of-state winegrowers to obtain the newly created permit. This was done to ensure compliance with the Granholm decision.

Under SB 118, the package must be clearly labeled as containing alcohol and the delivery company must obtain a physical signature of a person over the age 21 who accepts the package. In addition, out-of-state wineries must pay all applicable California taxes, including excise taxes. Wineries are required to contact the California Department of Tax and Fee Administration (CDTFA) for tax payment instructions.

According to testimony provided to the Senate Governmental Organization during the committee's November 30, 2021 informational hearing on this topic, the Wine Institute testified that wine delivered to consumers represents approximately two-percent of wine sold to consumers.

This bill does not alter in any way any of the provisions related to the current authority of wineries to ship directly to consumers.

**Prior/Related Legislation**

SB 1198 (McGuire, 2022) would have created the 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 resident's personal use and not for resale. (Never Heard in the Assembly Governmental Organization Committee)

AB 920 (Aguiar-Curry, Chapter 729, Statutes of 2022) 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 specified.

SB 517 (McGuire, 2021) would have created the 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 resident's personal use and not for resale. (Never Heard in the Senate Governmental Organization Committee)

SB 620 (Allen, 2021) 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 resident's personal use and not for resale, as specified. (Never Heard in the Assembly Governmental Organization Committee)

SB 1198 (McGuire, 2022) would have created the 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 resident's personal use and not for resale. (Never Heard in the Assembly Governmental Organization Committee)

SB 1164 (Skinner, Chapter 695, Statutes of 2018) made various changes to the craft distiller's 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 the craft distiller's license which, among other things, allow a licensee to manufacture up to 100,000 gallons of distilled spirits annually. Additionally, the licensee is authorized to sell to a consumer participating in a distilled spirits tasting, on the distiller's licensed premises, up to 2.25 liters of distilled spirits in any combination of prepackaged containers per day.

**FISCAL EFFECT:** Appropriation: No Fiscal Com.: Yes Local: No

**SUPPORT:**

California Artisanal Distillers Guild  
Adams Grain co.  
Alchemy Distillery  
Amador Distillery  
Autry Cellars  
Blinking Owl Distillery  
Calwise Spirits Co.  
Castoro Cellars  
Central Coast Distillery  
Charbay Distillery  
Cutler's Artisan Spirits  
Devils Creek Distillery  
Distillers of Slo County  
Donati Wine and Spirits  
Dry Diggings Distillery  
Dunning Vineyards  
Essential Spirits Alambic Distilleries  
Golden Beaver Distillery, Inc.  
Greenbar Distillery  
Hearst Ranch Winery  
Hinterhaus Distilling  
Home Base Spirits  
Humboldt Distillery  
Jetty Wave Distillery

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  
Re:Find Distillery  
Ringgold Distilling  
R6 Distillery  
Shelter Distilling, Inc.  
Spirit Works Distillery  
St. George Distillery  
Summerwood Winery  
Surf City Still Works  
Treecraft Distillery  
UPS  
Ventura Spirits Distillery  
Young & Yonder Spirits  
Willie's Tin Shop  
Willow Creek Distillery  
10<sup>th</sup> Street Distillery  
117°West Spirits

**OPPOSITION:**

Alcohol Justice  
California Alcohol Policy Alliance

**ARGUMENTS IN SUPPORT:** Supporters of the bill argue that, “AB 1088 is necessary because the law allowing California craft distillers to sell their products online and ship to consumers ends on January 1, 2024. On average, online sales and direct to consumer shipping now represents 30% of craft distiller revenue. Most of California’s family owned craft distilleries are slowly recovering from COVID. Tourism and in-person purchases at their tasting rooms are still down because of COVID, reduced tourism, the economy and inflation. AB 1088 is critical because online sales and shipping to consumers will allow California Craft Distillers to make sales beyond their tasting rooms to make up for the lost revenue from lack of in-person sales.



**ARGUMENTS IN OPPOSITION:** According to Alcohol Justice, “[this] bill further threatens to circumvent distributorships by allowing in-person delivery of 2.25 liters per customer per day. This is an absurd quantity of alcohol for an individual to consume, a level that would see them dead. That level only makes sense if it is not for personal use, belying the idea that this is not intended to be a replacement for alcohol picked up during normal grocery runs. Even disregarding the slow suicide this level of consumption implies, there are strong associations between heavy home alcohol use and a wide range of domestic harms, including accidental injury, child neglect and child abuse, and intimate partner violence.”