

Date of Hearing: June 30, 2016

ASSEMBLY COMMITTEE ON GOVERNMENTAL ORGANIZATION

Adam Gray, Chair

SB 1426 (Hall) – As Amended May 31, 2016

SENATE VOTE: 32-4

SUBJECT: Alcoholic beverage control: tied-house restrictions: compensation

SUMMARY: Establishes a new tied-house exception in the Alcoholic Beverage Control Act (Act) that authorizes, until January 1, 2022, a person who does not hold an ownership interest in more than five California on-sale retail licenses, to be compensated by an alcoholic beverage supplier for promotional or marketing services subject to specified conditions. Specifically, **this bill:**

- 1) Defines “authorized licensee” for purposes of this bill to mean a manufacturer, winegrower, manufacturer’s agent, rectifier, California winegrower's agent, beer manufacturer, holder of an out-of-state beer manufacturer's certificate, distilled spirits manufacturer, holder of a distilled spirits rectifier’s general license, distilled spirits manufacturer's agent, brandy manufacturer, brandy importer, holder of an out-of-state distilled spirits shipper’s certificate, holder of a distilled spirits importer’s general license, distilled spirits importer, or craft distiller.
- 2) Provides that an authorized licensee may compensate a person who does not hold an ownership interest in more than five California on-sale retail licenses for promotional or marketing services of the authorized licensee’s products, subject to the following conditions:
 - a) Any compensation agreement with the person must be in the form of a written contract and include the conditions outlined in this bill.
 - b) The authorized licensee may have written contracts regarding compensation authorized by this bill with no more than five persons at any given time.
 - c) The person shall not be exclusively responsible for the on-sale retail licensee’s purchasing decisions of the brands of alcoholic beverages owned by the authorized licensee compensating the person.
 - d) The authorized licensee compensating the person shall not utilize the person to engage in any endorsement or promotional or marketing activity for alcoholic beverages on the premises of the on-sale retail licensee in which the person has an ownership interest.
 - e) All compensation the authorized licensee pays to the person must be based solely on the person’s promotional and marketing activities and shall not be related directly or indirectly to the sale of alcoholic beverages by the on-sale retail licensee in which the person has an ownership interest.
 - f) The person shall not personally serve any alcoholic beverages while on the premises of an on-sale retail licensee. (This prohibition does not apply to an event held at an

unlicensed venue under a caterer's permit.)

- g) The on-sale retail licensee in which the person holds an ownership interest in must offer for sale, and serve, alcoholic beverages that compete with the brands of the authorized licensee compensating the person for promotional or marketing services.
 - h) Prohibits the name, image, and brand of the on-sale retail licensee in which the person has an ownership interest from being featured or referenced in any advertising of the brands sold by the authorized licensee compensating the person except the name and address of the on-sale retail licensee in which the person has an ownership interest may be advertised when promoting specific events at which the compensated person does not provide services.
 - i) Prohibits the person from being involved in the decisions by the authorized licensee regarding the selection of on-sale retail licensees that will offer for sale the brands the person is compensated to promote and market.
- 3) States that a licensee that is not an authorized licensee shall not compensate a person under this bill and shall not directly or indirectly underwrite, share in, or contribute to the costs of compensation authorized by this bill.
 - 4) Provides that any officer, director, or agent of an authorized licensee that is compensated by that authorized licensee for promotional or marketing services of the authorized licensee's products shall not be subject to the conditions outlined in item #2 above (a-i).
 - 5) States that an on-sale retail licensee in which the compensated person holds an ownership interest that solicits, or receives any compensation from an authorized licensee for any unlawful activity relating to promotion or marketing services shall be guilty of a misdemeanor punishable by up to six months imprisonment, by a fine of \$10,000, or by both.
 - 6) Provides that an authorized licensee who, through coercion or other illegal means, induces, directly or indirectly, a holder of a wholesaler's license to provide compensation to a person pursuant to this bill shall be guilty of a misdemeanor punishable by up to six months imprisonment, by a fine of \$10,000, or by both.
 - 7) Provides that an authorized licensee or person who violates any provision of this bill shall be guilty of a misdemeanor punishable by up to six months imprisonment, by a fine of \$10,000, or by both. Also, establishes a similar misdemeanor and fine for an on-sale retail licensee who, through coercion or other illegal means, induces or conditions, directly or indirectly, the purchase or sale of alcoholic beverages upon an authorized licensee's selection or decision about the promotional or marketing services of a person compensated by the authorized licensee.
 - 8) Contains legislative findings and declarations that it is necessary and proper to require a separation between manufacturing interests, wholesale interests, and retail interests in the production and distribution of alcoholic beverages in order to prevent suppliers from dominating local markets through vertical integration and to prevent excessive sales of alcoholic beverages produced by overly aggressive marketing techniques. Any exception

established by the Legislature to the general prohibition against tied interests must be limited to the express terms of the exception so as to not undermine the general prohibitions.

9) Contains a January 1, 2022 sunset provision.

EXISTING LAW:

1) Establishes 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 in this state and the collection of license fees.

2) Existing law, known as the "Tied-house" law, separates the alcoholic beverage industry into three component parts of manufacturer, wholesaler, and retailer. The original policy rationale for this body of law was to prohibit the vertical integration of the alcohol industry and to protect the public from predatory marketing practices. Generally, other than exemptions granted by the Legislature, the holder of one type of license is not permitted to do business as another type of licensee within the "Three-tier" system.

3) Restricts certain alcoholic beverage licensees from paying, crediting, or compensating a retailer for advertising in connection with the advertising and sale of alcoholic beverages and expressly authorizes exceptions to this prohibition.

4) Prohibits specified licensees from furnishing, giving, or lending money or other things of value, directly or indirectly, to a person engaged in operating, owning, or maintaining an off-sale licensed premises.

5) Prohibits the ABC from imposing a dollar limit of less than \$5 for consumer advertising specialties furnished by a distilled spirits supplier to a retailer or the general public. Allows beer manufacturers to give adult consumers promotional advertising items valued up to \$5. Existing law provides that consumer-advertising specialties furnished by a wine supplier to a retailer or to the general public shall not exceed \$1 per unit original cost to the supplier who purchased it.

6) Authorizes the holder of a winegrower's license, a beer manufacturer, a distilled spirits rectifier, a distilled spirits manufacturer, and a distilled spirits manufacturer's agent, to purchase advertising space and time from, or on behalf of, an on-sale retail licensee, under certain conditions, if the on-sale retail licensee is the owner, manager, agent of the owner, assignee of the owner's advertising rights, or major tenant of specified facilities.

7) Permits, until January 1, 2016, the appearance of a person employed or engaged by an "authorized licensee," as defined, at a promotional event held at the premises of an off-sale retail licensee for the purpose of providing autographs under specified conditions.

8) Defines an "on-sale" license as authorizing the sale of all types of alcoholic beverages: namely, beer, wine and distilled spirits, *for consumption on the premises* (such as at a restaurant or bar). An "off-sale" license authorizes the sale of all types of alcoholic beverages for consumption *off the premises* in original, sealed containers.

FISCAL EFFECT: Unknown

COMMENTS:

Background: The enactment of the 21st Amendment to the U.S. Constitution in 1933 repealed the 18th Amendment and ended the era of Prohibition. Accordingly, states were granted the authority to establish alcoholic beverage laws and administrative structures to regulate the sale and distribution of alcoholic beverages.

California's tied-house laws restrict wineries, breweries and distilled spirits manufacturers from compensating any retailer for advertising the sale of their alcoholic beverages. Over time, the Legislature has enacted numerous exceptions to the state's tied-house laws. For instance:

- Business and Professions (B&P) Code Section 25503.11 permits a manufacturer to own stock in a publicly traded retail licensee or serve on the board of a publicly traded retail off-sale licensee.
- B&P Code Section 25502.2 permits a person employed or engaged by a manufacturer to appear at a promotional event at the premises of an off-sale retail licensee for the purposes of providing autographs to consumers.
- B&P Code Section 25503.8 permits an alcoholic beverage manufacturer to purchase advertising space at large stadiums and arenas that sell their products.
- B&P Code Sections 25503.15(b) and 25503.30 allow winegrowers to own an interest in on-sale licenses, with limitations.

Purpose of the bill: The author's office notes that under this bill, and for a period of five years only, a supplier would be able to retain the services of a spokesperson that has an ownership interest in no more than five on-sale retail licenses. Additionally, the author's office states that this bill contains certain protections to assure that the promotional activity does not happen on the retail premise or influence the retail decisions.

Pending litigation: On January 7, 2016, the U. S. Court of Appeals for the Ninth Circuit issued a decision that may open the door to relaxing the laws restricting supplier-paid advertising in retail establishments. In the case, *Retail Digital Network LLC v. Jacob Appelsmith, as the Director of ABC*, the Court overturned a 29-year-old precedent, which held that those portions of the ABC Act prohibiting alcoholic beverage suppliers and wholesalers from paying for the privilege of advertising at a retail establishment did not violate the First Amendment. The Court applied recent U.S. Supreme Court jurisprudence to require a *heightened scrutiny* standard on state-imposed limitations of non-deceptive commercial speech whereby alcohol beverage suppliers and wholesalers are prohibited from, directly or indirectly, giving anything of value to retailers for advertising their products. In doing so, the Court remanded the case to the lower court that had upheld the earlier precedence for it to reconsider using a *heightened scrutiny* standard rather than the *intermittent scrutiny* standard that it had used in its ruling.

In support: Writing in support, Diageo states, "For decades, spokespersons have been used to promote alcohol brands. For example, Frank Sinatra did commercials for Budweiser in the 1960's; Dave Matthews partners with Constellation on Dreaming Tree Wine; Mila Kunis and Neil Patrick Harris currently promote Jim Beam and Heineken, respectively; and Diageo's brands are promoted by Jimmy Kimmel. When an individual becomes an influencer, companies

often engage that person to market their products. This is common practice not only in alcohol but also with sporting goods, snack foods and pharmaceuticals. In recent years, there has been an explosion of celebrities entering the restaurant business. Unfortunately, an individual who happens to have an interest in a restaurant or nightclub is prohibited from using their established celebrity status to serve in a promotional capacity for an alcoholic beverage manufacturer. In short, the individual has become a licensee and California law prohibits, except where the Legislature makes an exemption, a manufacturer from employing or making payments to a licensee.”

The Distilled Spirits Council supports this common sense bill "because it has appropriate safeguards, while allowing manufacturers to benefit from the promotional services of spokespersons, like celebrities, that can influence consumers' buying decisions."

Family Winemakers of California states, “For years, spokespersons have been utilized in the promotion of various alcohol brands. However, due to California’s tied-house restrictions, a person with an interest in a restaurant or similar venue is excluded from employing their celebrity status to operate in a promotional manner for a manufacturer of alcoholic beverages. This bill will inaugurate a new tied-house exemption that will authorize a manufacturer to maintain and utilize the work of a spokesperson that has ownership interest in a retail license.”

The Wine Institute states, “This bill contains many safeguards that will enable wineries to benefit from promotional services offered by various celebrity spokespersons to connect with consumers and expand their business.”

In opposition: Writing in opposition, the California Beer and Beverage Distributors (CBBD) state that, “SB 1426 would legalize the practice, now banned in California and across the nation, of alcohol beverage manufacturers being permitted to pay retailers for promotion and marketing of manufacturers’ products. Legalizing manufacturer payments to retailers is contrary to the State’s public policy interest in assuring a level playing field and equal access to the marketplace for all breweries, wineries and distillers operating in California – the biggest alcohol market in the country and home to the most breweries and wineries in the United States. It could also affect pending litigation and prejudicially affect the State of California’s position in that case.” [Retail Digital Network, LLC v. Jacob Appelsmith, as the Director of the ABC (2016).]

CBBD notes that, “bills such as SB 1426, have the potential for allowing dominant corporations in California to exert greater influence over the retail sector through payments for promotions and marketing to selected retailers. Originally touted as a bill to permit payments to celebrity spokespeople the bill has become a vehicle to allow any person who is at least 21 years old and has an ownership interest in more than five California on-sale retail licenses to be compensated for undefined ‘promotional and marketing activities’ on behalf of an alcohol beverage manufacturer’s brands.”

CBBD argues that the conditions set forth in SB 1426, “ostensibly to preserve retailer independence from a manufacturer’s control, are illusory protections and that the so-called firewalls do not prevent pay to play by manufacturers.” In addition, CBBD states that SB 1426 “would be the first instance in which a tied-house exception is created for the benefit of an individual as opposed to current exceptions allowing paid advertising to a retail licensee in public venues such as a stadium, sports arena, theme park, racetracks, and exposition parks. For the current exceptions, there were public policy considerations involved, such as promoting a

desirable economic activity in the venue and providing a funding source for public entities when they owned or operated the venue. With respect to SB 1426, no similar policy considerations are apparent to support this new broadly written exception.”

Also writing in opposition, the California Teamsters state, “this bill would allow those with significant market power to dominate the industry and we are concerned that such domination of the marketplace would jeopardize the jobs of our members who work in all aspects of the alcoholic beverage industry.”

Related legislation: AB 866 (Garcia) of 2016. Extends an existing “tied-house” exception in the ABC Act pertaining to the general prohibition against advertising arrangements between retail, wholesale and manufacturer licensees to include an outdoor stadium with a fixed seating capacity of at least 46,000 seats located in the City of San Diego (Petco Park – home of the San Diego Padres). (Pending in the Senate Appropriations Committee)

AB 1767 (Bigelow, 2016). Expands the specified conditions under which designated alcoholic beverage licensees may purchase advertising space or time in connection with events held on the premises of an exposition, park, stadium or arena owned by the on-sale licensee to include circumstances in which the premises are “leased” by the on-sale licensee. (Pending in Senate Governmental Organization Committee)

Prior legislation: SB 557 (Hall), Chapter 420, Statutes of 2015. Extended an existing tied-house exception pertaining to the general prohibition against advertising arrangements between retail, wholesale and manufacturer licensees to include a fairgrounds with a horse racetrack and equestrian and sports facilities located in the County of San Diego.

SB 462 (Wolk), Chapter 315, Statutes of 2015. Among other things, extended an existing tied-house exception pertaining to the general prohibition against advertising arrangements between retail, wholesale and manufacturer licensees to include a specified entertainment complex, known as the Green Music Center, located on the campus of Sonoma State University.

AB 600 (Bonta, Chapter 139, Statutes of 2014). Extended an existing tied-house exception pertaining to the general prohibition against advertising arrangements between retail, wholesale and manufacturer licensees to include an outdoor stadium with a fixed seating capacity of at least 68,000 seats located in the City of Santa Clara (Levi’s Stadium – new home of the San Francisco 49ers).

AB 2184 (Hall), Chapter 480, Statutes of 2012. Created a new tied-house exception in the Act that authorized wine, beer and spirits producers to participate in promotional events held at an off-sale retail licensed location for the purpose of providing autographs on bottles or other items to consumers.

AB 605 (Portantino), Chapter 230, Statutes of 2010. Created a new type of license (instructional tasting license) that allows the tasting of beer, wine, and distilled spirits at off-sale licensed premises.

AB 2293 (De Leon), Chapter 638, Statutes of 2008. Added a new provision to the Act that permits a manufacturer of distilled spirits, winegrower, rectifier, or distiller, or its authorized agent to provide their product, as well as entertainment and food to consumers over 21 years of

age during invitation-only events (free of charge), as specified. The events must occur on premises for which a caterer's permit authorization has been issued.

AB 1245 (Torrico), Chapter 629, Statutes of 2008. Modified an existing provision of the Act to allow beer manufacturers to give adult consumers promotional advertising items valued up to \$3.

REGISTERED SUPPORT / OPPOSITION:

Support

Diageo
Distilled Spirits Council
Family Winemakers of California
Wine Institute

Opposition

Alcohol Justice
California Beer and Beverage Distributors
California Craft Brewers Association
California Teamsters Public Affairs Council

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