GODFREY & KAHN S.C.

ONE EAST MAIN STREET, SUITE 500 • POST OFFICE BOX 2719
MADISON, WISCONSIN 53701-2719
TEL • 608.257.3911 FAX • 608.257.0609
www • GKLAW.COM

MEMORANDUM

TO: Interested Parties

FROM: Mike Wittenwyler / Nate Zolik
Godfrey & Kahn, S.C.

DATE: March 27, 2017

SUBJECT: Wisconsin Attorney General's Opinion on Cross-Tier Restrictions

In a letter dated February 22, 2017, but not released until March 16, 2017, the Wisconsin Department of Justice ("DOJ") issued an informal advisory opinion to the Wisconsin Department of Revenue ("DOR"), concluding that municipalities may issue a Class "B" retail license to a winery to sell beer, and a "Class C" retail license to a brewery to sell wine. DOJ's conclusions are not consistent with either the spirt or the letter of state law regulating alcohol beverages.

While the facts presented in the advisory opinion are relatively narrow, the practical industry implications of DOJ's conclusions are much broader and have the potential to upend Wisconsin's three-tier industry business practice and regulation.

WISCONSIN'S THREE-TIER SYSTEM AND REGULATORY FRAMEWORK

Not only does DOJ ignore several statutory and practical arguments that undercut its position, the conclusions in the advisory opinion ignore the spirit of Chapter 125 of the Wisconsin Statutes and the general principles underlying the three-tier system. Capturing the principles that apply across the state's alcohol beverage regulatory system, Chapter 125 begins with the following statement of legislative intent:

> **125.01 Legislative intent.** This chapter shall be construed as an enactment of the legislature's support for the 3-tier system for alcohol beverages production, distribution, and sale that, through uniform statewide regulation, provides this state regulatory authority over the production, storage, distribution, transportation, sale, and consumption of alcohol beverages by and to its citizens, for the benefit of the public health and welfare and this state's economic stability. Without the 3-tier system, the effective statewide regulation and collection of state taxes on alcohol beverages sales would be seriously jeopardized. It is further the intent of the legislature that without a specific statutory exception, all sales of alcohol beverages shall occur through the 3-tier system, from manufacturers to wholesalers holding a permit to retailers to consumers. Face-to-face retail sales at licensed premises directly advance the state's interest in preventing alcohol sales to underage or intoxicated persons and the state's interest in efficient and effective collection of tax.

This statement reflects and reinforces Wisconsin's longstanding public policy and legislative enactment of dividing the alcohol beverage industry into three segments or tiers: production, distribution, and retail sale. Without a specific statutory exception, sales occur through the three-tier system "from

manufacturers to wholesalers holding a permit to retailers to consumers." This general policy statement does not distinguish between type of manufacturer or wholesaler or retailer. Instead, the sale of all alcohol beverages under all circumstances shall adhere to the three-tier system unless there is a specific statutory exception. Contrary to this clear statement on how Chapter 125 is to be interpreted, DOJ takes an opposite approach in reaching its conclusions: without a express statutory prohibition, a practice is permitted.

A key purpose of the three-tier structure is to prevent producers and wholesalers from "havin[ing] control over retail outlets."[1] This legislative public policy is undermined where market participants in the producer-tier are permitted to engage in retail alcohol sales. And, under Wis. Stat. § 125.01, such cross-tier business practices are only allowed where there is a "specific statutory exception." As explained below, Chapter 125 does not provide any specific statutory exceptions to support the DOJ opinion which endorses cross-tier ownership interests and business practices in the Wisconsin alcohol beverages industry.

ISSUANCE OF A CLASS "B" (BEER BAR) RETAIL LICENSE TO A WINERY

In deciding that municipalities may issue Class "B" retail licenses to wineries, DOJ makes the following three conclusions:

(1) Nothing in Wis. Stat. § 125.26 (regarding retail licenses for the sale of fermented malt beverages) expressly prohibits a winery from obtaining a Class "B" retail license;

(2) Under Wis. Stat. § 125.32(3m), a winery qualifies as an "other business" which may obtain a Class "B" retail license only if it has a separate doorway from the Class "B" premises; and,

(3) The cross-tier interest restrictions included in Wis. Stat. § 125.69 do not prohibit a winery from obtaining a Class "B" retail license.

DOJ Conclusion (1) is contrary to the legislative intent and requirement in Wis. Stat. § 125.01 that there must be a specific statutory exception to deviate from the three-tier system.

DOJ Conclusion (2) – and the applicability of Wis. Stat. § 125.32(3m) to a winery – does not comprehend the concept of a regulated "premises", understand the legislative intent in adopting this statutory exception or grasp the impracticality of its conclusion. Moreover, even if Wis. Stat. § 125.32(3m) did apply, the DOJ opinion fails to acknowledge that if a winery were otherwise permitted to hold a Class "B" retail license, the winery and the Class "B" business would need to conducted on entirely separate premises. *See* Wis. Stat. § 125.32(3m) ("No other business [the winery] may be conducted on premises operating under a Class "B" license or permit.").

DOJ Conclusion (3) is incorrect and reflects a misreading of Wis. Stat. § 125.69. The pertinent subsection, Wis. Stat. § 125.69(1)(c), provides:

> No manufacturer, rectifier, winery, or out-of-state shipper permittee, whether located within or without this state, may hold any direct or indirect interest in any wholesale permit or establishment. Except as provided in pars. (a) and (b)4. and s. 125.53, **no retail licensee may hold any direct or indirect interest in any manufacturer, rectifier, winery**, or out-of-state shipper permittee.

[1] *State v. Kay Distributing Co., Inc*, 110 Wis. 2d 29, 37 (1982).

(emphasis added). This subsection is unambiguous: "no retail licensee" encompasses all retail licensees, not just "Class A" and "Class B" intoxicating liquor retailers. Other provisions of Wis. Stat. § 125.69 use the narrower "*intoxicating liquor* retail licensee" and "*intoxicating liquor* retail license" where the intended scope is more limited and not meant to include fermented malt beverage retailers. *See* Wis. Stat. § 125.69(4)(a) and (d) (emphasis added). Had the legislature intended "retail licensee," as used in Wis. Stat. § 125.69(1)(c), to mean "intoxicating liquor retail licensee," it would have said so, just as it did in Wis. Stat. § 125.69(4)(a) and (d).

DOJ adds extra words into Wis. Stat. § 125.69(1)(c) making "no retail licensee" become "no *intoxicating liquor* retail licensee," pointing to the fact that Wis. Stat. § 125.69 is located in Subchapter III of Chapter 125. And, DOJ asserts, Subchapter III is generally concerned with intoxicating liquor licenses and permits, rather than beer. DOJ reasons that, "[t]he location of the interest-restriction provision in Wis. Stat. § 125.69 suggests that it is meant to apply only to licensees under Subchapter III, intoxicating liquor licensees." While it is true that Subchapter III is titled, "Intoxicating Liquor," and most of its provisions relate to intoxicating liquor licensees and permittees, nothing in Subchapter III states that it does not (or could not) in any circumstance apply to an intoxicating liquor permittee's relationships with beer licensees or permittees. In fact, Wis. Stat. § 125.69(1)(d) expressly regulates a brewpub's interests in an intoxicating liquor retail licensee. And, Wis. Stat. § 125.69(1)(c) prohibits distillers and wineries from holding "any direct or indirect interest in **any** wholesaler permit or establishment," not just wholesalers permitted under Wis. Stat. § 125.54 as intoxicating liquor wholesalers. (emphasis added).

The DOJ opinion is also inconsistent with the legislative history of Wis. Stat. § 125.69(1)(c). That subsection's "no retail licensee" provision was enacted as part of 2007 Wisconsin Act 85. The Legislative Reference Bureau ("LRB") analysis accompanying that legislation supports interpreting "no retail licensee" to include all retailers, not just intoxicating liquor retail licensees:

> The substitute amendment [which became Act 85] specifies that certain restrictions on common ownership interests that apply under current law to manufacturers, rectifiers, and wholesalers also apply to wineries and out-of-state shipper permittees. The substitute amendment further provides that rectifiers, wineries, and out-of-state shipper permittees may not hold any direct or indirect interest in any wholesale permit or establishment and that, except for a retail license issued to a winery, **no retail licensee** may hold any direct or indirect interest in any manufacturer, rectifier, winery, or out-of-state shipper permittee.
>
> Under current law, an exception to the common ownership restrictions allows a winery to hold **one** retail license, which may be a "Class A" license or a "Class B" license. The substitute amendment clarifies this exception, including specifying that the retail licensed premises may be on the winery premises or on real estate owned or leased by the winery and that the winery may distribute its own wine to its own retail premises without going through a wholesaler.

LRB Analysis, Senate Substitute Amendment 1 to 2007 Senate Bill 485 (emphasis added). It was clearly understood, at least at the time when Act 85 was being enacted, that wineries were allowed one retail license: either a "Class A" or a "Class B" – not a Class "B" beer bar license.

And, that conclusion is further supported by the structure and content of the separate "winery permit" statute, which specifies the limited instances under which a winery may engage in retail sales. *See* Wis. Stat. § 125.53(1). Entirely ignored by the DOJ opinion, the winery statute provides that a winery permittee "may also have either one 'Class A' license or one 'Class B' license, but not both." *Id.* The statute also describes other specific circumstances where a winery may make retail sales. *Id.* ("A winery holding a permit under this section may also make retail sales and provide taste samples on county or district fair fairgrounds …"). Nowhere does the winery permit statute authorize wineries to become Class "B" beer bar licensees. If the legislature had intended that wineries be authorized to operate as beer bars, it would have included Class "B" licensees among those specifically authorized in Wis. Stat. § 125.53.

DOJ's answer to "Question One" ignores the broader framework of chapter 125; is inconsistent with the clear and specific prohibition of Wis. Stat. § 125.69(1)(c); and, fails to acknowledge the scope of permissible activity which the legislature specifically set forth in the winery statute, Wis. Stat. § 125.53.

ISSUANCE OF A "CLASS C" (RETAIL WINE ONLY) LICENSE TO A BREWERY

The DOJ opinion concludes that breweries may be issued "Class C" retail licenses and serve wine to consumers for on-premises consumption. While Wisconsin's brewery statute, Wis. Stat. § 125.29, sets forth a specific list of activities which permitted breweries are authorized to engage in – and that list only allows the retail sale of intoxicating liquor (including wine) for breweries that held an intoxicating liquor license on June 1, 2011 – DOJ reasons that because there is no specific prohibition against a brewery holding a "Class C" license, then it must be permissible. Here again, DOJ ignores that chapter 125 is to be construed as an enactment of three-tier structure and regulation of the alcohol beverages industry.

The brewery permitting statute, Wis. Stat. § 125.29, only makes sense in the context of Wisconsin's three-tier industry structure. The statute enumerates specific instances – "statutory exceptions" in the parlance of Wis. Stat. § 125.01 – where breweries may engage in retail sales. *See* Wis. Stat. § 125.29(3)(e) – (i). And, it includes a very specific exception covering a brewery's retail sale of intoxicating liquor:

> Nothwithstanding ss. 125.04(9) and 125.09(1), the retail sale of intoxicating liquor, for on-premise consumption by individuals at the brewery premises or an off-site retail outlet established by the brewer, **if the brewer held, on June 1, 2011,** a license or permit authorizing the retail sale of intoxicating liquor and if the intoxicating liquor has been purchased by the brewer from a wholesaler holding a permit under s. 125.54.

Wis. Stat. § 125.29(3)(h) (emphasis added). If, as DOJ suggests, breweries were otherwise allowed to obtain intoxicating liquor retail licenses – including "Class C" licenses – then the exception in Wis. Stat. § 125.29(3)(h) would not be necessary.

The exception in § 125.29 (3)(h) allowing a brewery to engage in retail sales of intoxicating liquor, provided it held a license on June 1, 2011, was enacted as part of 2011 Wisconsin Act 32 ("Act 32"), a biennial budget bill. Following enactment of Act 32, the Legislative Fiscal Bureau described the new retail provisions of the brewery statute as follows:

> Under [Act 32], a brewer may not also hold a retail license, but a brewer's permit authorizes a brewer to make retail sales at the brewery premises and at one off-site retail outlet the brewer establishes. At these two retail locations, the brewer may make retail

sales of its own beer and of other Wisconsin-made beer and, if the brewer held a retail liquor license on June 1, 2011, intoxicating liquor.

Research Bulletin 2012-1, Wisconsin Legislative Fiscal Bureau, p. 4. The statute establishes the allowable scope of a brewery's retail sale of intoxicating liquor; and, contrary to the DOJ opinion, unless a brewery held an intoxicating liquor license on June 1, 2011, it may not sell intoxicating liquor (including wine) at retail.

CONCLUSION

In sum:

- Wisconsin regulates alcohol beverages in a three-tier system from manufacturers to wholesalers holding a permit to retailers to consumers;

- Any exceptions to this three-tier framework and the legislative intent for how Chapter 125 should be construed must be by specific statutory provisions; and,

- There are no specific statutory exceptions to support DOJ's conclusions, and, instead, the content and structure of chapter 125 undercut the DOJ opinion and directly conflict with its underlying conclusions.

If you have further questions or need any additional information, please let us know.

16994501.1