

GROWING YOUR DISTRIBUTION NETWORK: WHAT BREWERS NEED TO KNOW BEFORE SELLING BEER OUT-OF-STATE

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Deciding to expand beer distribution out-of-state is a big step for many brewers. While strategically evaluating the best market conditions is essential before moving forward with out-of-state distribution, it should not be a brewer's sole consideration. There are also many legal issues that should be evaluated before a brewer settles on target states for its expanded distribution network. If a brewer fails to address these legal issues before commencing out-of-state distribution, it could result in increased start-up costs, additional licensing and tax obligations, or administrative penalties. Provided below are a few common issues that a brewer may run into as it looks towards out-of-state distribution:

Foreign Qualification

In some cases, the target state's regulators could view the sale of the brewer's products or the brewer's dealings with parties in the target state as "transacting business" in the state. If a brewer is viewed as transacting business in the target state, the brewer must register with that state as a foreign qualified entity. By foreign qualifying, there may be additional business tax and licensing obligations with which the brewer is required to comply. In addition, failing to register when registration is required could subject the brewer to administrative and tax penalties. Therefore, a brewer should carefully consider the requirements and consequences of foreign qualification in the target state and structure its operations and contractual arrangements with distributors and other contacts in the target state accordingly.

State Licensing

A brewer that desires to distribute its beer in another state must often register with the target state's alcohol regulatory agency and/or file for a state-specific license. It is also important to note that some states bifurcate the regulation of high and low alcohol content beers. Depending on the ABV/ABW of the brewer's beer, the brewer and the beer could be subject to different licensing rules. Failure to appropriately register or license with the target state and comply with requirements for out-of-state brewers could subject the brewer to administrative penalties.

Label and Product Registration

If a brewer only has home state label approval, the brewer should file for label approval with the Alcohol and Tobacco Tax and Trade Bureau ("TTB") before moving forward with out-of-state distribution. Depending on the target state, submission of the TTB label approval paperwork may be sufficient to meet the target state's label and product registration requirements. In other cases, the target state's approval of the product and label may be required in addition to TTB approval.

Brewers should note that what was an acceptable label under their home state's rules may not be sufficient to meet the labeling requirements of the TTB (if they have not already registered) and the target state. Errors in label submissions may delay federal and state approvals and push back distribution launch dates. Understanding label submission requirements can be essential to avoiding unnecessary resubmissions of label approval requests.

Distribution Agreement

A brewer contracting with distributors in the target state should be wary of relying on a version of the distribution agreement it currently uses in its home state. The target state may have special rules with respect to relationships between brewers and distributors that must be adhered to. Applicable state requirements should be included in any contractual arrangement between the brewer and its target state distributor. A brewer could face potential administrative and contractual penalties if it fails to abide by such state-specific requirements.

Alternative Strategic Arrangements

If a brewer is looking to expand its distribution network but is restricted by geographic limitations (e.g. shipping across the country) or it's limited in its brewing capacity, it should consider other alternative strategic arrangements to meet its distribution needs. For example, a brewer may be able to set up a contract brewing arrangement with a brewer located in the target state, whereby the brewer licensed in the target state produces the brewer's beer. If a brewer's beer is produced by a licensed brewer located in the target state, it may reduce cost burdens associated with shipping and transporting the beer, as well as eliminate many of the licensing obligations associated with shipping across state lines.

While this is by no means an exhaustive list of the legal issues that a brewer may be confronted with when distributing out-of-state, it does illustrate several legal risks that can be easily avoided with careful planning and consultation. A brewer should consult with an experienced attorney before proceeding with any out-of-state distribution in order to fully address all legal matters that it may encounter with the expansion of its distribution network.

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