



WineAmerica Newsletter – November 2009

From The President's Desk

Congress

Congress is working much later this year than normal. There are so many critical issues on their agenda—health care, financial regulation, climate change, two wars, immigration and the worst economic environment since the depression—that movement and finality are extremely difficult. Most of these difficult issues have been rendered semi-intractable because of hyper-partisan bickering as the desire to work together to solve real problems seems to have evaporated.

In the midst of this environment, WineAmerica has worked diligently to gain advantage for America's wineries by educating members of Congress, building relationships, explaining the impact of particular measures on the developing farm network of grape growing and wine making, and presenting alternatives when appropriate. The scorecard is pretty encouraging.

WineAmerica continues to play a leadership role in shaping the growing research agenda of the Department of Agriculture to be more responsive to our needs. This includes maintaining the yearly funding for various special projects like Pierce's disease research and the Viticulture Consortium, working to gain full funding for Agricultural Research Service buildings in Geneva, New York, and Davis, California, and seeking to make the hard won advances in the Farm Bill, the Clean Plant Network and the Specialty Crop Research Initiative work effectively for our industry. We have had good success on these fronts.

WineAmerica mobilized its grassroots network to defeat a potentially damaging excise tax increase on wine and other alcoholic beverages that was being justified as a means to fund part of health care reform. We stressed the enormous damage such a tax increase would wreak on the development of wineries, a key foundation of value added agriculture in all fifty states. The wide distribution of concern about the negative impact on wineries was extremely helpful in getting the tax increase taken off the table, where it remains for now.

A budgetary proposal to charge fees to TTB regulated entities, including wholesalers, wineries, and retailers was also defeated. It would have effectively reinstated the annual Special Occupational Tax (\$500-\$1,500 per winery) which we worked so hard to repeal only a few years ago.

We are still working on an exemption for wine, beer and spirits producers from the pending Food Safety bill in order to prevent another agency from both regulating wineries and imposing fees (\$500-\$2,000 per year) to pay for their regulatory efforts.

WineAmerica was successful in getting an exemption in the House passed bill and is now working with the Senate to ensure that the exemption is included in the final law.

Page 2

WHO

As we have frequently reported, the WHO process for developing a policy regarding the health effects of alcohol consumption continues. The current effort is directed towards the development of a “WHO global strategy” to reduce the harmful use of alcohol—more a set of policy options than a proscriptive mandatory formula. Some proponents, meanwhile, notably Finland, Thailand, and India, are seeking to model the effort after WHO’s strong anti-tobacco “framework convention”—a treaty now signed by 168 signatories. The anti-tobacco convention requires signatory countries to take specific actions to discourage tobacco consumption. As stated by the WHO: “The WHO FCTC [Framework Convention on Tobacco Control] asserts the importance of demand reduction strategies as well as supply issues.” The dangers of this approach for our industry are pretty obvious. The end result could mean higher taxes, restrictions on advertisements, and “control of availability” which would justify government owned outlets, limited hours, and limited outlets among other restrictions.

WHO’s current working document, a preliminary step in the development of the “strategy draft,” is the result of consultations with non-governmental organizations, alcohol beverage industry members, and member states in six regions. At this time, WHO is working on a draft strategy to be presented to the WHO executive board the week of January 18, 2010. If consensus can be reached, the draft strategy will go to the full WHO body (World Health Assembly) in May 2010 for approval.

As reported in the WineAmerica September Newsletter:

<http://www.wineamerica.org/newsroom/newsletters/September%202009%20Newsletter.pdf> ,

the working paper contains some pretty objectionable, population based, anti-alcohol proposals along with some approaches which are based on selectively addressing harmful use. Industry observers are not sure what mixture will emerge as a first draft strategy. WHO watchers believe the draft strategy will be made available for review around the end of November. That provides only a few weeks before mid-January, interspersed with holidays, for industry to lobby member countries, and especially countries on the executive board, to push to reshape the draft in a way that minimizes damage to alcohol beverage producers. The U.S. representative is not currently a member of the executive board but will be able to sit in on the mid-January executive board meeting and make comments.

After the text of the draft strategy is available, industry representatives worldwide will seek to meet with their country’s WHO representatives to stress that policy measures should be cost-effective, feasible and evidence-based. The industry will object to population-based measures that are aimed at reducing demand generally because they are not directed at harmful consumption. One key challenge we face will be to take a positive approach that does not make us look obstructionist. It would certainly not be beneficial to imitate the tobacco industry which vigorously fought against any WHO action in regard to reducing tobacco use. It is important that we emerge as reasonable cooperators and not be stigmatized as naysayers in the manner tobacco is now viewed by the WHO.

Page 3

Considering that there are evidence based mechanisms that target harmful consumption directly, we should be well-placed to accomplish this.

International Seminar

In October, WineAmerica and TTB sponsored a seminar on how to export wine. The seminar was directed at wine association leaders and provided an overview of the extensive resources of the Federal government to facilitate, finance and otherwise foster wine exports, with a focus on small winery needs. It is a curious anomaly that exporting small quantities of wine can often be less of a hassle and potentially more profitable than developing distribution and sales in another domestic state. Besides a helpful overview presented by JBC International (a consultant that represents WineAmerica, Wine Institute and California Association of Winegrape Growers) there were detailed presentations from USDA-Foreign Agricultural Service, Department of Commerce, Small Business Administration, Export-Import Bank, United States Trade Representative and TTB. Each agency offers a deep reservoir of assistance, and in some cases cost sharing for wineries interested in exploring, facilitating, or financing export activities. Members interested in getting further information can contact either me or our Vice President, Cary Greene.

Horticulture Hearing

Congress is examining how the specialty crop provisions of the Farm Bill are functioning. The Horticulture and Organic Agriculture subcommittee of the House Agriculture Committee, chaired by Rep. Dennis Cardoza (D-CA), held a hearing on the Horticulture and Organic Agriculture title of the Farm Bill. The two witnesses were Ms. Rayne Pegg, Administrator, Agricultural Marketing Service (AMS), and Ms. Cindy Smith, Administrator, Animal and Plant Health Inspection Service (APHIS) at USDA.

Several issues of interest to the wine industry arose during the hearing:

- The witnesses were asked why USDA and the Administration targeted the National Clean Plant Network for a funding reduction considering the Farm Bill provided mandatory funding for the program. In response, the witnesses cited the struggling economy, the overall need to cut costs, and their feeling that the Plant Protection and Surveillance Program was sufficient to address emerging issues. Chairman Cardoza disagreed and reminded the witnesses that the Clean Plant program is critically important to the specialty crop industry. He also stated that he and the other members of the Agriculture Committee want the funding to remain intact.
- USDA wants to give the specialty crop industry more time to get their block grant applications in order for 2010, so the Notice of Funds Available will be announced in November and grant applications will be due in June 2010.

USDA would like to see more states consider multi-state grant applications for block grants in 2010 to better leverage research dollars.

Recruiting—The Importance of WineAmerica Membership

WineAmerica does a lot of work addressing “big picture” issues on behalf of American wineries. Such issues include WHO draft strategy, allergen and nutrition labeling, potential tax increases and other major policy issues. Our trade association also does a lot of work on a day to day basis for the benefit of individual wineries and state associations: wine label assistance, negotiating discounts, advising on audits, support on land use issues and helping state associations address state law concerns. This mixture of benefits provides

Page 4

important value for members both in the short and long term. As always, that value needs to be explained to wineries so that our membership base will increase and we will retain existing members. For this we rely on our current members. You are best placed to be our advocates and explain the importance of WineAmerica to non-member wineries less familiar with our work. WineAmerica members benefit from a broad membership base—not only does it provide us credibility as representatives of the industry, but it also helps divide costs more equitably. Please reach out and help with the recruiting process.



Basic Concepts for Improving State Winery Laws

By Cary Greene

As harvest comes to a close, we've been fielding more phone calls about how to improve state law for local wineries. Essentially, the calls boil down to two questions: (1) what is a winery; and (2) what privileges should wineries be afforded.

Conceptually, winery privileges are far easier to understand and explain than the definition of "winery." Winery privileges can be listed. They must account for the obvious needs of wineries and the obstacles to meeting those needs like the realities of alcohol beverage regulation and the imperatives of profitability, but ultimately they're easy to catalog. They include things like the ability to produce wine, operate tasting rooms, conduct off-site tastings, sell wine to consumers, ship wine to consumers, and sell wine to wholesalers and retailers. They also include less obvious privileges like the ability donate wine, operate restaurants, hold winery festivals and sponsor winery concerts and events. When we field questions about winery privileges, we're really being asked about the political challenges to achieving them—how to defend the development of a privilege and what mechanism to use to implement it?

Defining the term "winery" is hard because it's a philosophical question. We know that being a winery involves the production of wine, but it's not just a farmer growing grapes and producing wine from only those grapes. We know being a winery *does not* involve being a business that seeks to become a winery only to game the system, for example, a retailer that tries to make itself look like a winery by purchasing some branded wines so it can operate in places where retailers are otherwise prohibited from operating. The general restrictiveness of alcohol beverage regulation and the hard fought openness of winery privileges may create incentives for businesses to seek winery licenses even though they may not operate as a true producing winery. So it becomes a question of balance—how to allow wineries the freedom to develop their operations while limiting opportunities for abuse of the winery license?

When states try to define "winery," they make a judgment about which elements are required for a business to qualify as a winery. At least two approaches, sometimes overlapping, are most common. Both approaches have their benefits and limitations and states looking to develop or improve their laws must decide for themselves what will fit local conditions.

First, is the definitional approach. In Oregon, a winery is any business that "principally produces wine or cider in this state." In Arizona, a winery must "produce not less than two hundred gallons and not more than seventy-five thousand gallons of wine annually"

Page 5

and “at least seventy-five per cent” of the wineries fruit must be grown in-state. The definitional approach sets basic parameters for wineries—wineries are entitled to exercise the privileges of a winery so long as they conform to the basic definitional terms.

Second, is the slice and dice approach—affording multiple state winery licenses. New York and Virginia, among other successful wine producing states, have multiple winery license systems. The basic idea is that a grape grower that has wine produced for it may be entitled to one set of privileges; a winemaker that grows its own fruit and produces wine may be entitled to another set of privileges; and a producer or bottler that makes wine from fruit grown out-of-state or purchases wine in bulk may be entitled to a set of lesser privileges. The slice and dice approach certainly limits potential for abuse—the further a winery gets from agriculture, the fewer additional privileges its license affords. At the same time, the approach can lead to licensing systems that are overly complex. In New York, for instance, wineries are required to obtain separate permits if they want to operate off-premise tasting rooms or to sell at farmers markets. The benefits of the slice and dice approach—clarity and flexibility—can be easily lost in hyper-categorization.

Through the laboratory of the states, winery policy slowly improves.

WineAmerica is always looking for opportunities to make winery policy better, whether it's helping craft strategies for developing local winery privileges or more philosophical questions such as defining a winery. If you need our direction and support, we're always available to our members and their state associations.



Regulatory News: November 2009

TTB Issues Guidelines Regarding Returns of Breakage

The following was published by TTB in their October 16, 2009 newsletter.

Breakage

TTB has received numerous inquiries concerning whether returns of breakage (empty broken bottles which initially contained products) would be permitted under 27 CFR 11.32 (Defective products). Specifically, the inquiries relate to a situation where the breakage occurs after the retailer takes possession of the product. The wholesaler, who is not at fault for the breakage, then accepts the return of the breakage from the retailer.

Section 105(d) of the Federal Alcohol Administration Act (Act) (27 U.S.C. 205(d)) provides for the return of products for “ordinary and usual commercial” reasons arising after the product has been sold. Sections 11.32 through 11.39 of 27 CFR Part 11 – Consignment sales, specify what are considered “ordinary and usual commercial reasons” for the return of products and outline the conditions and limitations for such returns.

TTB does not consider product breakage to be covered by any of the exemplars of unmarketable products specified in 27 CFR 11.32, nor does TTB believe that product breakage is covered by any of the other sections of the TTB regulations that describe circumstances in which products may be returned for “ordinary and usual commercial reasons” within the meaning of section 105(d).

WineAmerica
1015 18th Street NW
Suite 500
Washington, DC 20036

PHONE: 202-783-2756

FAX: 202-347-6341

EMAIL:
info@wineamerica.org

Staff Contacts

Bill Nelson, President
bnelson@wineamerica.org

Cary Greene
Vice President &
General Counsel
cgreene@wineamerica.org

Jennifer Montgomery
Dir. of Grassroots &
Political Affairs
jmontgomery@wineamerica.org

Michael Kaiser
Manager of Regulatory
Affairs
labels@wineamerica.org

Adam Graytock
Operations Manager
agraytock@wineamerica.org

TTB views the providing of cash, credit or product to a retailer for breakage as a prohibited inducement under the Tied house provisions of the Act under 27 U.S.C. 205(b)(3) and the related Tied house regulations in 27 CFR 6.21(c) and 6.41. The costs incurred by a wholesaler relating to retrieving the breakage from the retailer would also be viewed as inducements under the same Tied house provisions noted above. Should the requisite elements of interstate or foreign commerce, similar State law (for cases involving male beverages), and exclusion be present, a violation would exist.

Damaged Products

TTB has also received numerous inquiries regarding whether a return would be allowed under 27 CFR 11.32 when damage occurs to a product after the retailer has taken possession of it. It is TTB's policy that if the damage is caused by the product itself, such as product deterioration which results in leaking containers of damaged labels, the product will be considered a defective product under 27 CFR 11.32, and shall be eligible to be exchanged for an equal quantity of identical products or may be returned for cash or credit against outstanding indebtedness. However, if the damage to the product is attributable to the retailer, for example, an employee of the retailer runs a forklift through a pallet containing cases of vodka, then the product would not qualify as a defective product under 27 CFR 11.32 and therefore, the product would not be eligible for exchange, return, or credit. In this example, the broken empty bottles would be viewed as breakage and be treated as breakage. Other unmarketable products like damaged labels, half filled bottles, broken caps, as well as any other damages to the products related to the forklift accident, would be viewed as damaged products not qualifying as defective products.

Potential violations concerning the return of damaged products not qualifying as defective products would be pursued as Consignment sales violations of the Federal Alcohol Administration Act under 27 U.S.C. 205(d) and 27 CFR 11.21(c).

A onetime acceptance of the return of damaged products by a wholesaler from the retailer would not result in a violation unless the privilege of return was extended by the time of sale. However, it is TTB's position that the acceptance of a second return of damaged products by the wholesaler from the retailer would infer that an implied privilege of return existed at the time of sale and such return could result in violations of the Consignment sales provisions of the Act.

