

## **Brewery and Distillery Law: New Developments and Top Challenges**



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# **Brewery and Distillery Law: New Developments and Top Challenges**

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## Presenters

**SARAH B. BENNETT** is a partner at Chestnut Cambronne PA, and has a dynamic practice rooted in real estate. On the transactional side of her practice, she advises real estate brokers, management companies, homeowners' associations, buyers and sellers of commercial and residential real estate, and business owners on a litany of matters from real estate to corporate formation to contracts. Ms. Bennett also represents small to mid-size business owners beginning with the initial formation of the entity throughout the life of the business. She also maintains a presence in the litigation side of the practice, including court appearances and motion practice, in both district and appellate courts. Ms. Bennett is an active alumna of William Mitchell College of Law, where she serves as a mentor to first and second-year law students. She is an active member of both the Minnesota State Bar Association and Hennepin County Bar Association. She received her B.A. degree from DePauw University and her J.D. degree from William Mitchell College of Law. Ms. Bennett has been recognized as a Minnesota Rising Star by *Super Lawyers* magazine in the area of Real Estate Law in 2015-2017.

**JEFFREY C. O'BRIEN** is a partner with Chestnut Cambronne PA, and serves as general counsel to a wide variety of small and closely held businesses, as well as real estate investors and developers. He has significant experience working with craft breweries, distilleries, and wineries on an array of issues, including entity formation, financing, real estate matters, intellectual property protection, operational issues, and distribution contracts. Mr. O'Brien's clients also include real estate agents, developers and investors, community banks, title companies, restaurant operators, manufacturing companies, franchised businesses, retired professional athletes, financial advisors, insurance agents, and consulting businesses. He is certified as a real property law specialist by the Minnesota State Bar Association. A frequent lecturer and writer, Mr. O'Brien has presented and written articles on a variety of business and real estate topics. He is a regular guest on several radio shows and podcasts. Mr. O'Brien has been listed as a Minnesota Super Lawyer every year since 2013. Previously, he had been named a Rising Star by *Minnesota Super Lawyers* every year since 2008, a designation reserved for only 2.5 percent of all attorneys in Minnesota. Mr. O'Brien was named as one of the 40 Under Forty in 2014 by the *Minneapolis-St. Paul Business Journal*. He received a B.S. degree, cum laude, from the University of St. Thomas; and a J.D. degree, cum laude, from William Mitchell College of Law.

**GARY K. LULOFF** is a partner with Chestnut Cambronne PA, and specializes in the areas of civil litigation, class action litigation, and government representation. Mr. Luloff has represented clients in criminal and civil courts around the state, before the Minnesota Court of Appeals and, through amicus curiae briefs, before the Minnesota Supreme Court. He is also admitted to practice in the United States District Court for the District of Minnesota. Mr. Luloff also served for six years as an investigator on the Second District Ethics Committee, and has been named a Rising Star each year since 2013. He received a B.A. degree from Carleton College and a J.D. degree from William Mitchell College of Law.

## **Presenters (Cont.)**

**NATALIE R. WALZ** is a litigation and transactional partner at Chestnut Cambronne PA, primarily practicing in the areas of real estate and intellectual property. Ms. Walz advises and assists clients regarding a broad range of legal and business matters, including issues related to intellectual property, trademark and copyright protection and enforcement, real estate, and homeowner association law. She has represented clients in state and federal courts, as well as before the Trademark Trial and Appeal Board. Ms. Walz has been named a Minnesota Rising Star by *Super Lawyers* magazine. In law school, Ms. Walz received the Dean's Award in Trial Advocacy and Sports Law. She also worked as an extern for the Chief Judge of the Minnesota Court of Appeals, and served as a volunteer assisting in the representation of individuals in Housing Court. Ms. Walz is a member of the Minnesota State Bar Association, Hennepin County Bar Association and the American Bar Association. She also participates in the mentor program at the University of St. Thomas School of Law. She received a B.A. degree, cum laude, from the University of St. Thomas; and a J.D. degree from the University of St. Thomas School of Law.



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Jeffrey C. O'Brien, Chestnut Cambronne PA

### State Brewery Bill Changes

- Need to register with the Secretary of State to obtain a tax ID.
- If you are 10 or more days late in filing or paying your taxes, you will be placed on the public **Tax Delinquency Liquor Posting List**.
  - Being on this list means that no wholesaler, manufacturer, or brewer can sell or deliver any product to you.
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  - The state also has the power to revoke or deny a renewal of license.

## State Brewery Bill Changes

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- In Minnesota, a brewery must obtain this license. This license must be renewed annually. Takes 30 days to process and can cost anywhere from \$20 - \$15,000 depending on the type of facility or license.
- **Requirements:**
  - \$10,000 Surety Bond;
  - Be at least 21 years old;
  - Has not had a license issued under Minn. Stat. § 340A revoked within the past years; and
  - Not been convicted of a felony within the past 5 years or any willful violation of federal, state, or local ordinances governing the manufacture, sale, distribution, or possession for sale of distribution of alcoholic beverages

## State Brewery Bill Changes

- While the TTB's licensing requirements and regulations apply for breweries and distilleries in any state within the U.S., state and local laws vary by jurisdiction.
- Be aware of which agency or agencies are responsible for reviewing your application and provide such agency/agencies with all required and requested documentation in order to ensure expeditious review and approval

## State Specific

- California: Proposition 65 warning regulations effective August 30, 2018
- Illinois: H.B. 4897 addresses issues relating to the sale, transfer, and storage of beer
- Pennsylvania: Sales and Use Tax Bulletin 2018-02 concerning taxation on the sale of malt or brewed beverages by manufacturers
- Rhode Island: H.B. 7092 reduces the alcoholic beverage manufacturing and wholesale licensing fee from \$3,000 to \$5,000
- Louisiana: House Resolution 244 designates the week of September 24 through 30, 2018 as Louisiana Craft Brewer Week
- Vermont: H.B. 710 creates an exception to the beer franchise law for certificate of approval holders and manufacturers that distribute not more than 50,000 barrels of malt

## State Franchise Law Database

- The Brewers Association has created a database of U.S. beer franchise laws: <https://www.brewersassociation.org/government-affairs/laws/franchise-laws/>

## New Excise Tax Reporting Guidelines

- Tax is calculated on the beer which is reported to be removed for consumption or sale in the United States
- Reported tax amounts should match Brewer's Report of Operations
- Any adjustments should be documented/explained in the appropriate section on form
- The Brewers Association has a summary of every state's excise tax rates:  
<https://www.brewersassociation.org/government-affairs/laws/state-excise-tax-rates/>

## Craft Beverage Modernization and Tax Reform Act

- Recalibrated the federal beer excise tax small brewers pay on each barrel of beer produced
- \$16 per barrel on first 6 million barrels
- \$18 per barrel for remaining barrels
- \$3.50 per barrel for first 60,000 barrels for production under 2 million barrels
- Reduced tax rates on distilled spirits

## TBB Issues Beer Transfer Guidance

- The Tax and Trade Bureau (TTB) published TTB Procedure 2018-1 Transfer of Beer Between Breweries Not of the Same Ownership providing brewers with guidance regarding the transfer of beer, without payment of tax, from one brewery to another brewery not of the same ownership
- Previously, only breweries of the same ownership could transfer beer between them without payment of tax. T
- The Craft Beverage Modernization and Tax Reform Act allows for the transfer of beer between breweries not of the same ownership without payment of tax.

## Pay-to-Play Beer Laws

- Safe harbor for consumer tastings or samplings
- Safe harbor for giving advertising materials to retailers
- Safe harbor for advertising retailers
- Near prohibition against paying retailers for advertising or for displaying your products
- Rules for events and live entertainment at retailers and
- Safe harbor for coupons

# THANK YOU!

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## How the Tax Cuts and Jobs Act Impacts Craft Brewers

Jeffrey C. O'Brien, Chestnut Cambronne PA

## Cash Basis Method for Accounting and Accounting for Inventories

- Allowed for tax purposes only for smaller entities and useful when:
  - For simpler accounting systems with accounting personnel who are not familiar with the more intricate accrual basis of accounting
  - Where there is no inventory to be tracked or valued
  - Where there is no need for an audit, as may be required by a lender
  - When the company is in the services business (which implies that there is no inventory)

## Cost of Equipment Write-Offs

<b>2018 Section 179</b>	
Example Calculation	
<b>Equipment Purchases:</b>	<b>\$ 1,150,000</b>
<b>First Year Write Off:</b> <small>(\$1,000,000 = maximum in 2018)</small>	<b>\$ 1,000,000</b>
<b>100% Bonus First Year Depreciation:</b> <small>(updated to 100% via Tax Cuts and Jobs Act)</small>	<b>\$ 150,000</b>
<b>Normal First Year Depreciation:</b> <small>(20% in each of 5yrs on remaining amount)</small>	<b>\$ 0</b>
<b>Total First Year Deduction:</b> <small>(\$1,000,000 + 150,000 + 0)</small>	<b>\$ 1,150,000</b>
<b>Cash Savings:</b> <small>(\$1,150,000 x 35% tax rate)</small>	<b>\$ 402,500</b>
<b>Equipment cost after Tax:</b> <small>(assuming a 35% tax bracket)</small>	<b>\$ 747,500</b>

Compliments of [www.crestcapital.com](http://www.crestcapital.com)

## New Rules Regarding Expensing Business Interests

- Allows for immediate depreciation of capital assets for the first 5 years after their purchase
- Receive a tax break on capital investments in the same year they are made rather than over several years
- Expands the cap on deductions from \$500,000 to \$1,000,000
- Expires in 2025
- Also includes interest deduction for business loans

## Research and Development Credit Opportunities

- Small businesses with \$50 million or less in gross receipts may claim the credit against the AMT for research and development
- Must be:
  - Technical in nature
  - Qualify as a permitted purpose (for the development of a new or improved aspect of their business)
  - Have the element of experimentation

## Excise Tax Rate Decrease

- Federal excise tax reduced to \$3.50/barrel from \$7/barrel on the first 60,000 barrels for domestic brewers producing less than 2 million barrels annually
- Reduced to \$16/barrel from \$18/barrel on the first 6 million barrels for all other brewers and beer importers
- \$18/barrel rate for over 6 million remains
- Transfer of beer between bonded facilities now allowed without tax liability

## 20% Deduction for Certain Pass-Through Income

- Income earned through entities such as sole proprietorships, LLCs, and partnerships entitled to a 20% deduction before income tax rates applies
- Includes:
  - Income from a sole proprietorship
  - Income from an LLC or S-corporation
  - Partnership income
  - Income from rental properties (Including income passed through from REITs)
  - Any S-corporation, partnership, or trust that owns an interest in another pass-through business.
- Limited for people who make more than \$157,000 a year. Deduction restricted to:
  - 50% of the wages paid by pass-through entity or
  - 25% of the wages paid plus 2.5% of the “tangible, depreciable property” to make income
- Cannot deduct wage income

## Converting to a C Corporation

- If your company plans to distribute all profits as dividends of a C-Corp., the effective tax cost will be higher to investors than if the business is a pass-through.
- Typically, dividends are taxed to an individual recipient at the qualified dividend rate of 20%, though there is usually no preferential tax rate at the state and local level.
- Dividends may also be subject to the 3.8% net investment income tax mentioned above.
- Taking into account only federal taxes, the effective double tax rate (combining the corporate and individual rates) is 39.8% on earnings distributed as dividends.

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# Entity Selection, Formation and Financing Difficulties Specific to Breweries and Distilleries

Sarah B. Bennett and Jeffrey C. O'Brien, Chestnut Cambronne PA

## The Complicated Three-Tier System



## Entity Formation

- Partnership
  - occurs when two or more people agree to conduct business together.
  - no specific documentation is required before a partnership is formed

## Entity Formation

- Subchapter S Corporation (“S Corp”)
  - Must make an election with the IRS
  - Restrictions on who can own shares of an S Corp
  - All shareholders have the same rights
  - Possible SE Tax Minimization
  - Preferable to C Corporation for small, closely held businesses (no double tax)

## Entity Formation

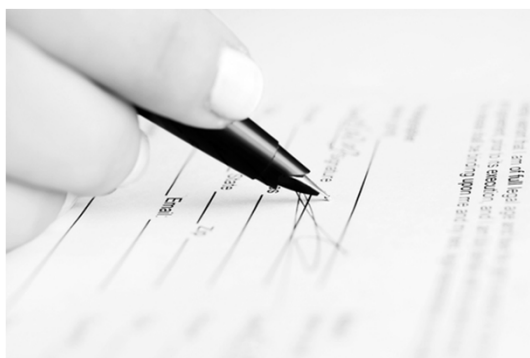
- Limited Liability Company (LLC)
  - Flexible structure
  - Ability to vary allocation of governance rights and financial rights
  - Single member LLC “disregarded” for federal income tax purposes; sole proprietorship income
  - Drawback: full SE tax (FICA applies to all income whether salary or profits)

## S Corp vs. LLC

- FICA Tax Minimization – S Corp
- Flexibility – LLC
- BUT: DON’T WORRY: Most state corporation and LLC statutes provide for a mechanism to convert an LLC to a corporation and a corporation to an LLC



## Entity Selection Tax Traps, Including Double Taxation



## Operational Issues, Including Difficulties in Decision- Making



## Drafting and Negotiating Sticky Provisions In Operating Agreements

- General Governance Documents
- Additional Brewery/ Distillery Provisions
  - Include provisions that require the ownership in the business to be subject to maintaining or passing any required local licensing.
  - If the owner does not meet these standards or fails to maintain these stands, the governance documents can establish procedures to terminate the relationship with the individual, including a forced buy-out of the owner's interest in the company.

## Carefully Documenting and Reporting Losses and Shortages

- Document any payments to the legal entity from the owners as either paid-in-capital or loans
- Do not commingle personal and business funds
- Do not pay owners in cash
- All payments to shareholders should be clearly documented as being wages, expense reimbursements, or profit distributions
- All expenses paid to shareholders should be reflected in formal expense reimbursement reports, backed up by appropriate receipts and invoices

## Documentation and State Filing Requirements

- Standard Documents

### S Corporation

- Articles of Incorporation
- Bylaws
- Initial Written Actions of Shareholders/Directors
- Shareholder Control Agreement (w/ Buy-Sell Provisions)
- Form SS-4
- Form 2553 (S Election)

### LLC

- Articles of Organization
- Operating Agreement
- Initial Written Actions
- Form SS-4

## Management and Governance: Hidden Dangers

- Operating agreements
- Membership control
- Partnership
- Shareholder control
- Buy-sell
- bylaws

## Brewery Financing Challenges – Crowdfunding and More

- What is a security?
  - 1933 Act default requires registration of any securities offering
  - Alternative: find an applicable exemption from registration
  - Also need to find an exemption from registration under state Blue Sky laws (each state where an investor resides)
- Accredited Investors
- Investment Capital
  - Section 4(2)
  - Regulation D
    - Rule 504
    - Rule 505
    - Rule 506 (now 506(b))

## Challenges in Raising Early Stage Capital Needs as it Relates to Growth

- Structuring a Private Offering
  - What percentage of ownership to sell?
  - Difference between voting and financial rights
  - Preferred distributions
  - “Sunset” provisions – call rights, put rights, etc.

## Complying With Complex State and Federal Securities Laws

- SEC registration is time consuming and expensive.
- For most small businesses, SEC registration is not a feasible option.
- Register" such sale with the Securities Exchange Commission (SEC) or
- Identify a specific exemption that allows such sale to be conducted without registration.

**THANK YOU!**

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# Intellectual Property, Marketing and Advertising: Hidden Dangers

Natalie R. Walz, Chestnut Cambronne PA

## Purpose of Trademarks

- Indicate the source of a product
- Distinguish products from each other and from other competitors
- Protect a company's investment in its business and brand
- Protect consumer expectations of quality and consistency

## Breweries in the US

	2012	2013	2014	2015	2016	2017
<b>Regional Craft Breweries</b>	97	119	135	178	186	202
<b>Microbreweries</b>	1,143	1,471	2,076	2,626	3,196	3,812
<b>Brewpubs</b>	1,180	1,308	1,528	1,740	2,042	2,252
<b>Large non-craft</b>	23	23	26	30	51	71
<b>Other non-craft</b>	32	31	20	14	16	35
<b>Total</b>	2,475	2,952	3,785	4,588	5,491	6,372

### Definitions:

- Regional craft brewery: annual product of between 15,000 and 6,000,000 barrels
- Microbrewery: less than 15,000 barrels per year, with 75% or more of its beer sold offsite
- Brewpub: restaurant-brewery that sells 25 percent or more of its beer on site
- “Craft” is a reference to the majority of the beer being marked by innovative beers

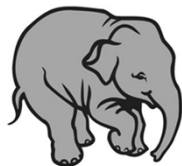
## Beer without Trademarks



## What Can Qualify as a Trademark?

- Nearly any matter that distinguishes the source of one product from another, including:
  - Words
  - Designs
  - Color(s)
  - Product Configurations, Packaging, Containers
  - Sales Environment
  - Scents
  - Sounds
  - Touch

## Beer Trademark: More than Just Words





## Non-Traditional Trademarks: Trade dress

- Trade dress refers to the overall appearance or image of a product



## Non-Traditional Trademarks: Trade Dress

- To be protectable, trade dress must be both non-functional and distinctive
  - Functionality: any attribute that makes the product more useful, or more easily used, or that contributes to the ease or economy of manufacture or distribution
    - Utilitarian Functionality: the product feature is either essential to the use or purpose of the article or affects the cost or quality of the article
    - Aesthetic Functionality: the product feature is one, the exclusive use of which, would put competitors at a non-reputation related disadvantage

## Non-Traditional Trademarks: Trade Dress

- To be protectable, trade dress must be both non-functional and distinctive
  - Distinctiveness: a product or its attribute's ability to identify a single source of goods or services, even if the source is unknown
    - Inherent: immediately capable of identifying a source of origin for a good or service
    - Acquired: trade dress that has obtained distinctiveness through use or promotion over time

## Non-Traditional Trademarks: Trade dress

- The mark consists of a compass design applied to a container of the goods



## Beer and Wine

- Likelihood of confusion established by showing that the goods are related in some manner and/or that the circumstances surrounding their marketing give rise to the mistaken belief that a the goods emanate from the same source



## Clearance: Can I Use the Mark?

- Why conduct clearance searches?
  - Avoid disputes with third-parties
    - And potential litigation costs
  - Avoid lost investment of time and money due to rebranding
- Two main types: preliminary and comprehensive
  - Preliminary searches are quick “knock out” searches of the USPTO to identify clear problems
  - Comprehensive searches look at the USPTO and common law uses (websites, state databases, etc.)

## Databases to Search

- Federal
  - U.S. Patent and Trademark Office
  - Alcohol and Tobacco Tax and Trade Bureau (TTB)
- State Licensing Agencies
  - State Liquor Licensing
  - Secretary of State (business entities and trademarks)
- Internet and Common Law
  - Google and Untappd

## How Much Clearance?

- Best practice: always conduct preliminary search
  - Identify marks with nationwide rights that would be difficult to defend against
- Comprehensive search for brewery name
  - Likely cost prohibitive for individual beer names
  - Consider trademark search engine
- Considerations
  - Will sales be regular, frequent, or significant?
  - How expensive to rebrand if a third-party objects?
  - What extent of distribution, if any?



## Adopt Strong Marks at the Outset

- Strong marks provide wider range of exclusivity
  - Competitors can get closer to weak marks with own brands
- Strong marks are immediately protectable
  - Weak marks may require acquired distinctiveness
- Acquired distinctiveness through extensive use
  - Commercial success through significant sales
  - Consumer awareness through advertising and publicity
  - Length of use (5 years may be sufficient for registration purposes)

## Enforcement Strategies

- Failure to enforce marks can diminish value
  - If multiple third-parties are using similar marks with the same or related goods, it can narrow the scope of protection afforded to a mark
  - Failure to enforce against a known infringer can prevent you from later enforcing your rights under the doctrines of laches, acquiescence, or estoppel

## Enforcement Strategies

- Develop your scope of enforcement
  - Enforce only brewery name or individual product marks?
  - Where will you set your “fences”?
    - How similar must the mark be?
    - How related must the goods or services be?
    - Third-party registration, use, or both?
- Monitoring can be done through third-party watch services or self-monitoring

## Enforcement Strategies

- Educate staff regarding documentation of instances of actual confusion
  - Misdirected phone calls, e-mails, etc.
- Before objecting, really consider the **business** case for enforcement
  - How is it harming your business, how could it harm your business in the future?
    - Is there a credible basis for pre- or post-sale confusion?
  - Customize your response based on these facts and issues

## Enforcement Strategies

- Trademark Trial and Appeal Board
  - Administrative agency operating similar to federal court, but can only address the right to register a trademark. It cannot issue injunctions or monetary awards.
  - Third-parties can oppose pending applications and cancel some existing registrations
  - Often more time and cost efficient than district court
- Letters of Protest with the USPTO
  - Ex parte petition, effective in limited circumstances
  - May avoid need to oppose a third-party application

## Enforcement Strategies

- Business contact sometimes best
  - Letters, phone calls, e-mails, etc.
    - Letters can be ghost written by attorneys where helpful
    - Attorney can also be involved later if escalation required
- Contact potential infringer early
  - Makes it easier (and cheaper) to comply with requests

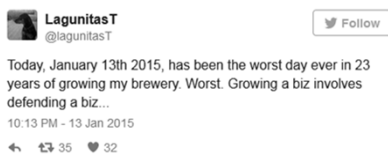
# Enforcement Strategies

- Addressing use of trademarks
  - Plaintiffs: trademark infringement lawsuits
  - Defendants: declaratory judgment actions
  - Attorney fee awards under *Octane Fitness*
    - New, more lenient standard for awards
- UDRP actions for some internet use

# Consider Public Perception



Lagunitas filed an infringement lawsuit, but within 48 hours:





## Copyright: Brewing Recipes and Processes

- Copyright protects original works of authorship
- Copyright does not protect ideas, procedures, methods, systems, processes, concepts, principles or discoveries
- Copyright does not protect a recipe that is a mere listing of ingredients
- Copyright may extend to a creative explanation of the recipe

## Copyright: Brewing Recipes and Processes

- Our Northeast Pale Ale is brewed with Pale and Pilsner malt, along with a copious amount of Citra hops that give a super hazy and juicy color to the beer. Bright oranges fall on the nose with a smooth, citrus flavor on the palate. If you close your eyes, you just might think this beer was juiced rather than brewed.”



## Confidentiality and Non-Disclosure Agreements

- Hidden dangers:
  - Proper identification of the parties to the agreement, including the proper legal name of the business entity.
  - Execution of the agreement by an individual with authority to bind the recipient of the confidential information.
  - Proper definition of what constitutes confidential information such that it includes all confidential information that may be disclosed but not so broad that it is unenforceable.
  - Failing to treat confidential information as confidential

## Compliance with Other Regulations

- TTB restrictions that affect brand names
  - No misleading names with respect to characteristics of the product
  - No disparagement of competitor brands
  - No “obscene or indecent” designs

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# Difficulties in Obtaining the Correct Licenses and Permits

Jeffrey O'Brien, Chestnut Cambronne PA

## Federal Regulatory Framework

- **Alcohol and Tobacco Tax and Trade Bureau (TTB)**
  - The Alcohol and Tobacco Tax and Trade Bureau (TTB) regulates craft beer at the federal level. (Brew Law 101 at 59).
  - Anyone brewing beer for sale must obtain a Brewer's Notice from the TTB. You can find the form online at their website but be aware the process can take on
  - average 129 days. *Id.*
  - The application requires a heavy amount of paperwork, including personal information for every officer, director, and shareholder who holds at least 10% interest in the company. *Id.*

## Federal Regulatory Framework

- **Food and Drug Administration (FDA)**
  - Federally regulates any “facility that manufactures, processes, packs, or holds food or beverages – including alcoholic beverages – for consumption in the United States.” *Id* at 60.
  - You must register with the FDA biannually, but there is no fee involved. *Id.*

## State Regulatory Framework

- Need to register with the Secretary of State to obtain a tax ID.
- If you are 10 or more days late in filing or paying your taxes, you will be placed on the public **Tax Delinquency Liquor Posting List**.
  - Being on this list means that no wholesaler, manufacturer, or brewer can sell or deliver any product to you.
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- **Requirements:**
  - \$10,000 Surety Bond;
  - Be at least 21 years old;
  - Has not had a licensed issued under Minn. Stat. § 340A revoked within the past years; and
  - Not been convicted of a felony within the past 5 years or any willful violation of federal, state, or local ordinances governing the manufacture, sale, distribution, or possession for sale of distribution of alcoholic beverages

## State - Level Registration

- While the TTB's licensing requirements and regulations apply for breweries and distilleries in any state within the U.S., state and local laws vary by jurisdiction.
- Be aware of which agency or agencies are responsible for reviewing your application and provide such agency/agencies with all required and requested documentation in order to ensure expeditious review and approval.

## Local Regulatory Framework

- State specific

Example) Minnesota licensing for growlers and tap/cocktail rooms

- Must obtain license from Municipality even though it is state regulated

## Top Permitting and Licensing Issues

- First and foremost, it is imperative to understand what permits and licenses must be obtained at each level of government before operations can legally begin.
- At the **Federal level**, when you are seeking a brewer's notice or distilled spirits plant license, be sure that your application is complete and accurate, as incomplete applications will not be reviewed and will ultimately be dismissed.
- At the **State level**, be aware of which agency or agencies are responsible for reviewing your application and provide such agency/agencies with all required and requested documentation in order to ensure expeditious review and approval.
- It is also imperative to understand what **local requirements** exist as to the brewery or distillery, be they taproom/cocktail room licenses or other issues (such as growler sales restrictions and/or garden variety land use/zoning requirements).

## Navigating TBB Labeling Regulations: Federal Level

- Information and documents to be submitted to the TTB in connection with the Brewer's Notice application include the following:
  - Articles of Organization (LLC) / Articles of Incorporation Corp.)
  - Operating Agreement (LLC) / By Laws (Corp.)
  - Federal EIN (from IRS)
  - Owner Officer Questionnaires (for each owner of 10%+ and each officer)
  - List of all owners and officers identifying percentage of voting ownership, amount of funds invested, etc. (if owner is an entity, EIN)
  - Source of Funds Documents (bank statements, loan documents, etc.)
  - Diagram of Premises
  - Description of Property (usually metes & bounds is best)

## Navigating TBB Labeling Regulations: Federal Level

### **CONTINUED**

- Description of Equipment (more reviewers are requiring this, at least provide size of tanks)
- Description of the Building (walkthrough of the brewery premises)
- Environmental Questionnaire (number of employees, amount of waste, disposal of liquid and solid waste, electric/gas provider name, etc.)
- Supplemental (disposal of waste into navigable waterways, etc.)
- Brewer's Bond
- Consent of Surety (if using a non-contiguous warehouse, alternating premises between a brewery and a distillery, running an alternating proprietorship, etc.)
- Lease agreement or mortgage (with permission to use premises as a brewery/distillery)
  - an attorney



## Navigating TBB Labeling Regulations: Federal Level

### **CONTINUED**

- Assumed name registration (if applicable)
- Security statement
- Designation of a main contact person
- Copy of ID for main contact person
- Signing authority resolution for application contact
- TTB's Signing Authority Form

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# Other Issues

Jeffrey O'Brien, Chestnut Cambronne PA

## Labeling Challenges

- TBB labeling regulations
- Local and state regulations
- Formula approvals

## Choosing Distributors Carefully: Hidden Dangers to be Aware Of and Distribution Agreements

- State distribution laws
- Franchise laws
- “Notice-and-cure” requirements
- Self-distribution

## Neglecting Labor and Employment Issues

- Contract Brewing
- At will employees
- Volunteers/ Student Interns
- Fair Labor Standards Act
- Independent Contractor

## Navigating the Complex Legal, Regulatory and Policy Landscape

- Critical recordkeeping
- Required records
- Tax mistakes
- Brewer's Report of Operations

## Difficulties in Choosing to Lease or Purchase Real Estate

- Location, Location, Location!
- Commercial lease agreements:
  - Triple net
  - gross

## Challenges in Satisfying Brewery and Distillery Plant, Equipment and Inventory Needs

## Complicated Insurance and Liability Matters

- General liability insurance;
- Workers compensation; and
- Dram shop (if the business is serving alcohol for on-premise consumption).

# THANK YOU!

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# Ethical Challenges

Gary K. Luloff, Chestnut Cambronne PA

## Ethical Standards and Civil Liability

- Lawyer Ethics: Not an Oxymoron
- Model Rules of Professional Conduct
- States' Rules of Professional Conduct or Professional Responsibility

## Ethical Standards and Civil Liability

- Majority courts: violation of ethical standards is evidence of attorney malpractice.
- Compliance with ethical standard may be defense to attorney malpractice.

## Avoiding Conflicts of Interest

- What is a conflict of interest?
- Who determines whether a conflict exists?
- Is there a conflict?



## Avoiding Conflicts of Interest

- Who is the client?
- How is attorney-client relationship formed?
- Can the lawyer represent despite the conflict?
- What is concurrent representation and informed consent?

## Who is the Client?

- Organization or entity as client
  - (LLC, Corporation)
- Representation of individuals
- Representation of affiliates

## Confidentiality

- What is a lawyer's duty of confidentiality?
- What is the attorney-client privilege?
- When an entity (LLC or Co.) is the client?

## Adequacy of Fees and Charges

- What is a retainer agreement?
- What is a reasonable fee?
- Can a lawyers take an ownership stake in exchange for services?
- What transactions are prohibited?

## What Would You Do?

- Ethical Scenarios

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**Hot Topics, New Developments,  
Law Changes and More!**

**Submitted by Jeffrey C. O'Brien**



**Hot Topics, New Developments, Law Changes, and  
More!**

**Submitted by Jeffrey C. O'Brien  
Chestnut Cambronne PA**

## **A. State Brewery Bill Changes**

- a. Need to register with the Secretary of State to obtain a tax ID.
- b. If you are 10 or more days late in filing or paying your taxes, you will be placed on the public Tax Delinquency Liquor Posting List. Being on this list means that no wholesaler, manufacturer, or brewer can sell or deliver any product to you. You cannot purchase beverages for resale if you are on the list. The state also has the power to revoke or deny a renewal of license.
- c. Wholesaler/Manufacturer's Intoxicating Liquor License
  - In Minnesota, a brewery must obtain this license. This license must be renewed annually. Takes 30 days to process and can cost anywhere from \$20 - \$15,000 depending on the type of facility or license.
  - Requirements:
    - a. \$10,000 Surety Bond;
    - b. Be at least 21 years old;
    - c. Has not had a license issued under Minn. Stat. § 340A revoked within the past years; and
    - d. Not been convicted of a felony within the past 5 years or any willful violation of federal, state, or local ordinances governing the manufacture, sale, distribution, or possession for sale or distribution of alcoholic beverages.
- **State Specific Legislative Updates:**
  - a. California: Proposition 65 warning regulations effective August 30, 2018
  - b. Illinois: H.B. 4897 addresses issues relating to the sale, transfer, and storage of beer
  - c. Pennsylvania: Sales and Use Tax Bulletin 2018-02 concerning taxation on the sale of malt or brewed beverages by manufacturers
  - d. Rhode Island: H.B. 7092 reduces the alcoholic beverage manufacturing and wholesale licensing fee from \$3,000 to \$5,000
  - e. Louisiana: House Resolution 244 designates the week of September 24 through 30, 2018 as Louisiana Craft Brewer Week



- f. Vermont: H.B. 710 creates an exception to the beer franchise law for certificate of approval holders and manufacturers that distribute not more than 50,000 barrels of malt

**B. New Excise Tax Reporting Guidelines**

- a. Tax is calculated on the beer which is reported to be removed for consumption or sale in the United States
- b. Reported tax amounts should match Brewer's Report of Operations
- c. Any adjustments should be documented/explained in the appropriate section on form
- d. A summary of every states excise tax rates can be found here:  
<https://www.brewersassociation.org/government-affairs/laws/state-excise-tax-rates/>

**C. Craft Beverage Modernization and Tax Reform Act**

- See attached Appendix
  1. The Tax and Trade Bureau (TTB) published TTB Procedure 2018-1 Transfer of Beer Between Breweries Not of the Same Ownership providing brewers with guidance regarding the transfer of beer, without payment of tax, from one brewery to another brewery not of the same ownership. Previously, only breweries of the same ownership could transfer beer between them without payment of tax. However, the Craft Beverage Modernization and Tax Reform Act allows for the transfer of beer between breweries not of the same ownership without payment of tax.

**D. Pay-to-Play Beer Laws**

- **6 categories of advertising through near prohibitions and “safe harbors” for federal regulators:**
  1. Safe harbor for consumer tastings or samplings
    - Permitted
    - Can be purchased from that retailer but not above ordinary retail price
  2. Safe harbor for giving advertising materials to retailers
    - \$300 limit on product displays
    - Product and displays must bear “conspicuous and substantial advertising matter”
    - Tap handles with or without brewer’s logos may be sold at cost or higher to retailers if the retailers pay within 30 days
    - Special recordkeeping
    - Paying the retailer for displaying or advertising is prohibited
  3. Safe harbor for advertising retailers
    - Brewers can advertise names and addresses of two or more unaffiliated retailers
  4. Near prohibition against paying retailers for advertising or for displaying your products
    - Paying or crediting a retailer for advertising is prohibited if it compromises the retailer’s independence
  5. Rules for events and live entertainment

- Sponsorship and advertising of temporary retailers is permissible (dealers who are not retailers for more than four days in a row and less than 5 events per year)
  - No rules for advertising at ball parks and stadiums
6. Safe harbor for coupons
- Permissible if the coupons can be redeemed at all retailers within the geographical area

#### **D. State Franchise Law Summary**

- See Attached Appendix B

APPENDIX 1

Exempt Ingredients and Processes Determined to be  
Traditional Under TTB Ruling 2015-1

TTB Ruling 2015-1  
Attachment 1

**Exempt Ingredients Under the conditions of TTB Ruling 2015-1**

*Industry members are responsible for ensuring that all ingredients, including any parts of fruit, used in the production of malt beverages or beer are wholesome products suitable for human food consumption and comply with applicable ingredient safety regulations of the Food and Drug Administration.*

INGREDIENT	DESCRIPTION/LIMITATION
AGAVE	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
ALLSPICE	As outlined in FDA's GRAS listing at <u>21 CFR 182.10</u> . Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
ANISE	As outlined in FDA's GRAS listing at <u>21 CFR 182.10</u> . Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
APPLES	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
APRICOTS	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
BASIL	Includes bush basil and sweet basil, as outlined in FDA's GRAS listing at <u>21 CFR 182.10</u> . Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
BILBERRIES	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
BLACKBERRIES	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
BLUEBERRIES	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
BLACK CURRANTS	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups. <i>Also see RED CURRANTS</i>
BLOOD ORANGES	Whole, juice, puree, concentrate, peel, or zest. <i>Does not</i> include extracts, essential oils, or syrups.
BOYSENBERRIES	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
BROWN SUGAR	When brewers use brown sugar in the fermentation of a malt beverage, the designation is not required to refer to the ingredient. Instead, the malt beverage may be labeled as a "beer" or "ale" and so forth.
CANDY (CANDI) SUGAR	When brewers use candy/candi sugar in the fermentation of a malt beverage, the designation is not required to refer to the ingredient. Instead, the malt beverage may be labeled as a "beer" or "ale" and so forth.
CAMOMILE (CHAMOMILE)	Includes English, Roman, German, and Hungarian, as outlined in FDA's GRAS listing at <u>21 CFR 182.10</u> . Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
CAPSICUM	As outlined in FDA's GRAS listing at <u>21 CFR 182.10</u> . Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.

INGREDIENT	DESCRIPTION/LIMITATION
CARAWAY, BLACK CARAWAY (BLACK CUMIN)	Includes caraway, black caraway (black cumin), as outlined in FDA's GRAS listing at <u>21 CFR 182.10</u> . Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
CARDAMOM (CARDAMON)	As outlined in FDA's GRAS listing at <u>21 CFR 182.10</u> . Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
CASSIA	Includes Chinese, Padang, Batavia, and Saigon cassias, as outlined in FDA's GRAS listing at <u>21 CFR 182.10</u> . Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
CHERRIES	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
CHICORY	Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
CHOCOLATE	<i>Does not</i> include extracts, essential oils, or syrups. Brewers may make non-misleading references to the use of chocolate malt by designating a product as, for example, "chocolate stout," even though it contains no added chocolate.
CINNAMON	Includes Ceylon, Chinese, and Saigon cinnamons, as outlined in FDA's GRAS listing at <u>21 CFR 182.10</u> . Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
CLEMENTINE	Whole, juice, puree, concentrate, peel, or zest. <i>Does not</i> include extracts, essential oils, or syrups.
CLOVE	Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
COCOA	Includes cocoa powder or cocoa nibs. <i>Does not</i> include extracts, essential oils, or syrups.
COCONUT	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
COFFEE	Coffee beans, coffee grounds, or coffee brewed with water. <i>Does not</i> include extracts, essential oils, or syrups.
CORIANDER	As outlined in FDA's GRAS listing at <u>21 CFR 182.10</u> . Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
CRANBERRIES	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
CUMIN (CUMMIN), BLACK CUMIN (BLACK CARAWAY)	Includes cumin (cummin) and black cumin (black caraway), as outlined in FDA's GRAS listing at <u>21 CFR 182.10</u> . Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
DATES	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
ELDER FLOWERS	As outlined in FDA's GRAS listing at <u>21 CFR 182.10</u> . Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
FIGS	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
GINGER	As outlined in FDA's GRAS listing at <u>21 CFR 182.10</u> . Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
GRAINS OF PARADISE	As outlined in FDA's GRAS listing at <u>21 CFR 182.10</u> . Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.

INGREDIENT	DESCRIPTION/LIMITATION
GRAPES	Whole, juice, puree, concentrate, or grape must. <i>Does not</i> include extracts, essential oils, or syrups. <b>REMINDER:</b> As set forth in the ruling, any exemption from the formula requirement applies only when used in the production of a malt beverage as defined at <u>27 CFR 7.10</u> .
GRAPEFRUIT	Whole, juice, puree, concentrate peel, or zest. <i>Does not</i> include extracts, essential oils, or syrups.
HIBISCUS	Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
HONEY	<i>Does not</i> include extracts, essential oils, or syrups.
HUCKLEBERRIES	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
JASMINE	Spices may be whole or ground. <i>Does not include extracts, essential oils, or syrups.</i>
JUNIPER BERRIES	Spices may be whole or ground. <i>Does not include extracts, essential oils, or syrups.</i>
KALE	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
KIWI	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
KUMQUAT	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
LACTOSE	When brewers use lactose in the production of a malt beverage, the designation is not required to refer to the ingredient. Instead, the malt beverage may be labeled as a "beer" or "ale" and so forth.
LEMONS	Whole, juice, puree, concentrate, peel, or zest. <i>Does not</i> include extracts, essential oils, or syrups.
LEMON GRASS	Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
LIME	Whole, juice, puree, concentrate, peel, or zest. <i>Does not</i> include extracts, essential oils, or syrups.
MACE	As outlined in FDA's GRAS listing at <u>21 CFR 182.10</u> . Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
MANGO	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
MARIONBERRIES	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
MAPLE SUGAR/SYRUP	When brewers use maple sugar/syrup in the fermentation of a malt beverage, the designation is not required to refer to the ingredient. Instead, the malt beverage may be labeled as a "beer" or "ale" and so forth.
MOLASSES/BLACKSTRAP MOLASSES	When brewers use molasses/blackstrap molasses in the fermentation of a malt beverage, the designation is not required to refer to the ingredient. Instead, the malt beverage may be labeled as a "beer" or "ale" and so forth.
NECTARINE	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
NUTMEG	As outlined in FDA's GRAS listing at <u>21 CFR 182.10</u> . Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.

INGREDIENT	DESCRIPTION/LIMITATION
ORANGES	Whole, juice, puree, concentrate, peel, or zest. <i>Does not</i> include extracts, essential oils, or syrups.
ORANGE BLOSSOM/FLOWER	Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
OYSTERS/OYSTER SHELLS	Whole oysters, juice, or puree. <i>Does not</i> include extracts, essential oils, or syrups. Oyster shells may be used when consistent with good commercial practice.
PASSIONFRUIT	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
PEARS	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
PEACHES	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
PEPPER, BLACK OR WHITE	Includes black pepper and white pepper, as outlined in FDA's GRAS listing at 21 CFR 182.10. Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
PEPPER, CAYENNE OR RED	Includes cayenne peppers and red peppers, as outlined in FDA's GRAS listing at 21 CFR 182.10. Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
PEPPERS	Includes hot, chili and bell peppers. Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
PEPPERMINT	As outlined in FDA's GRAS listing at 21 CFR 182.10. Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
PINEAPPLE	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
PLUM	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
POMEGRANATE	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
PUMPKINS	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
RAISINS	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
RASPBERRIES	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
RED CURRANTS	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups. <i>Also see BLACK CURRANTS</i>
ROSEMARY	As outlined in FDA's GRAS listing at 21 CFR 182.10. Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
SAFFRON	As outlined in FDA's GRAS listing at 21 CFR 182.10. <i>Exempt when used only as a flavor and not exclusively as a coloring material.</i> Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
SAGE, GREEK SAGE	As outlined in FDA's GRAS listing at 21 CFR 182.10. Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.

INGREDIENT	DESCRIPTION/LIMITATION
SODIUM CHLORIDE	When brewers use sodium chloride in the fermentation or flavoring of a malt beverage, the designation is not required to refer to the ingredient. Instead, the malt beverage may be labeled as a “beer” or “ale” and so forth.
SPEARMINT	As outlined in FDA’s GRAS listing at <u>21 CFR 182.10</u> . Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
STAR ANISE	As outlined in FDA’s GRAS listing at <u>21 CFR 182.10</u> . Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
STRAWBERRIES	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
SWEET POTATOES	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
TANGERINE	Whole, juice, puree, concentrate, peel, or zest. <i>Does not</i> include extracts, essential oils, or syrups.
TEA	Tea may be whole leaves or ground. <i>Does not</i> include extracts, essential oils, or syrups. REMINDER: as set forth in the ruling, the exemption from any formula requirement applies only when used in the production of a malt beverage as defined at <u>27 CFR 7.10</u> , and would not apply to products (such as many kombucha products) fermented solely from tea and sugar, which are beer under the IRC, but is not a “malt beverage.”
THYME/WILD OR CREEPING THYME	Includes thyme and wild or creeping thyme, as outlined in FDA’s GRAS listing at <u>21 CFR 182.10</u> . Spices may be whole or ground. <i>Does not</i> include extracts, essential oils, or syrups.
VANILLA	As outlined in FDA’s GRAS listing at <u>21 CFR 182.10</u> . REMINDER: As set forth in the ruling, the exemption of vanilla from the formula requirement applies only to the use of vanilla in the form of whole or crushed vanilla beans. <i>Does not</i> include vanilla powders, extracts, essential oils, or syrups.
WATERMELON	Whole, juice, puree, or concentrate. <i>Does not</i> include extracts, essential oils, or syrups.
YUZU	Whole, juice, puree, concentrate, peel, or zest. <i>Does not</i> include extracts, essential oils, or syrups.

**Processes Determined to be Traditional**

*Industry members may use woodchips, staves, or spirals derived from barrels that were previously used in the production or storage of distilled spirits or wine as part of the process of aging beer, as well as woodchips previously used in the aging of distilled spirits or wine, provided that this process does not add any discernible quantity of distilled spirits or wine to the beer.*

- Aging beer in plain barrels or with plain woodchips, spirals or staves made of any type of wood.
- Aging beer in barrels, containing no discernible quantity of wine or distilled spirits, that were previously used in the production or storage of wine or distilled spirits.
- Aging beer with woodchips, spirals or staves derived from barrels, containing no discernible quantity of wine or distilled spirits, that were previously used in the production or storage of wine or distilled spirits, or with woodchips, containing no discernible quantity of wine or distilled spirits, that were previously used in the aging of wine or distilled spirits.



APPENDIX 2

**PRE-COLA PRODUCT EVALUATIONS FOR  
DISTILLED SPIRITS PRODUCTS**

The following chart lists the current pre-COLA product evaluation requirements for a number of distilled spirits products. An "X" in the table indicates that a pre-COLA product evaluation of the type shown is required as a condition of COLA approval for the product and must be obtained prior to applying for label approval. A copy of the approved pre-COLA document must be submitted with the COLA application. In addition to the pre-COLA product evaluations noted below, a sulfite analysis is required for standard wines that do not have a sulfite declaration on the label. Descriptions of the pre-COLA product evaluations are provided in the text of Industry Circular 2007-4.

This chart is provided as general guidance. Particular circumstances may dictate the need for a pre-COLA product evaluation for a specific product even though no such requirement is indicated on the chart.

PRODUCT	DOMESTIC (D) OR IMPORTED (I)	LABORATORY ANALYSIS	PRE-IMPORT LETTER	FORMULA (TTB F 5100.51 or TTB F 5110.38)	COMMENT
A Blend Of Straight Bourbon Whiskies Or Blended Straight Bourbon Whiskies	D I	- -	- -	- -	PRODUCT OF U.S. ONLY
A Blend Of Straight Corn Whiskies Or Blended Straight Corn Whiskies	D I	- X	- -	- -	
A Blend Of Straight Malt Whiskies Or Blended Straight Malt Whiskies	D I	- X	- -	- -	
A Blend Of Straight Rye Malt Whiskies Or Blended Straight Rye Malt Whiskies	D I	- X	- -	- -	
A Blend Of Straight Rye Whiskies Or Blended Straight Rye Whiskies	D I	- X	- -	- -	
A Blend Of Straight Wheat Whiskies Or Blended Straight Wheat Whiskies	D I	- X	- -	- -	
A Blend Of Straight Whiskies Or Blended Straight Whiskies	D I	- X	- -	- -	
Advocaat	D I	- -	- X	X -	
Alcohol	D I	- -	- -	- -	
Amaretto	D I	- -	- X	X -	
Anise	D I	- -	- X	X -	
Anisette	D I	- -	- X	X -	

PRODUCT	DOMESTIC (D) OR IMPORTED (I)	LABORATORY ANALYSIS	PRE-IMPORT LETTER	FORMULA (TTB F 5100.51 or TTB F 5110.38)	COMMENT
Applejack	D	-	-	X*	*If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	X	-	-	
Apricot Sour	D	-	-	X	
	I	-	X	-	
Aquavit	D	-	-	X	
	I	-	X	-	
Arack/Arak	D	-	-	X	
	I	-	X	-	
Armagnac	D	-	-	X*	*PRODUCT OF FRANCE ONLY; however, harmless coloring/flavoring/ blending materials may be added in the U.S. If harmless coloring/ flavoring/blending materials are added in the U.S., a formula is required.
	I	-	-	-	
Bitters	D	-	-	X	
	I	-	X	-	
Black Russian	D	-	-	X	
	I	-	X	-	
Blended Applejack Or Applejack – A Blend	D	-	-	X	
	I	X	-	-	
Blended Bourbon Whisky Or Bourbon Whisky – A Blend	D	-	-	X	PRODUCT OF U.S. ONLY
	I	-	-	-	
Blended Canadian Whisky Or Canadian Whisky – A Blend	D	-	-	-	PRODUCT OF CANADA ONLY
	I	-	-	-	
Blended Corn Whisky Or Corn Whisky – A Blend	D	-	-	X	
	I	X	-	-	
Blended Irish Whisky Or Irish Whisky – A Blend	D	-	-	-	PRODUCT OF THE REPUBLIC OF IRELAND OR NORTHERN IRELAND ONLY
	I	-	-	-	
Blended Light Whisky Or Light Whisky – A Blend	D	-	-	X	PRODUCT OF U.S. ONLY
	I	-	-	-	
Blended Malt Whisky Or Malt Whisky – A Blend	D	-	-	X	
	I	X	-	-	
Blended Rye Malt Whisky Or Rye Malt Whisky – A Blend	D	-	-	X	
	I	X	-	-	
Blended Rye Whisky Or Rye Whisky – A Blend	D	-	-	X	
	I	X	-	-	
Blended Scotch Whisky Or Scotch Whisky – A Blend	D	-	-	-	PRODUCT OF SCOTLAND ONLY
	I	-	-	-	
Blended Wheat Whisky Or Wheat Whisky – A Blend	D	-	-	X	
	I	X	-	-	

PRODUCT	DOMESTIC (D) OR IMPORTED (I)	LABORATORY ANALYSIS	PRE-IMPORT LETTER	FORMULA (TTB F 5100.51 or TTB F 5110.38)	COMMENT
Blended Whisky Or Whisky – A Blend	D	-	-	X	
	I	X	-	-	
Bourbon Cordial/Bourbon Liqueur	D	-	-	X	PRODUCT OF U.S. ONLY
	I	-	-	-	
Bourbon Whisky	D	-	-	-	PRODUCT OF U.S. ONLY
	I	-	-	-	
Brandy (Grape Only)	D	-	-	X*	*If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	-	-	-	
Brandy Alexander	D	-	-	X	
	I	-	X	-	
Brandy Cordial/ Brandy Liqueur	D	-	-	X	
	I	-	X	-	
Calvados					*PRODUCT OF FRANCE ONLY; however, harmless coloring/flavoring/ blending materials may be added in the U.S. If harmless coloring/ flavoring/blending materials are added in the U.S., a formula is required.
	D	-	-	X*	
Canadian Whisky	D	-	-	-	PRODUCT OF CANADA ONLY
	I	-	-	-	
Cognac					*PRODUCT OF FRANCE ONLY; however, sugar, caramel and/or oak chip infusion may be added in the U.S. If sugar, caramel and/or oak chip infusion are added in the U.S., a formula is required.
	D	-	-	X*	
Cordial	D	-	-	X	
	I	-	X	-	
Corn Whisky	D	-	-	X*	*If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	X	-	-	
Crème De _____	D	-	-	X	
	I	-	X	-	
Curacao	D	-	-	X	
	I	-	X	-	
Distilled Spirits Specialty (Product requiring a statement of composition)	D	-	-	X	
	I	-	X	-	
Dried Fruit Brandy (e.g., "Raisin Brandy")	D	-	-	X*	*If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	X	-	-	
Egg Nog	D	-	-	X	
	I	-	X	-	

PRODUCT	DOMESTIC (D) OR IMPORTED (I)	LABORATORY ANALYSIS	PRE-IMPORT LETTER	FORMULA (TTB F 5100.51 or TTB F 5110.38)	COMMENT
Flavored Brandy	D	-	-	X	
	I	X	-	-	
Flavored Gin	D	-	-	X	
	I	X	-	-	
Flavored Rum	D	-	-	X	
	I	X	-	-	
Flavored Vodka	D	-	-	X	
	I	X	-	-	
Flavored Whisky	D	-	-	X	
	I	X	-	-	
Fruit Brandy (Other Than Grape, e.g., "Pear Brandy")	D	-	-	X*	*If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	X	-	-	
Gin - Compound	D	-	-	X	
	I	-	X	-	
Gin - Distilled	D	-	-	-	
	I	-	X	-	
Gin - Redistilled	D	-	-	X	
	I	-	X	-	
Gin Cordial/Gin Liqueur	D	-	-	X	
	I	-	X	-	
Goldwasser	D	-	-	X	
	I	-	X	-	
Grain Spirits	D	-	-	-	
	I	-	-	-	
Grappa/Grappa Brandy	D	-	-	X*	*If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	X	-	-	
Imitation Distilled Spirits	D	-	-	X	
	I	X	-	-	
Immature Brandy (Grape Only)	D	-	-	X*	*If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	-	-	-	
Irish Whisky	D	-	-	-	PRODUCT OF THE REPUBLIC OF IRELAND OR NORTHERN IRELAND ONLY
	I	-	-	-	
Kirschwasser	D	-	-	X	
	I	X	-	-	
Kummel	D	-	-	X	
	I	-	X	-	
Lees Brandy (Any Kind)	D	-	-	X*	*If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	X	-	-	

PRODUCT	DOMESTIC (D) OR IMPORTED (I)	LABORATORY ANALYSIS	PRE-IMPORT LETTER	FORMULA (TTB F 5100.51 or TTB F 5110.38)	COMMENT
Light Whisky	D	-	-	X*	PRODUCT OF U.S. ONLY *If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	-	-	-	
Liqueur	D	-	-	X	
	I	-	X	-	
Malt Whisky	D	-	-	X*	*If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	X	-	-	
Marc Brandy (Any Kind)	D	-	-	X*	*If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	X	-	-	
Mescal/Mezcal	D	-	-	-	PRODUCT OF MEXICO ONLY
	I	-	-	-	
Neutral Brandy (Any Kind)	D	-	-	X*	*If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	X	-	-	
Neutral Spirits	D	-	-	-	
	I	-	-	-	
Ouzo	D	-	-	X	
	I	-	X	-	
Peppermint Schnapps	D	-	-	X	
	I	-	X	-	
Pisco	D	-	-	X*	*If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	-	-	-	
Pisco Sour	D	-	-	X	
	I	-	X	-	
Pomace Brandy (Any Kind)	D	-	-	X*	*If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	X	-	-	
Powdered Distilled Spirits	D	-	-	X	
	I	X	-	-	
Raki	D	-	-	X	
	I	-	X	-	
Recognized Cocktails	D	-	-	X*	*The product must appear in an industry recognized bartending guide such as "Mr. Bostons"®
	I	-	X*	-	
Residue Brandy (Any Kind)	D	-	-	X*	*If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	X	-	-	
Rock And Bourbon	D	-	-	X	PRODUCT OF U.S. ONLY
	I	-	-	-	
Rock And Brandy	D	-	-	X	
	I	-	X	-	

PRODUCT	DOMESTIC (D) OR IMPORTED (I)	LABORATORY ANALYSIS	PRE-IMPORT LETTER	FORMULA (TTB F 5100.51 or TTB F 5110.38)	COMMENT
Rock And Rum	D	-	-	X	
	I	-	X	-	
Rock And Rye	D	-	-	X	
	I	-	X	-	
Rum	D	-	-	X*	*If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	-	-	-	
Rum Cordial/Rum Liqueur	D	-	-	X	
	I	-	X	-	
Rye Cordial/Rye Liqueur	D	-	-	X	
	I	-	X	-	
Rye Malt Whisky	D	-	-	X*	*If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	X	-	-	
Rye Whisky	D	-	-	X*	*If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	X	-	-	
Sambuca	D	-	-	X	
	I	-	X	-	
Scotch Whisky	D	-	-	-	PRODUCT OF SCOTLAND ONLY
	I	-	-	-	
Slivovitz	D	-	-	X*	*If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	X	-	-	
Sloe Gin	D	-	-	X	
	I	-	X	-	
Spirit Whisky	D	-	-	X	
	I	X	-	-	
Straight Bourbon Whisky	D	-	-	-	PRODUCT OF U.S. ONLY
	I	-	-	-	
Straight Corn Whisky	D	-	-	-	
	I	X	-	-	
Straight Malt Whisky	D	-	-	-	
	I	X	-	-	
Straight Rye Malt Whisky	D	-	-	-	
	I	X	-	-	
Straight Rye Whisky	D	-	-	-	
	I	X	-	-	
Straight Whisky	D	-	-	-	
	I	X	-	-	
Substandard Brandy	D	-	-	X	
	I	X	-	-	
Tequila	D	-	-	-	PRODUCT OF MEXICO ONLY
	I	-	-	-	
Triple Sec	D	-	-	X	
	I	-	X	-	

PRODUCT	DOMESTIC (D) OR IMPORTED (I)	LABORATORY ANALYSIS	PRE-IMPORT LETTER	FORMULA (TTB F 5100.51 or TTB F 5110.38)	COMMENT
Vodka	D	-	-	X*	*If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	X	-	-	
Wheat Whisky	D	-	-	X*	*If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	X	-	-	
Whisky	D	-	-	X	
	I	X	-	-	
Whisky Distilled From Bourbon Mash	D	-	-	X*	PRODUCT OF U.S. ONLY *If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	-	-	-	
Whisky Distilled From Malt Mash	D	-	-	X*	PRODUCT OF U.S. ONLY *If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	-	-	-	
Whisky Distilled From Rye Malt Mash	D	-	-	X*	PRODUCT OF U.S. ONLY *If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	-	-	-	
Whisky Distilled From Rye Mash	D	-	-	X*	PRODUCT OF U.S. ONLY *If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	-	-	-	
Whisky Distilled From Wheat Mash	D	-	-	X*	PRODUCT OF U.S. ONLY *If harmless coloring/ flavoring/blending materials are added, a formula is required.
	I	-	-	-	



# COLAs Online

## eApplication Statuses in COLAs Online

You may view the status of your eApplications in COLAs Online through the Home: My eApplications page. You may also view the status of your eApplications through the Search Results: eApplications page by performing a Search for eApplications. There is a description of the eApplication statuses provided at the end of this document.

Home: My eApplications

The Home: My eApplications page is your home page and displays the list of your most recent 300 e-filed applications (submitted or saved but not submitted). The eApplications initially display in descending order by Status Date, regardless of status, but may be sorted by selecting the column headings. Figure 1 details the Home: My eApplications page.

**Figure 1: Home: My eApplications**

The screenshot shows the 'COLAs Online' web application interface. At the top, there is a navigation menu with links: 'Formulas Online', 'Home: My eApplications', 'Create an eApplication', 'Search for eApplications', 'My Profile', 'Contact Us', 'Instructions', and 'Log Off'. Below the navigation, a welcome message is displayed for 'JANE SMITH'. A 'My eApplications' section contains a 'Create an eApplication' button and a note about application visibility. A table titled 'Printable Version' lists three applications. The 'Status' column in the table is circled in red. At the bottom, there is a search bar and a footer with the Alcohol and Tobacco Tax and Trade Bureau logo and contact information.

TTB ID	Permit No.	Brand Name	Enciful Name	Serial No.	Status Date	Status
12164001000002	BWN-MA-5555	POM BRAND		123456	06/12/2012	RECEIVED
12164001000002	BR-ME-SUN-111	POM		123456	06/12/2012	RECEIVED
12158001000002	BWN-MA-5555	POM WINES		121234	06/06/2012	CORRECTED



## eApplication Statuses in COLAs Online

### View Statuses in My eApplications

Follow these steps to view your list of e-filed applications and their statuses:

1. Select the [Home: My eApplications](#) link from the menu box on any page. The Home: My eApplications page displays. See Figure 1.
2. To sort the list of e-filed applications, click on one of the column headings.

► **Note:** You can sort the list by any column heading.

3. To view more e-filed applications, select the [Next](#) link.

► **Note:** Each page displays 20 applications.

The [statuses](#) display next to the eApplications in the Status column.

### Search for eApplications

The Search for eApplications page allows you to search for your e-filed COLAs. Figure 2 and Figure 3 detail the Search for eApplications page.

Figure 2: Search for eApplications (Top)

The screenshot shows the top portion of the COLAs Online search page. At the top, there is a header for the Alcohol and Tobacco Tax and Trade Bureau, U.S. Department of the Treasury. Below this is the 'COLAs Online' logo and a navigation menu with links: Formulas Online, Home: My eApplications, Create an eApplication, Search for eApplications, My Profile, Contact Us, Instructions, and Log Off. The main heading is 'Search for eApplications'. Underneath, there are search criteria fields: 'Submitted By' (set to JSCFMEXT), 'Date Submitted' (From and To date pickers), 'Date Status Last Updated' (From and To date pickers), 'TTB ID', and 'Serial #'. A note specifies that searches by permit number only return data from 04/26/2003 forward. A list of permit numbers is provided with checkboxes: BR-ME-SUN-111: POM RIVER BREWING COMPANY, BWN-MA-5555: POM WINERY, LLC, DSP-ME-222: POM ROCK DISTILLERIES, INC., PR-S-333: POM & CO. INC., and VA-I-6666: POM MARKETING GROUP.

## eApplication Statuses in COLAs Online

Figure 3: Search for eApplications (Bottom)

The screenshot shows a search form for eApplications. The form includes several sections:

- Product Name:** Radio buttons for Brand Name, Fanciful Name, and Either.
- Type of Application:** Checkboxes for Certificate of Label Approval and Certificate of Exemption.
- Type of Product:** Checkboxes for Wine, Distilled Spirits, and Malt Beverage.
- Source of Product:** Checkboxes for Domestic and Imported.
- Type of Submission:** Checkboxes for Resubmission After Rejection and Distinctive Bottling (with a sub-option for Distinctive Liquor Bottle Approval).
- Representative ID:** A text input field.
- COLA Status:** A dropdown menu currently showing "--Select Status--".


At the bottom of the form are three buttons: "Clear and Start Over", "Back to My eApplications", and "Search". Below the form is a footer containing the TTB logo, a disclaimer, and a warning about system monitoring.

Follow these steps to begin searching:


1. Select the [Search for eApplications](#) link from the main menu on any page. The Search for eApplication page displays. See Figure 1 and Figure 2.
2. Select the Submitted By radio button to include either those submitted only by you or to include all others with the same signing authority.

► **Note:** Enter one or more fields of search criteria.

3. Enter Date Submitted Range (From Date and To Date).

► **Note:** The format is MM/DD/YYYY. Select the  icon to display a pop-up calendar to find the correct date.

4. Enter Date Status Last Updated Range (Last Updated From Date and To Date).

► **Note:** The format is MM/DD/YYYY. Select the  icon to display a pop-up calendar to find the correct date.

5. Enter a TTB ID.

### eApplication Statuses in COLAs Online

6. Enter a Serial #.
7. Select the Plant Registry/Basic Permit/Brewer's No. value(s) in the list provided.
8. Enter the Product Name.
9. Select the Brand Name, Fanciful Name or Either radio option. Enter name text.
10. Select the Type of Application.  
**►Note:** Select all that apply.
11. Select the Type of Product for the search.  
**►Note:** Select all that apply.  
**►Note:** If Type of Product is "Wine," then the Grape Varietal(s) field displays as a search criterion.
12. Select Source of Product
13. Select Type of Submission.
14. Select Distinctive Liquor Bottle.
15. Enter the Representative ID in the field provided.
16. Select the COLA Status from the drop-down list provided.
17. Select the **Search** button to view your search results. The Search Results: eApplications page displays with the records that match your search criteria. See [Search Results: eApplications](#).
18. Select the **Clear and Start Over** button to reset all data fields to perform a new search.
19. Select the **Back to My eApplications** button to return to the home page.  
**►Note:** To perform a wildcard search, enter a "%" at the beginning or end of the search criteria value.  
**►Note:** Search results are limited to a maximum of 500 items.  
**►Note:** You cannot search for paper filed COLA applications from within COLAs Online. To check on the status of a paper filed application, call ALFD Customer Service at 866-927-2533.

## eApplication Statuses in COLAs Online

View Statuses in Search Results: eApplications

The Search Results: eApplications page provides detailed results information on e-filed COLA applications based on search criteria. Figure 4 details the Search Results: eApplications page.

Figure 4: Search Results: eApplications

**COLAs Online**  
ALCOHOL AND TOBACCO TAX AND TRADE BUREAU

TTB F 5100.31: Application For and Certification/Exemption of Label/Bottle Approval

- Formular Online
- Home: My eApplications
- Create an eApplication
- Search for eApplications
- My Profile
- Contact Us
- Instructions
- Log Off

**Search Results: eApplications**

Printable Version

TTB ID	Permit No.	Brand Name	Fanciful Name	Serial No.	Status Date	Status
10204001000003	DSP-ME-222	POM DISTILLERS		101234	07/26/2010	REJECTED
10204001000001	DSP-ME-222	POM DISTILLERS		101234	07/23/2010	WITHDRAWN

1 to 2 of 2 (Total Matching Records: 2)

New Search      Back to My eApplications

Alcohol and Tobacco Tax and Trade Bureau, 2003. Contact us at: [webmaster@ttd.treas.gov](mailto:webmaster@ttd.treas.gov)

DEPARTMENT OF THE TREASURY

While the Alcohol and Tobacco Tax and Trade Bureau (TTB) makes every effort to provide complete information, data such as company names, addresses, permit numbers, and other data provided in the registry may change over time. TTB makes no warranty, expressed or implied, and assumes no legal liability or responsibility as to the accuracy, reliability or completeness of furnished data. Label images contained within the Public COLA Registry may appear differently, with respect to type size, contrast, per inch and contrasting background, than actual labels on the container. We also remind users of the Public COLA Registry that section V of the instructions for the TTB COLA form 5100.31, Allowable Revisions to Approved Labels, identifies various types of label information that may be changed by the COLA holder without the need for re-approval. TTB welcomes suggestions on how to improve our Public COLA Registry. Please contact us via email at [altd@ttd.gov](mailto:altd@ttd.gov).

If you have difficulty accessing any information in the site due to a disability, please contact us via email ([webmaster@ttd.treas.gov](mailto:webmaster@ttd.treas.gov)) and we will do our best to make the information available to you.

This site is best viewed at 800x600 screen resolution or higher using Internet Explorer 7.0. If you are using Internet Explorer 8.0, click [here](#) for more information on browser compatibility.

WARNING: THIS SYSTEM IS THE PROPERTY OF THE UNITED STATES DEPARTMENT OF TREASURY. UNAUTHORIZED USE OF THIS SYSTEM IS STRICTLY PROHIBITED AND SUBJECT TO CRIMINAL AND CIVIL PENALTIES. THE DEPARTMENT MAY MONITOR, RECORD, AND AUDIT ANY ACTIVITY ON THE SYSTEM AND SEARCH AND RETRIEVE ANY INFORMATION STORED WITHIN THE SYSTEM. BY ACCESSING AND USING THIS COMPUTER YOU ARE AGREEING TO ABIDE BY THE TTB RULES OF BEHAVIOR, AND ARE CONSENTING TO SUCH MONITORING, RECORDING, AND INFORMATION RETRIEVAL FOR LAW ENFORCEMENT AND OTHER PURPOSES. USERS SHOULD HAVE NO EXPECTATION

Follow these steps to view the search results of your e-filed applications and their statuses:

1. Select the [Search for eApplications](#) link from the menu box on any page.
2. Enter search criteria.
3. Select the **Search** button. The search results based on the value entered display. See Figure 3.

► **Note:** Search results are limited to a maximum of 500 items.

4. To sort the search results, click on any column heading.
5. To view more search results, select the [Next](#) link.

The [statuses](#) display next to the eApplications in the Status column.

## eApplication Statuses in COLAs Online

### eApplication Statuses

The following available statuses display next to the eApplications in the Status column:

- **Approved** – This status indicates a final action regarding a particular application. Applications enter this status when both the application and the labels meet all applicable requirements. At this point an application becomes a Certificate. This status authorizes the Certificate holder to either bottle or remove from Customs custody alcohol beverages that bear labels identical to those shown on the Certificate.
- **Assigned** – Applications enter this status when they are assigned to a specialist and the internal evaluation begins.
- **Corrected** – Applications change from “Needs Correction” to “Corrected” after the applicant makes the required revisions and resubmits the application back to TTB for review. Once the review process starts the status changes to “Assigned,” once again until the internal evaluation is complete.
- **Expired** – While generally “Approved” Certificates never expire, under certain limited conditions Certificates are given an expiration date by TTB at the time of approval. The status of an “Approved” Certificates changes to “Expired” when the expiration date is reached.
- **Needs Correction** – Applications in this status have been reviewed by TTB but cannot be approved as submitted. The application is returned to the submitter with a list of corrections that need to be made to either the application or to the label itself. The submitter has 30 days to make the corrections. If the application is not returned to TTB within 30 days from the date the application is returned then the status changes to “Rejected.” If the submitter makes the corrections and resubmits the application to TTB within 30 days, the status changes to “Corrected.” Applications in the “Needs Correction” status may also be “Withdrawn” by the applicant.
- **Received** – Applications enter this status when they are received by TTB and remain in this status until internal evaluation begins. Once the evaluation process starts the status changes to “Assigned,” until the internal evaluation is complete.
- **Rejected** – This status indicates a final TTB action regarding a particular application. Paper applications enter this status when initial TTB review discloses that either the application or the label does not comply with Federal requirements. Electronic applications are generally returned for correction rather than rejected; however, an electronic application may be rejected if all the necessary corrections are not made to an application that was returned for correction. Electronic applications that have been returned for correction enter this status if the application is not resubmitted to TTB within 30 days. A rejection does not restrict the ability to resubmit a new application with corrected labels at a later date.
- **Revoked** – “Approved” Certificates will change to this status when TTB rescinds approval because either the labeling laws or regulations have changed rendering the Certificate invalid or the Certificate was approved by TTB in error.
- **Saved not submitted** – An application in this status has been either completely or partially created, but has not yet been submitted to TTB for review. TTB cannot view applications in this status. An application may only remain in this status for up to 30

### eApplication Statuses in COLAs Online

days. After 30 days in this status the application is automatically deleted. If the application is submitted, the status changes to "Received."

- **Surrendered** – "Approved" Certificates will change to this status when the Certificate holder voluntarily communicates to TTB that they no longer need the Certificate. Generally "Approved" Certificates do not expire, however, TTB encourages all industry members to surrender obsolete Certificates either by written communication for paper filed applications or electronically if applications were e-filed.
- **Withdrawn** – This status indicates that the applicant withdrew the application before TTB took final action. A withdrawal does not restrict the ability to resubmit a new application at a later date.

FOR TTB USE ONLY				DEPARTMENT OF THE TREASURY ALCOHOL AND TOBACCO TAX AND TRADE BUREAU APPLICATION FOR AND CERTIFICATION/EXEMPTION OF LABEL/BOTTLE APPROVAL <i>(See Instructions and Paperwork Reduction Act Notice Below)</i>							
TTB ID				<b>PART I - APPLICATION</b> 8. NAME AND ADDRESS OF APPLICANT AS SHOWN ON PLANT REGISTRY, BASIC PERMIT, OR BREWER'S NOTICE. INCLUDE APPROVED DBA OR TRADENAME IF USED ON THE LABEL <i>(Required)</i>  8a. MAILING ADDRESS, IF DIFFERENT							
1. REP. ID. NO. <i>(If any)</i>		CT	OR								
2. PLANT REGISTRY/BASIC PERMIT/BREWER'S NO. <i>(Required)</i>		3. SOURCE OF PRODUCT <i>(Required)</i> <input type="checkbox"/> Domestic <input type="checkbox"/> Imported									
4. SERIAL NUMBER <i>(Required)</i>		5. TYPE OF PRODUCT <i>(Required)</i> <input type="checkbox"/> WINE <input type="checkbox"/> DISTILLED SPIRITS <input type="checkbox"/> MALT BEVERAGES									
6. BRAND NAME <i>(Required)</i>		7. FANCIFUL NAME <i>(If any)</i>									
9. E-MAIL ADDRESS		10. GRAPE VARIETAL(S) <i>Wine only</i>						11. FORMULA		18. TYPE OF APPLICATION <i>(Check applicable box(es))</i> a. <input type="checkbox"/> CERTIFICATE OF LABEL APPROVAL b. <input type="checkbox"/> CERTIFICATE OF EXEMPTION FROM LABEL APPROVAL <i>"For sale in _____ only" (Fill in State abbreviation)</i> c. <input type="checkbox"/> DISTINCTIVE LIQUOR BOTTLE APPROVAL. TOTAL BOTTLE CAPACITY BEFORE CLOSURE _____ <i>(Fill in amount)</i> d. <input type="checkbox"/> RESUBMISSION AFTER REJECTION TTB ID _____	
12. NET CONTENTS		13. ALCOHOL CONTENT						14. WINE APPELLATION <i>(If on label)</i>			
15. WINE VINTAGE DATE <i>(If on label)</i>		16. PHONE NUMBER						17. FAX NUMBER			
19. SHOW ANY INFORMATION THAT IS BLOWN, BRANDED, OR EMBOSSED ON THE CONTAINER (e.g., net contents) ONLY IF IT DOES NOT APPEAR ON THE LABELS AFFIXED BELOW. ALSO, SHOW TRANSLATIONS OF FOREIGN LANGUAGE TEXT APPEARING ON LABELS.											
PART II - APPLICANT'S CERTIFICATION											
Under the penalties of perjury, I declare: that all statements appearing on this application are true and correct to the best of my knowledge and belief; and, that the representations on the labels attached to this form, including supplemental documents, truly and correctly represent the content of the containers to which these labels will be applied. I also certify that I have read, understood, and complied with the conditions and instructions which are attached to an original TTB F 5100.31, Certificate/Exemption of Label/Bottle Approval. I consent to the return of processed applications in the manner indicated on this application and set forth in the applicable instructions.											
20. DATE OF APPLICATION		21. SIGNATURE OF APPLICANT OR AUTHORIZED AGENT			22. PRINT NAME OF APPLICANT OR AUTHORIZED AGENT						
PART III - TTB CERTIFICATE											
This certificate is issued subject to applicable laws, regulations, and conditions as set forth in the instructions portion of this form.											
23. DATE ISSUED		24. AUTHORIZED SIGNATURE, ALCOHOL AND TOBACCO TAX AND TRADE BUREAU									
FOR TTB USE ONLY											
QUALIFICATIONS											
							EXPIRATION DATE <i>(if any)</i>				

AFFIX COMPLETE SET OF LABELS BELOW *(See General Instructions 4 and 6)*

## I. PURPOSE OF THIS CERTIFICATE

This certificate authorizes you to bottle and remove the product identified on the certificate from the plant(s) identified on the certificate where it was bottled or packed, or to remove products in containers from Customs custody. NOTE: This certificate does not constitute trademark protection.

## II. CONDITIONS OF THIS CERTIFICATE

- A. This certificate does not relieve you from liability for violations of the Federal Alcohol Administration Act, the Alcoholic Beverage Labeling Act of 1988, the Internal Revenue Code of 1986, or related regulations and rulings.
- B. You must ensure that: 1) all the information on your application is true and correct and 2) any and all information (including words, text, illustrations, graphics, etc.) shown or presented on the label(s) affixed to this certificate is truthful, accurate and not misleading.
- C. The Alcohol and Tobacco Tax and Trade Bureau (TTB) does not routinely review submitted labels for compliance with applicable requirements for mandatory label information regarding type size, characters per inch or contrasting background. You must ensure that the mandatory information on the actual labels is legible and displayed in the correct type size, number of characters per inch, and on a contrasting background in accordance with the TTB labeling regulations, 27 CFR parts 4, 5, 7, and 16, as applicable. TTB does reserve the right to review applications for compliance with these requirements and to return non-compliant applications.

## III. INSTRUCTIONS FOR COMPLETING AND SUBMITTING THIS APPLICATION

NOTE: Applications may be filed electronically by accessing the TTB website at <https://www.ttbonline.gov/colasonline/>.

### A. GENERAL INSTRUCTIONS

1. You must print or type your application and sign it in ink. Submit your application in duplicate to the ADVERTISING, LABELING AND FORMULATION DIVISION, ALCOHOL AND TOBACCO TAX AND TRADE BUREAU, 1310 G STREET N.W., BOX 12, WASHINGTON, DC 20005. (paper filers only)
2. You may use exact copies of TTB F 5100.31 in lieu of an original form. Copies do not have to include the instruction page; however, you remain subject to all the provisions and instructions outlined on the form. We suggest that you use an original form whenever possible. See Section IV for how to obtain a supply of forms. (paper filers only)
3. Generally, the person, firm, or corporation who will bottle or pack the product must file the application. However, for a product to be imported in containers intended for sale at retail, the application must be filed by the importer. In the case of a product to be relabeled by a wholesaler, the application must be filed by the wholesaler.
4. You must firmly affix (with glue or tape - DO NOT STAPLE) all labels that will appear on the container. Printer's proofs and photocopies are acceptable. If labels are in the form of can flats, photocopies are requested. (paper filers only)
5. You may NOT make pen and ink changes, write out information, type over or cross out information, or paste information over labels affixed to this application. (Paper filers only)
6. You must reduce oversized labels so that they fit in the space provided. You must indicate in Item 19 that labels have been reduced and the percentage of reduction.

### B. SPECIFIC INSTRUCTIONS

- ITEM 1. Include a third party representative ID Number if your application will be submitted by a third party representative, and if you consent to the disclosure of information about the application to this representative, as well as the return of the processed application to this representative. Third party filers who do not already have a Representative ID Number, please contact TTB to obtain one. (See section IV for contact information)
- ITEM 2. For bonded wine cellars, taxpaid wine bottling houses, and distilled spirits plants, enter the applicable registry number (BW- or TPWBH- or DSP- number). Importers must enter the TTB basic permit number and brewers must enter the brewer's notice number. Wholesalers applying to relabel must enter the wholesaler's basic permit number. If you intend to bottle this product at more than one of your locations (distilled spirits and malt beverages only), show the registry number/brewer's notice number of each location where the product will be bottled. In this instance, Item 8 should reflect your principal place of business. You may also use Item 8a to reflect additional registry/brewer's notice numbers if the space provided in item 2 is insufficient. In this instance, cross out the words "Mailing Address, if different."
- ITEM 3. Indicate the source of the product by checking the appropriate box.
- ITEM 4. You must assign a sequential serial number beginning with the last two digits of the current calendar year to each application and its duplicate, not to exceed 6 characters; e.g., 12-1, 12-2, etc.
- ITEM 5. Indicate the type of product by checking the appropriate box. For Sake, check the "wine" box.
- ITEM 6. A brand name is the name under which the product is sold. If the product is not sold under a brand name, enter the name of the bottler, packer, or importer, as applicable.
- ITEM 7. A fanciful name is a name that further identifies the product and is required for some specialty products. It is optional for other products.
- ITEM 8. Indicate your company name and address exactly as they appear on your plant registry, basic permit, or brewer's notice (include your approved DBA or trade name if you use it on the label). In the case of distilled spirits and malt beverages that are bottled at more than one location indicate your principal place of business address in this field.
- ITEM 8a. You may enter a mailing address here if you receive mail at an address other than the address shown in Item 8.
- ITEM 9. You may provide the e-mail address of the person who should receive TTB's response to this application. TTB will process and return all paper applications to this e-mail address if one is provided.
- ITEM 10. You must list in this block each grape varietal (if any) that appears on wine labels.
- ITEM 11. The term "Formula" encompasses the following pre-COLA product evaluations: domestic beverage alcohol formulas, pre-import approval letters, lab analyses, and submissions formerly known as statements of process (SOPs). A formula is a quantitative list of ingredients and a step-by-step method of manufacture for alcohol beverages (wine, distilled spirits, and malt beverages) requiring approval from TTB prior to production or importation as set out in Industry Circular 2007-4. TTB's regulatory authority for such products may also be found in 27 CFR parts 4, 5, 7, 19, 24, 25, and 26. Please visit [http://www.ttb.gov/formulation/pre\\_cola.shtml](http://www.ttb.gov/formulation/pre_cola.shtml) for more information about when a formula is required. For any domestic or imported alcohol beverage product requiring formula approval, specify the TTB Formula ID/TTB ID number, or TTB lab number. A copy of the approved formula or pre-import approval letter must accompany this label application. If the formula approval was obtained electronically through Formulas Online, the system-generated TTB Formula ID number must be provided.
- ITEM 12. Indicate the container size(s) (net contents) covered by label(s) affixed to the application. You may indicate a range of sizes. You are not required to obtain separate certificates for each size container on which a label or set of labels will be used.
- ITEM 13. Enter the alcohol content stated on the label.
- ITEM 14. Fill in only if a wine appellation of origin is stated on the label.
- ITEM 15. Fill in only if the wine vintage date is stated on the label.
- ITEM 16. Provide the phone number of the person responsible for the application.
- ITEM 17. Provide the fax number of the person responsible for the application.
- ITEM 18. You must check "a" OR "b." You must also check "c" if you intend to bottle distilled spirits in a distinctive container. You must check "d" and enter the TTB ID number as shown in the upper left hand corner of the rejected application if you are submitting an application that was previously rejected. If you check "b": 1) you may only sell this product in the State where it is bottled AND 2) the statement "For sale in \_\_\_\_\_ only" (using State abbreviation) must appear on each container. We do not issue certificates of exemption for products imported in bottles or for malt beverages.
- ITEM 19. The instructions for this item are on the front of the form.
- ITEM 20. Enter date application is prepared or submitted.
- ITEM 21. The applicant or authorized agent must sign in this block.
- ITEM 22. The signer's name must be printed in this block.

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IV. CONTACT INFORMATION

**For Additional Information Contact:**  
 Advertising, Labeling and Formulation Division (ALFD)  
 Alcohol and Tobacco Tax and Trade Bureau  
 1310 G. Street, N.W., Box 12  
 Washington, DC 20005  
 Phone (202) 453-2250  
 1-866-927-2533 (Toll Free)  
 E-mail address: alfd@ttb.gov

**For A Supply Of This Form (TTB F 5100.31) Contact:**  
 The form may be ordered electronically by accessing the TTB Web site at  
[http://www.ttb.gov/forms/ordering\\_forms.shtml](http://www.ttb.gov/forms/ordering_forms.shtml)  
 The form may be electronically accessed at the TTB Web site at  
<http://www.ttb.gov/forms/f510031.pdf>

V. ALLOWABLE REVISIONS TO APPROVED LABELS

Once a label receives TTB approval, you are permitted to make certain changes to that label without submitting it to TTB. The label(s) identified on and affixed to this certificate may be revised without resubmission as follows:

NOTE: Any revision(s) you make to your approved label(s) must be in compliance with the applicable regulations in 27 CFR parts 4, 5, 7, and 16, and any other applicable provision of law or regulation, including, but not limited to, the conditions set forth in the "Comments" below.

YOU MAY...	REVISION APPLIES TO			COMMENTS
	WINE	DISTILLED SPIRITS	MALT BEVERAGE	
1. Delete any non-mandatory label information, including text, illustrations, graphics, etc.	YES	YES	YES	If the non-mandatory information in question relates to other information that remains on the label, it is your responsibility to ensure that the remaining information is not misleading after the deletion.
2. Reposition any label information, including text, illustrations, graphics, etc.	YES	YES	YES	The repositioning must comply with any placement requirements applicable to mandatory information. For example, some types of mandatory information must appear on the brand label or must appear together with other label information.
3. Change the color(s) (background and text), shape and proportionate size of labels. Change the type size and font, and make appropriate changes to the spelling (including punctuation marks, changing letters from upper case to lower case and vice versa, and abbreviations) of words, in compliance with the regulations. Change from an adhesive label to one where label information is etched, painted or printed directly on the container and vice versa.	YES	YES	YES	All mandatory information must be readily legible and appear on a contrasting background. If you received approval for a single label then you may not divide the label into multiple labels without re-approval. All changes must comply with applicable regulations, and changes in spelling (including punctuation marks and abbreviations) must not change the meaning of the previously approved information.
4. Change the stated percentages for blends of grape varieties and appellations of origin for wine labels.	YES	N/A	N/A	When used for any of these items, the total percentages for each element must equal 100%. You may not change the name of the stated varieties or appellations without submitting a new application.
5. Add, change or delete a vintage date for wine labels.	YES	N/A	N/A	If the vintage date is deleted, no reference to "Vintage" may be made on any label or other materials (e.g., caps, capsules, corks, etc.) affixed to the bottle. When adding a new vintage date, you must comply with all applicable regulations, including the requirements regarding appellations of origin.
6. Change the optional "produced" or "made" by statements on wine labels to "blended," "vinted," "cellared" or "prepared" by statements.	YES	N/A	N/A	
7. Add, change or delete the stated amount of acid and/or the pH level for wine labels.	YES	N/A	N/A	
8. Change the stated amounts of sugar at harvest and/or residual sugar for wine labels.	YES	N/A	N/A	See ATF Ruling 82-4 for policy regarding use of sugar content statements and when such statements are required.
9. Add or delete bonded winery or taxpaid wine bottling house number for wine labels.	YES	N/A	N/A	If used, the number must appear in direct conjunction with the bottler's name and address.
10. Change the net contents statement.	YES	YES	YES	Revisions must comply with all applicable regulations governing net content statements and standards of fill. Please ensure that all applicable type size requirements are met for each container size.
11. Change the mandatory statement of alcohol content, as long as the change is consistent with the labeled class and type designation, and all other labeling statements.	YES	YES	YES (Flavored Malt Beverages Only)	For example, you may change the alcohol content of a grape wine labeled with a varietal designation from 13 percent to 15 percent alcohol by volume even though it results in a change to the product's tax classification. However, if the product was designated and labeled as a "table wine," an alcohol content of 15 percent alcohol by volume would be inconsistent with the rules for use of that designation, so this change would not be permitted. Similarly, a label bearing a "rum" designation may not be changed to state an alcohol content of less than 40 percent alcohol by volume. The revised alcohol content statement must be consistent with all other mandatory or optional labeling statements.
12. Add, delete, or change an optional statement of alcohol content for malt beverage labels.	N/A	N/A	YES	Malt beverages that contain alcohol derived from added flavors or other added nonbeverage ingredients (other than hops extract) containing alcohol are subject to mandatory alcohol content statement requirements.
13. Change the statement of percentage of neutral spirits and the name of the commodity from which a distilled spirit is produced.	N/A	YES	N/A	These changes must not result in a change to the class or type designation of the distilled spirits product.
14. Change the mandatory age statement, or delete or change an optional age statement for distilled spirits labels.	N/A	YES	N/A	These changes must not result in a change to the class or type designation. See 27 CFR 5.22 and 5.40 for further information about age statements and minimum aging requirements applicable to certain classes and types of spirits.
15. Delete or change an optional age statement, including a barrel aging statement, for wine and malt beverage labels.	YES	N/A	YES	Statements of age on wine labels must comply with 27 CFR 4.39(b).
16. Add, delete, or change statements or information in order to comply with the requirements of the State in which the malt beverage is to be sold.	N/A	N/A	YES	Applies only to malt beverages sold in that particular state (including the District of Columbia or the Commonwealth of Puerto Rico).
17. Add a new Serving Facts statement or statement of average analysis, add a Serving Facts statement to replace a statement of average analysis, or change the numerical values for calories, carbohydrates, protein, and fat contained in an existing statement.	YES	YES	YES	The statement must be in compliance with TTB Ruling 2013-2 and TTB Ruling 2004-1. A new Serving Facts statement is an allowable revision only if it is in one of the formats that is set forth in the examples attached to TTB Ruling 2013-2.
18. Add, delete, or change stated bottling date, production date (day, month, and/or year) or freshness information including bottling, production or expiration dates or codes.	YES	YES	YES	Bottling dates added to wine labels must comply with 27 CFR 4.39(c).
19. Change the name or trade name to reflect a different name already approved for use by the responsible bonded wine cellar, taxpaid wine bottling house, distilled spirits plant, brewery, or importer. Change the address where it is within the same State.	YES	YES	YES	This means that a bonded wine cellar, taxpaid wine bottling house, distilled spirits plant, brewery or importer may revise the label to include the use of a name or trade name that is already approved for that particular industry member. The name or trade name must appear on the basic permit, brewer's notice, or other qualifying documents for the company to whom the original certificate was issued. If the name or trade name is also used as the brand name on the label, resulting in a change of brand name, you must submit a new application. The change in address is ONLY allowed for in-state moves or other changes to the COLA holder's address that have already been reflected on the industry member's basic permit, brewer's notice, or other qualifying documents.
20. Add, delete, or change the name and/or address of the foreign producer, bottler, or shipper.	YES	YES	YES	The producer, bottler, or shipper must be located in the same country originally shown.
21. Add, delete, or change the name, address, and/or trademark of the wholesaler, retailer, or persons for whom the product is imported or bottled.	YES	YES	YES	

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22. Add, delete, or change bottle deposit information, or recycling information or logos.	YES	YES	YES	
23. Add, delete, or change UPC barcodes and/or 2D mobile barcodes, e.g., QR codes or Microsoft Tags.	YES	YES	YES	Addition or change of UPC Code must be in compliance with Industry Circular 77-23. Any information retrieved from 2D barcodes must be in compliance with all applicable advertising regulations.
24. Add, delete, or change a Web site address, phone number, fax number, or zip code.	YES	YES	YES	
25. Add, delete, or change a lot or batch identification number or other serial numbers.	YES	YES	YES	
26. Add, delete, or change trademark, copyright symbols (e.g., TM, ©, ®), kosher symbols, company logos, and/or social media icons.	YES	YES	YES	Symbols, logos and icons may not violate TTB regulations. Advertisements on social media sites must be in compliance with all applicable advertising regulations.
27. Add, delete, or change optional information about awards or medals, or the signature of the brewer, winemaker, or distiller of the product.	YES	YES	YES	
28. Add, delete, or change holiday- and/or seasonal-themed graphics, artwork and/or salutations.	YES	YES	YES	Holiday/seasonal-themed information or graphics must not conflict with or qualify the mandatory information and must comply with all applicable regulations, including the rules governing prohibited practices.
29. Delete or change promotional sponsorship-themed graphics, logos, artwork, dates, event locations and/or other sponsorship-related information. (Examples: sports leagues, team organizations, annual sporting events, and annual or semi-annual festivals.) Delete or change charitable endorsement information to include information about the proceeds.	YES	YES	YES	If authorization by a third party was required for use of such promotional sponsorship-themed information on a label when first approved, it is the responsibility of the industry member to have any necessary documentation of authorization to cover the revisions to the approved label(s). The labeling statements may not create a misleading impression.
30. Add, delete, or change a label or sticker that provides information about a rating or recognition provided by an organization (e.g., "Recognized as one of the top values in vodka by x Magazine" or "Rated as the best 2012 wine by x Association"), as long as the rating or recognition reflects simply the opinion of the organization and does not make a specific substantive claim about the product or its competitors.	YES	YES	YES	These statements or graphics must not conflict with or qualify any mandatory information and must comply with all applicable laws and regulations. Substantive claims about the product or its competitors are not covered by this exemption.
31. Delete all organic references from the label.	YES	YES	YES	If you choose to delete one organic claim on a label on which you have received approval to make organic claims, then all organic claims, references and certification statements must be deleted on the revised label. The deletion of individual references or certification statements is not permitted without a new COLA.
32. Change an approved sulfite statement to any of these options: *Contains Sulfites*, *Contains (s) Sulfiting Agent(s)*, *Contains [name of specific sulfiting agent]*, *Contains Naturally Occurring and Added Sulfites*, or *Contains Naturally Occurring Sulfites*.  *Sulphites* may be used in lieu of "Sulfites."	YES	YES	YES	A sulfite statement is required when sulfur dioxide or a sulfiting agent is detected at a level of 10 or more parts per million, measured as total sulfur dioxide. The statement used must accurately reflect all of the sulfur dioxide or sulfiting agent(s) present in the alcohol beverage. For wine: Any other variation of the statement or removal of the statement requires a lab analysis. For sulfite waivers, the proprietor must have proof of sample analysis from a TTB-certified laboratory or from the TTB Compliance Laboratory.
33. Add, delete, or change information about the number of bottles that were "made," "produced," "brewed," or "distilled" in a batch; respectively.	YES	YES	YES	Example: "100 bottles produced"
34. Add certain instructional statements to the label(s) about how best to consume or serve the product. Only the statements listed in the comments section may be added.	YES	YES	YES	Only the following statements are approved to be added to a label: "Refrigerate After Opening" "Do Not Store in Direct Sunlight", "Best If Frozen For ___ to ___ Hours", "Shake Well", "Pour Over Ice", "Best When Chilled", "Best Served Chilled", "Serve Chilled", "Serve at Room Temperature"

If you have questions about what is mandatory information and what is non-mandatory information, please consult the applicable regulations in 27 CFR parts 4, 5, 7 and 16, or contact TTB. See Section IV for how to contact TTB.

#### PAPERWORK REDUCTION ACT NOTICE

This request is in accordance with the Paperwork Reduction Act of 1995. We collect this information to verify your compliance with the Federal laws and regulations we administer for the labeling of alcohol beverages. The information is mandated by statute (27 U.S.C. 205) and is used to obtain a benefit.

We estimate 31 minutes as the average burden for you to complete this form depending on your individual circumstances. You may comment to us about the accuracy of this burden estimate and suggest ways for us to reduce the burden. Address your comments or suggestions to: Reports Management Officer, Regulations and Rulings Division, Alcohol and Tobacco Tax and Trade Bureau, 1310 G Street, NW, Box 12 Washington, DC 20005.

We may not conduct this collection of information, and you are not required to respond to this request, unless it displays a valid, current OMB control number.

#### DISCLOSURE STATEMENT

We require this information under the authority of 27 U.S.C. 205(e). You must disclose this information so we may verify your compliance with the Federal laws and regulations we administer for the labeling of alcohol beverages.

We use this information for the purposes described in the preceding paragraph. In addition, the information may be disclosed to other Federal, State, and local law enforcement and regulatory agency personnel to verify information on the application and to aid in the performance of their duties. The information may further be disclosed to the Justice Department if it appears that the furnishing of false information may contribute to a violation of Federal law. If you fail to supply complete information, then there will be a delay in the processing of your application.

After TTB issues a certificate of label approval, a certificate of exemption from label approval, or a distinctive liquor bottle approval, copies of the approved applications are made available for public inspection.

# **How the Tax Cuts and Jobs Act Impacts Craft Brewers**

**Submitted by Jeffrey C. O'Brien**



# **How the Tax Cuts and Jobs Act Impacts Craft Brewers**

**Submitted by Jeffrey C. O'Brien  
Chestnut Cambronne PA**

#### **A. Cash Basis Method for Accounting and Accounting for Inventories**

- Cash basis accounting is a method of recording accounting transactions for revenue and expenses only when the corresponding cash is received, or payments are made
- Allowed for tax purposes only for smaller entities and useful when:
  - For simpler accounting systems with accounting personnel who are not familiar with the more intricate accrual basis of accounting
  - Where there is no inventory to be tracked or valued
  - Where there is no need for an audit, as may be required by a lender
  - When the company is in the services business (which implies that there is no inventory)

#### **B. Cost of Equipment Write-Offs**

- Section 179 of the IRS tax code allows businesses to deduct the full purchase price of qualifying equipment/software from your gross income
- \$1,000,000 cap for 2018
- \$2,500,000 limit on total amount of equipment purchased for 2018
- Equipment must be used for business 50% of the time
- List of qualifying equipment:

[https://www.section179.org/property\\_that\\_qualifies\\_for\\_section\\_179/](https://www.section179.org/property_that_qualifies_for_section_179/)

#### **C. New Rules Regarding Expensing Budget Interest**

Under the current tax system, capital investments like buildings, vehicles and brewing equipment are treated as “depreciable assets” and as such are allowed to be deducted from income at increasing levels over a fixed term of five, seven or 39 years, according to depreciation schedules set by the IRS. In contrast, the new tax rules allow for immediate depreciation of capital assets for the first five years after their purchase. This would allow small businesses to receive a tax break on capital investments in the same year they are made rather than waiting to receive the tax benefits over several years. In addition, the final tax bill expands the cap on these deductions from \$500,000 to \$1,000,000. These provisions, like the pass-through rules, expire in 2025.

#### **D. Research and Development Credit Opportunities**

As of January 2016, eligible small businesses (\$50 million or less in gross receipts) may claim the credit against the AMT. This will benefit a significant number of closely held businesses and their shareholders who previously had to defer some or all use of their credit due to the AMT limitations. Additionally, certain small businesses (\$5 million or less in gross receipts) will have the ability to offset the credit-against-payroll tax liability (capped at \$250,000 for up to five years)

- **Technical in Nature:** Though the R&D credit is not just for scientists, its application is science-based. To qualify, research and development activity must rely on the principals of engineering, physics, biology or computer science.
- **Permitted Purpose:** Contrary to popular belief, R&D does not exclusively pertain to new products. Taxpayers can reap the benefits of R&D as long as they are working on projects undertaken for the development of a new or improved aspect of their business. Processes, functions, products, quality increases and substantial cost reductions all fall under the umbrella of permitted purposes.
- **Process of Experimentation:** Qualified research involves an element of trial and error. The venture's process of experimentation must be designed to evaluate alternatives to achieve a result where the potential to achieve that result is initially uncertain. Measures that are taken to produce a hypothesis and test it are noted by the IRS when deciphering which research and development activities are entitled to the R&D credit.

#### Examples of R&D:

- Adding new equipment pertaining to process improvement or new bottling/brewing equipment;
- Developing new or improved hopping techniques or varieties of hops;
- Developing new or improved yeast strains or fermentation processes;
- Developing new or improved bottling and canning processes;
- Developing new or improved bottle designs (including cans/crowns, etc.);
- Developing new or improved keg filling techniques, water recycling or waste management;
- Developing new or improved product formulations or improved ingredient mixing methods;
- Developing new or improved prototype batches or improved preservatives;
- Testing of new or improved designs to ensure shelf life or longevity; and
- Testing of product ingredient combinations relative to new flavors or enhancements.
- 

#### E. Excise Tax Rate Decrease

- Federal excise tax reduced to \$3.50/barrel from \$7/barrel on the first 60,000 barrels for domestic brewers producing less than 2 million barrels annually
- Reduced to 416/barrel from \$18/barrel on the first 6 million barrels for all other brewers and beer importers
- \$18/barrel rate for over 6 million remains
- Transfer of beer between bonded facilities now allowed without tax liability

#### **F. 20% Deduction for Certain Pass-Through Income**

- Income earned through entities such as sole proprietorships, LLCs, and partnerships entitled to a 20% deduction before income tax rates applies
- Includes:
  - Income from a sole proprietorship
  - Income from an LLC or S-corporation
  - Partnership income
  - Income from rental properties (Including income passed through from REITs)
  - Any S-corporation, partnership, or trust that owns an interest in another pass-through business.
- Cannot deduct wage income

#### **G. Converting to a C Corp**

Under the Act:

- The top federal rate for individuals is reduced from 39.6% to 37% tax on ordinary income such as wages, dividends that are not qualified dividends and short-term capital gains (gains on investment assets held for less than one year). This tax rate will return to 39.6% after 2025 unless the reduced rate is extended or made permanent by subsequent legislation.
- Net investment income continues to be taxed at 3.8%, which is in addition to the top rate of 37%, on any investment income for married couples with gross incomes over \$250,000 filing jointly and for individuals with gross incomes over \$200,000.

The federal corporate tax rate drops from 35% to 21%.

The drop in the corporate tax rate to 21%, together with the fact that C-Corps. can continue to deduct state and local taxes (SALT) beyond the \$10,000 cap for individuals, makes a conversion to a C Corp. look very attractive. However, companies should think



carefully before making any changes to their business structures that could be expensive to unwind. Some things to consider:

- If your company plans to distribute all profits as dividends of a C-Corp., the effective tax cost will be higher to investors than if the business is a pass-through.

Typically, dividends are taxed to an individual recipient at the qualified dividend rate of 20%, though there is usually no preferential tax rate at the state and local level. Dividends may also be subject to the 3.8% net investment income tax mentioned above. Taking into account only federal taxes, the effective double tax rate (combining the corporate and individual rates) is 39.8% on earnings distributed as dividends.

If a business does not make distributions to its owners and reinvests its profits (excluding salary and perks) then a C-Corp. structure may result in income tax savings. On the other hand, if the business distributes all of its profit out to its owners annually, then the double tax resulting from a C-Corp. structure will be disadvantageous. In between these extremes, the benefits of one structure over another can be determined mathematically.

Only a small group of businesses will derive enough upside from converting to a C-Corp. to offset the double tax hit that occurs from a distribution to shareholders. Such businesses will have the following attributes:

- Generate a large amount of income;
- Reinvest heavily in its business;
- Intend to keep cash within the business for some substantial amount of time; and
- Pay substantial state and local taxes (which remain deductible for C-Corps. but are capped for individuals).



**Entity Selection, Formation and Financing  
Difficulties Specific to Breweries and Distilleries**

**Submitted by Sarah B. Bennett and Jeffrey C. O'Brien**



**Entity Selection, Formation and Financing Difficulties**

**Submitted by Sarah B. Bennett and Jeffrey C. O'Brien  
Chestnut Cambronne PA**

**a. Title IV and Regulation A+:** Reg A+, which went into effect in June 2015, has been described as a mini-IPO or "IPO-Lite," in that it allows nearly any company with principal offices in the U.S. or Canada to use internet crowdfunding to raise up to \$50 million per year from any number of both accredited and non-accredited investors under a regulatory scheme that is far less burdensome than that of a traditional IPO. There is no prohibition on general solicitation, and offering companies are not required to independently verify the sophistication (income or net worth) of their investors. Corporations, limited liability companies, and limited partnerships can take advantage of Reg A+'s two-tiered offering scheme and can sell nearly all types of securities, including equity, debt, and debt securities convertible into equity securities. Furthermore, the securities issued in Reg A+ will be unrestricted and freely transferable. One of the most exciting changes for companies seeking to raise capital under Reg A+ is that Tier 2 offerings are not subject to state Blue Sky registration and merit review (further explained below).

**a. Tier 1:** Tier 1 offerings are largely similar to old Regulation A offerings, but the old limit of \$5 million raised in a 12-month period per issuer has now been increased to \$20 million. Unlike Tier 2, there is no limit on the amount a non-accredited investor may invest in any Tier 1 offering.

**i. State Registration:** Tier 1 still requires that offerors register under the Blue Sky laws of every state in which money is raised. However, the NASAA (North American Securities Administrators Association) recently launched a multi-state coordinated review program for Regulation A offerings that, if successful, would allow an issuer to register with multiple states by filing just one package with a relatively quick turnaround time. This could make Tier 1 much more attractive for many issuers, given its lower cost.

- ii. Reporting:** Tier 1 is less burdensome than Tier 2 in terms of SEC requirements for initial filing and ongoing reporting. Tier 1 does not require audited financial statements nor ongoing reporting. The only requirement is that offering companies file a Form 1-Z to report the completion of their offering.
- b. Tier 2:** Under Tier 2, companies are allowed to raise up to \$50 million in a 12-month period and, most importantly, there is no requirement that the offering company register under any state Blue Sky laws because the federal Reg A+ preempts state law. Tier 2 offerings must only be registered with and approved by the SEC. On the other hand, Tier 2 limits investment by non-accredited investors to the greater of 10% of their annual income or net worth, excluding their primary residence, per offering. Tier 2 also includes substantially more onerous reporting requirements than Tier 1.
  - i. Audited Financial Statements:** Tier 2 issuers must provide the SEC with two years of audited financial statements before approval, while Tier 1 issuers only need to provide "reviewed" statements.
  - ii. Ongoing Reporting:** After a successful Tier 2 raise, Tier 2 issuers who have 300 or more record holders of the security offered must also file the following ongoing reports:
    - 1.** Detailed annual reports, using Form 1-K;
    - 2.** Semiannual reports, using Form 1-SA, including unaudited interim financial statements and a management discussion; and
    - 3.** Current event reports, using Form 1-U, reporting all fundamental changes.

### Comparison of Rule 506(c), Reg CR and Reg A+

	<b>Title II Rule 506(c)</b>	<b>Title III Reg CR</b>	<b>Regulation A+ Tier 1</b>	<b>Regulation A+ Tier 2</b>
Maximum Dollars Raised	No maximum	\$1 million per 12 months, including affiliates	\$20 million per 12months	\$50 million per 12 months
Permitted Investors	Only Accredited	Anyone	Anyone	Anyone
Per-Investor Limits	None	Yes-depends on income and net worth of investor, and applies to all Reg CF deals per year.	None	For non-accredited investors, 10% of income or net worth whichever is more, per deal
General Solicitation (Advertising) Permitted?	Yes	Yes, but only through portal	Yes	Yes
Testing the Waters Permitted	Yes	Yes	Yes	Yes
Securities Sold Through Third Party Portal?	Yes (but not required)	Yes (required)	Yes (but not required)	Yes (but not required)
Can Issuer Run Its Own Portal?	Yes	No	Yes	Yes
Pre-Sale Information Required	Moderate	Substantial	Very substantial, akin to a registration statement for a public company.	Very substantial, akin to a registration statement for public company.
Audited/Reviewed Financial Statements Required?	No	Depends on size of offering; most first time users will have to provide reviewed statements.	No	Yes



	<b>Title II Rule 506(c)</b>	<b>Title III Reg CR</b>	<b>Regulation A+ Tier 1</b>	<b>Regulation A+ Tier 2</b>
Pre-Sale Approval Required	No	No	Yes-submission must be approved by SEC and the states where the securities will be sold (through a coordinated review).	Yes-Submission must be approved by SEC; state approval not required.
Investor Verification	Verification required	Self-certification	N/A	Self-certification
Ongoing Reporting	None	Moderate	None	Substantial ongoing reporting, akin to a min-public company, but waived depending on number of investors.
Length of Process	Fast	Moderate	Very Slow	Very Slow

## **B. LLC vs. Corporation**

- A business organization is governed by both the laws of the jurisdiction in which it organizes and the laws of all jurisdictions in which it conducts business. This section is an introduction to the major concepts a brewery or distillery may face upon organization and should not be relied upon for any particular jurisdiction.
- An entrepreneur must first decide under which entity type it will operate. Most likely, the choice will come down to LLC, S-Corp, or C-Corp.
- There are many factors to consider when choosing an entity type, including liability, raising capital and control, and taxation.
- 

### **1. Limited Liability Company (LLC)**

- Governing Law:** Governed by state statute. The affairs of an LLC are governed predominantly through its various governance documents. The

most prevalent governance document is the operating agreement, which defines the rights and duties of the LLC's members.

- b. Formation:** File articles of organization with the proper state office, typically the Secretary of State. The limited required articles include the name of the LLC, the LLC's in-state address, its organizer(s), the number of membership interests authorized, and the duration it is to exist.
- c. Management:** Owners are called members. An LLC can have one or more members. The LLC can be member-managed, which means that its members perform the day-to-day management of the company, or it can be manager-managed, wherein managers control the management and governance of the company. In Minnesota, the LLC can also be board-managed, where there are one or more governors who designate officers and managers to act for the LLC who have limited authority granted by the board.
- d. Capital Contributions:** An LLC can receive capital contributions by any and all of its members, in the form of any consideration, such as money, real property, personal property, or services for the company.
- e. Pass Through Taxation Benefits:** Unless it chooses otherwise, an LLC is taxed as a pass-through entity, which means that the taxation passes through to the LLC members based on the member's individual ownership interest. However, the members are taxed for their ownership interest regardless of whether or not they received any actual distributions in that tax year.
- f. Limited Personal Liability:** Members are not personally liable for the obligations and debts of the LLC beyond their initial capital contributions, provided that corporate formalities are observed by the members.
- g. Newer Form with Flexibility:** Not well-developed set of case law. LLC flexibility often results in a limitation of duties owed to minority owners. However, LLCs can be tailored to meet nearly any situation and are the most widely used business entities currently.

## 2. Corporation: C-Corporation and S-Corporation

- a. **Governing Law:** State statutes govern. Most states have well-developed case law to interpret statutes governing corporations. Articles of incorporation, bylaws or shareholder control agreements create and enforce the rights and duties of a corporation's shareholders.
- b. **Formation:** Both the S-Corp and C-Corp are separate legal entities formed by a state filing. These documents, typically called the Articles of Incorporation or Certificate of Incorporation, are the same for both S-Corps and C-Corps.
- c. **Management Structure:** Both have shareholders, directors and officers. Shareholders are the owners of the company and elect the board of directors, who in turn oversee and direct corporation affairs and decision-making, but are not responsible for day-to-day operations. The directors elect the officers to manage daily business affairs.
- d. **Liability Protection:** Shareholders are not personally liable for any debts or obligations beyond the amount of capital they have contributed to the corporation, unless the corporation fails to follow proper corporate formalities.
- e. **Corporate Formalities:** Both are required to follow the same internal and external corporate formalities and obligations, such as adopting bylaws, issuing stock, holding shareholder and director meetings, filing annual reports, and paying annual fees.
- f. **Taxation:** Taxation is often considered the most significant difference for small business owners when evaluating S-Corporations versus C-Corporations.
  - (1) **C-Corporations:** Separately taxable entities. They pay taxes at the corporate level. They also face the possibility of double taxation if corporate income is distributed to business owners as dividends, which are considered personal income. Tax on corporate income is paid first at the corporate level and again at the individual level on dividends.

(2) **S-Corporations:** Pass-through tax entities. They do not pay income, tax at the corporate level. The profits/losses of the business are instead "passed-through" the business and reported on the owners' personal tax returns. Any tax due is paid at the individual level by the owners.

g. Corporate ownership: C-Corporations have no restrictions on ownership, but S-Corporations do. The S-Corporation must meet certain characteristics such as:

- (1) it cannot have more than 100 shareholders;
- (2) its shareholders must be individuals;
- (3) its shareholders must be citizens or residents of the United States;
- (4) it must be organized in the United States; and
- (5) it can only issue one class of stock.

C-Corporations therefore provide a little more flexibility when starting a business if you plan to grow, expand the ownership or sell your corporation.

## **B. Tax Considerations**

1. **LLC:** May be taxed as:

- a. a disregarded entity if it has one member. The member experiences complete pass through taxation. The member gets taxed on all profits based on tax bracket, whether distributed or not; or
- b. a partnership if it has multiple members. The members experience complete pass through taxation. The members get taxed on all profits based on their tax bracket and ownership interest, whether distributed or not; or
- c. it may elect to be taxed as a corporation. The members experience incomplete pass through taxation, which allows the company to retain earnings from year to year and avoid being taxed regardless of a distribution.

2. **Corporation**

- a. C-Corporation; Double Taxation: Taxed at the entity level as well as shareholder level, who each get taxed individually for any distributions received from the corporation.
- b. S-Corporation; Pass Through Taxation: Shareholders are only taxed individually.

## C. Structuring, Management and Governance

### 1. Management

- a. LLC/Corporation: States may require an LLC or corporation to have certain designated officers for assist in the company's day-to-day operations. These officer positions may be held by one or more of the company's owners, but can also be held by a non-owner. Officer positions will also often have statutorily-defined duties that can be general to each officer or specific to a particular position, but can be altered with approval of the members or shareholders through agreements. The officers must carry out their duties in the best interests of the company and its owners.

- i. **LLC:** Can be managed by its members, designated managers, or board of governors. Managers and members of the board of governors can be, but are not required to be, members of the LLC. The individuals responsible for the management of the LLC may also delegate their authority to officers, such as the president, vice president, secretary, or treasurer.

- ii. **Corporation:** Typically, management is vested in the board of directors. The board of directors serve the interests of the shareholders.

- Closely Held Corporation: Generally, the shareholders will serve on the board.

- 2. **Fiduciary Duties:** Individuals responsible for management and operations of a company are generally required to adhere to the duty of care, duty of loyalty, and duty of good faith in discharging their duties on behalf of the company. If such

individuals fail to perform these duties, they may be liable to the company and its owners.

- a. Duty of Care:** A legal obligation which is imposed on an individual requiring adherence to a standard of reasonable care while performing any acts that could foreseeably harm others.
- b. Duty of Loyalty:** A legal obligation which requires fiduciaries to put the corporation's interests ahead of their own. Corporate fiduciaries breach their duty of loyalty when they divert corporate assets, opportunities, or information for personal gain.
- c. Duty of Good Faith:** A general presumption that the parties to a contract will deal with each other honestly, fairly, and in good faith, so as to not destroy the right of the other party or parties to receive the benefits of the contract. It is implied in every contract in order to reinforce the express covenants or promises of the contract.

**3. Corporate Formalities for LLC/Corporation:** Must observe certain formalities in order to maintain the limited liability shield extended to its members/shareholders .

- Piercing the Corporate Veil: The legal standard for extending personal liability varies by state, but the following suggestions help maintain the limited liability shield after forming a limited liability entity:
  - a.** Ensure the entity is sufficiently capitalized;
  - b.** Document any payments to the legal entity from the owners as either paid-in-capital or loans;
  - c.** Do not commingle personal and business funds;
  - d.** Do not pay owners in cash;
  - e.** Owners should never use the business's cash or assets for personal use or pay personal bills with company funds;
  - f.** All of the entity's taxable income should be reported on the entity's tax returns and tax returns should be filed promptly;

- g.** Shareholders who are actively involved in the business should receive a "reasonable" pre-determined wage or salary for their services;
- h.** All payments to shareholders should be clearly documented as being wages, expense reimbursements, or profit distributions;
- i.** All expenses paid to shareholders should be reflected in formal expense reimbursement reports, backed up by appropriate receipts and invoices;
- j.** Owners should not receive "profit distributions" if the entity is insolvent;
- k.** All creditors should be paid regularly before distributing any profits;
- l.** Any purchase of property, computers, equipment, etc. from shareholders should be at commercially reasonable prices and terms and documented in formal written agreement;
- m.** Obtain appropriate insurance for the type of business in question;
- n.** Prepare appropriate bylaws, operating agreements, etc.;
- o.** Hold annual meeting of directors, shareholder, or members and prepare the minutes in a corporate minute book, which should reflect major corporate transactions;
- p.** Hold elections and appoint officers and directors for the entity;
- q.** Obtain federal and state tax identification numbers;
- r.** Obtain sales tax exemption certificates;
- s.** Issue share certificates to owners (if corporation);
- t.** File annual registration statement with Secretary of State to remain in "good standing" if the state law requires it;
- u.** Sign all contracts, agreements, purchases, plans, loan, investments, and accounts in the name of and on behalf of the entity;
- v.** Train officers and directors how to sign contracts, purchase orders, and agreements on behalf of the entity;
- w.** Register all "assumed names" being used by the entity;
- x.** Use the official corporate name on all letterhead, business cards, marketing materials, coupons, websites, etc. to clearly notify third parties that the business has limited liability;

- y. If possible, run the business profitably and pay dividends/profit distributions to the owners periodically; document the same;
- z. Avoid entering into transactions or incurring debts when the company is insolvent;
  - aa. Avoid having the dominant owner siphon funds from the business;
  - bb. Ensure that all officers and directors have a meaningful voice in the business, participate in decision-making, and periodically meet and vote on major corporate decisions;
  - cc. Avoid using the corporation merely as a façade for individual dealings.

## **D. Drafting and Negotiating Formation Agreements**

### **1. General Governance Documents**

- a. Drafting formation agreements is very important for memorializing the rights, responsibilities, and expectations of a business's owners, officers, managers, or board members.
- b. 'Governance documents often expressly provide provisions regarding the decision-making process, profit and loss allocations and distributions, fiduciary duties, conduct and procedures for meetings, and delegation of officer positions and duties.
- c. A few examples of agreements: operating, member control, partnership, shareholder control, buy-sell, bylaws.

### **2. Additional Brewery/Distillery Provisions**

- a. Include provisions that require all proposed members, shareholders, directors or officers to pass the appropriate TTB background check process.
- b. Include provisions that require all proposed members, shareholders, directors or officers to pass any applicable local requirements to obtain and hold a liquor license or any other relevant local licensing requirements.



- i. Include provisions that require the ownership in the business to be subject to maintaining or passing any required local licensing.
- ii. If the owner does not meet these standards or fails to maintain these stands, the governance documents can establish procedures to terminate the relationship with the individual, including a forced buy-out of the owner's interest in the company.

## **E. Capital Raising, Crowdfunding, and Other Financing Methods**

### **1. Current Regulatory Landscape and Key Definitions**

- a. **Generally:** Nearly every means by which a company raises capital involves securities laws. These laws regulate the manner in which securities are sold, the amount of money that may be raised, the persons to whom the securities may be offered, and the method by which investors may be solicited.
- b. **Federal Registrations and Exemptions:** As a general rule, in order to comply with Federal securities laws, a person selling a security must either:
  - i. "register" such sale with the Securities Exchange Commission (SEC) or
  - ii. identify a specific exemption that allows such sale to be conducted without registration.
    - SEC registration is time consuming and expensive.
    - For most small businesses, SEC registration is not a feasible option.
- c. **State Blue Sky Laws:** In addition, an issuer selling securities must adhere to blue sky laws in each state where the securities are being sold, all of which vary from each other.

### **2. Private Placements**

- a. **Section 4(2):** The most common federal exemption entrepreneurs rely on is Section 4(2) of the Securities Act, which exempts "transactions...not involving any public offering" - i.e., a **private placement**. A company

seeking to determine whether an offering will be exempt from registration under Section 4(2) will need to evaluate a number of factors which, although routinely addressed by courts, seldom lead to a definitive answer as to whether an offering is a "public offering" under Section 4(2). Different courts emphasize different factors critical to the Section 4(2) exemption, no single one of which necessarily controls. The factors are guidelines, and include:

- i.** Offeree qualification (i.e., whether the investors are sophisticated);
  - ii.** Manner of the offering (i.e., whether the company will engage in advertising or other promotional activities);
  - iii.** Availability and accuracy of information given to offerees and purchasers (i.e., whether the people to whom the company proposes to sell securities have access to basic financial information about the company);
  - iv.** The number of offerings and number of purchasers (i.e., whether the company solicited investment from a large group of people); and;
  - v.** Absence of intent to redistribute (i.e., whether the people to whom the company proposes to sell securities have an intention to hold the securities for investment purposes - generally for a minimum holding period of 24 months).
- b. Regulation D:** The SEC provides a clear set of "safe harbor" rules that issuers can follow to ensure that they are conducting a valid private placement under Section 4(2). The most common safe harbors that small companies have customarily relied upon in conducting private placements are Rule 504 and Rule 506 (now called Rule 506(b) - see below).
- i. General Solicitation:** Rule 502(c) provides that "neither the issuer nor any person acting on its behalf shall offer or sell the securities by any form of general solicitation or general advertising, including, but not limited to, the following:

1. any advertisement, article, notice or other communication published in any newspaper, magazine, or similar media or broadcast over television or radio; and
  2. any seminar or meeting whose attendees have been invited by any general solicitation or advertising." In general, this means that issuers will need to have a substantial pre-existing relationship with a potential investor before making an offer of securities under Rule 504 or Rule 506(b).
- ii. Accredited investor:** Under Rule 501(a), an accredited investor is a person who meets certain qualifications and, therefore, is deemed able to protect himself or herself in making investment decisions without additional protections under the securities laws, such as those obtained through the SEC registration process and the public disclosure of information about the company that is made through the process of becoming an SEC reporting company. There are several ways to qualify as an accredited investor with the most common being:
1. an individual with at least \$200,000 (or \$300,000 jointly with a spouse) in annual income over the past 2 years or at least \$1 million in net worth (excluding the value of a principal residence); or
  2. an entity in which all of the equity owners are accredited investors or the entity has at least \$5 million in net assets.

### 3. The "Old Rules" For Raising Capital

- a. **Rule 504:** Generally speaking, Rule 504 allows companies to raise up to \$1 million from an unlimited number of accredited and non-accredited investors (subject to counterpart state Blue Sky registrations and exemptions). Companies are not permitted to engage in general solicitation except for in states where the securities have been registered or states that

provide an exemption from registration that allows the company to generally solicit to accredited investors only.

**i. State law counterpart:-** Limited Offering Exemption: Most states have a "limited offering" exemption that is often relied on by companies who are conducting Rule 504 offerings. Normally, sales by a company to no more than 35 non-accredited investors (and an unlimited number of accredited investors) during any 12 consecutive months are exempt from registration.

**b. Rule 506:** Rule 506 is the most common "safe harbor" relied on by companies conducting private placements. Generally speaking, Rule 506 allows an issuer to raise an unlimited amount of capital from an unlimited number of accredited investors and up to 35 non-accredited investors. However, if even one non-accredited investor becomes a purchaser in the offering, then the company must provide all investors with a very detailed disclosure document that satisfies other SEC requirements. For this reason, the practical reality is that Rule 506 offerings are usually restricted to accredited investors only.

**i. State law counterpart:** Securities issued in reliance on Rule 506 are considered Federal "covered securities" and the offer and sale of such securities are exempt from registration as long as the issuer makes a notice filing.

**ii.**

**4. The "New" Rules:** Jumpstart Our Business Startups (JOBS) Act: On April 5, 2012, Congress passed the JOBS Act in an effort to foster job growth by modernizing Federal securities laws. The JOBS Act consisted of three key parts that are relevant for securities crowdfunding:

**Title II**

**Title III**

**Title IV**

<b>Advertising in Connection with Sales to Accredited Investors</b>	<b>Crowdfunding for All</b>	<b>Reg A+/"Mini-IPOs"</b>
Also called Rule 506(c)	SEC released proposed rules in October 2013	SEC released final rules in March 2015
Became effective in October 2013	The proposed rules have been almost universally criticized	Became effective in June 2015
Growing in popularity	Revised rules went into effect in May 2016	Not very useful for small businesses

**b. Title II and Rule 506(c) - Advertising to Accredited Investors:** In late 2013, the SEC (pursuant to the authority granted to it under Title II of the JOBS Act), finalized new Rule 506(c) which allows companies to generally solicit (or advertise) their securities offerings so long as all of the investors who actually purchase securities in the offer are accredited. This means that companies may now talk about their offerings in public seminars, send out email blasts, push offering information out on social media sites, as well as run ads on TV, radio, and the Internet. Companies who comply with Rule 506(c) are now free to talk about their offering to whomever they want (including non-accredited investors). Companies who generally solicit under Rule 506(c) may only sell the securities to accredited investors.

**(1) Verification Steps:** Using Rule 506(c), however, comes with certain additional compliance requirements. Companies must take additional steps to verify that all purchasers actually are accredited. In Rule 506(c), the SEC listed several non-exclusive methods that are deemed to satisfy the verification requirements (provided that the issuer does not have knowledge that the purchaser is non-accredited). The "safe harbors" include:

- (i) Income verification by checking federal tax forms, including W-2's and tax returns, and a statement by the investor that he or she expects enough income in the current year to remain accredited;

(ii) Net worth verification by checking a recent credit report (with the past 3 months) and bank or investment account statements, together with a written representation from the purchaser that he or she has disclosed all liabilities necessary to make a determination of net worth; and

(iii) Certification of accredited investor status by a registered broker-dealer, SEC-registered investment advisor, licensed attorney, or CPA who has verified the purchaser's accredited investor status.

### Comparison of Rules 504, 506(b) and 506(c)

	Rule 504	Rule 506(b)	Rule 506(c)
How much money can I raise?	Up to \$1M	Unlimited	Unlimited
Can I advertise the sale of my securities?	No, unless coupled with a state exemption or registration that allows advertising.	No, unless coupled with a state exemption or registration that allows advertising.	Yes.
To whom can I sell securities?	Anyone. However, counterpart state exemptions or registrations may impose additional restriction on number to non-accredited investors	Unlimited number of accredited investors.  Up to 35 non-accredited investors if you believe they are “sophisticated”.	Unlimited number of accredited investors
Do I have to comply with SEC’s formal information delivery requirements?	No, but counterpart state exemption or registration may impose additional requirements.	No, if only accredited investors are included.	No.

		Yes, if any non-accredited investors are included.	
Do I have to verify that any accredited investors are truly accredited?	No, accredited investors can “self-certify”.	No, accredited investors can “self-certify”.	Yes, you must take “reasonable steps” to verify that the investors are, in fact, accredited.

**c. Title III "retail" crowdfunding and Regulation CF:** Title III of the JOBS Act was meant to democratize the business funding process by allowing non-accredited individuals the opportunity to participate online and invest into private companies. The SEC delayed releasing final rules for years, and the system finally went live in May 2016. Issuers must comply with multiple requirements and limitations, namely:

- Issuer may only raise up to \$1M in any 12-month period.
- Individual investor limits:
  - If the investor's annual net income OR net worth is < \$100k, then the investor may invest the greater of: (a) \$2,000; or (b) 5% of the investor's annual income or net worth.
  - If the investor's annual net income AND net worth is > \$100k, then the investor may invest 10% of the investor's annual income or net worth
- Investors are subject to a \$100k max across all Reg CF offerings in any 12-month period.
- Issuer must provide financial statements based on offering size:
  - < \$100k -> Internally prepared, certified statements
  - \$100k - \$500k 4 CPA reviewed statements
  - \$500k - \$1M -> CPA audited financials (or CPA reviewed statements if the issuer is a first time user of the system).
- Issuer must file a robust disclosure document with the SEC.

- Issuer is subject to annual SEC reporting obligations.
- Offerings must be made through registered portals. The portals must be either (a) registered with the SEC as a broker-dealer; or (b) registered as a portal operator with the SEC and be a member of FINRA.

**d. Title IV and Regulation A+:** Reg A+, which went into effect in June 2015, has been described as a mini-IPO or "IPO-Lite," in that it allows nearly any company with principal offices in the U.S. or Canada to use internet crowdfunding to raise up to \$50 million per year from any number of both accredited and non-accredited investors under a regulatory scheme that is far less burdensome than that of a traditional IPO. There is no prohibition on general solicitation, and offering companies are not required to independently verify the sophistication (income or net worth) of their investors. Corporations, limited liability companies, and limited partnerships can take advantage of Reg A+'s two-tiered offering scheme and can sell nearly all types of securities, including equity, debt, and debt securities convertible into equity securities. Furthermore, the securities issued in Reg A+ will be unrestricted and freely transferable. One of the most exciting changes for companies seeking to raise capital under Reg A+ is that Tier 2 offerings are not subject to state Blue Sky registration and merit review (further explained below).

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Administrators Association) recently launched a multi-state coordinated review program for Regulation A offerings that, if successful, would allow an issuer to register with multiple states by filing just one package with a relatively quick turnaround time. This could make Tier 1 much more attractive for many issuers, given its lower cost.

**ii. Reporting:** Tier 1 is less burdensome than Tier 2 in terms of SEC requirements for initial filing and ongoing reporting. Tier 1 does not require audited financial statements nor ongoing reporting. The only requirement is that offering companies file a Form 1-Z to report the completion of their offering.

**b. Tier 2:** Under Tier 2, companies are allowed to raise up to \$50 million in a 12-month period and, most importantly, there is no requirement that the offering company register under any state Blue Sky laws because the federal Reg A+ preempts state law. Tier 2 offerings must only be registered with and approved by the SEC. On the other hand, Tier 2 limits investment by non-accredited investors to the greater of 10% of their annual income or net worth, excluding their primary residence, per offering. Tier 2 also includes substantially more onerous reporting requirements than Tier 1.

**i. Audited Financial Statements:** Tier 2 issuers must provide the SEC with two years of audited financial statements before approval, while Tier 1 issuers only need to provide "reviewed" statements.

**ii. Ongoing Reporting:** After a successful Tier 2 raise, Tier 2 issuers who have 300 or more record holders of the security offered must also file the following ongoing reports:

**1.** Detailed annual reports, using Form 1-K;

2. Semiannual reports, using Form 1-SA, including unaudited interim financial statements and a management discussion; and
3. Current event reports, using Form 1-U, reporting all fundamental changes.

### Comparison of Rule 506(c), Reg CR and Reg A+

	<b>Title II Rule 506(c)</b>	<b>Title III Reg CR</b>	<b>Regulation A+ Tier 1</b>	<b>Regulation A+ Tier 2</b>
Maximum Dollars Raised	No maximum	\$1 million per 12 months, including affiliates	\$20 million per 12 months	\$50 million per 12 months
Permitted Investors	Only Accredited	Anyone	Anyone	Anyone
Per-Investor Limits	None	Yes-depends on income and net worth of investor, and applies to all Reg CF deals per year.	None	For non-accredited investors, 10% of income or net worth whichever is more, per deal
General Solicitation (Advertising) Permitted?	Yes	Yes, but only through portal	Yes	Yes
Testing the Waters Permitted	Yes	Yes	Yes	Yes
Securities Sold Through Third Party Portal?	Yes (but not required)	Yes (required)	Yes (but not required)	Yes (but not required)
Can Issuer Run Its Own Portal?	Yes	No	Yes	Yes
Pre-Sale Information Required	Moderate	Substantial	Very substantial, akin to a registration statement for a public company.	Very substantial, akin to a registration statement for public company.

	<b>Title II Rule 506(c)</b>	<b>Title III Reg CR</b>	<b>Regulation A+ Tier 1</b>	<b>Regulation A+ Tier 2</b>
Audited/Reviewed Financial Statements Required?	No	Depends on size of offering; most first time users will have to provide reviewed statements.	No	Yes
Pre-Sale Approval Required	No	No	Yes-submission must be approved by SEC and the states where the securities will be sold (through a coordinated review).	Yes-Submission must be approved by SEC; state approval not required.
Investor Verification	Verification required	Self-certification	N/A	Self-certification
Ongoing Reporting	None	Moderate	None	Substantial ongoing reporting, akin to a min-public company, but waived depending on number of investors.
Length of Process	Fast	Moderate	Very Slow	Very Slow

## 5. Other Crowdfunding Methods

**a. Rule 504 + State registration:** Theoretically, a company may legally conduct a small (less than \$1 million) crowdfunding campaign by combining a Federal Rule 504 exemption with state registered offering.

**i. General Solicitation under Rule 504:** Rule 504 allows an issuer to engage in general solicitation to accredited and non-accredited investors if the issuer either:

1. Registers the offering exclusively in one or more states that require a publicly filed registration statement and delivery of a substantive disclosure document to investors; or

2. Registers and sells the offering in a state that requires registration and disclosure delivery and also sells in a state without those requirements, so long as the company delivers the disclosure documents required by the state where the company registered the offering to all purchasers (including those in the state that has no such requirements).
- ii. **SCOR Offering Option:** Some states provide a simplified process for "small corporate offering registrations" that otherwise are exempt from Federal registration under Rule 504.
- b. Federal intrastate exemption + State crowdfunding exemption**
- i. **Section 3(a)(11) and Rule 147:** Another lesser known Federal securities exemption is the "intrastate" exemption embodied by Section 3(a)(11) of the Securities Act and Rule 147 promulgated by the SEC. Generally speaking, Section 3(a)(11) exempts from SEC registration any offering that is confined to the borders of a single state. To qualify for this exemption, the company must meet requirements of Rule 147, which include:
    1. The company must be incorporated in the state in which it is offering the securities;
    - ii. The company must only sell the securities to individuals residing in that state;
    - iii. 80% of the company's consolidated gross revenues must be derived from the state in which the offering is conducted;
    - iv. 80% of the company's consolidated assets must be located within the state in which the offering is conducted; and
    - v. 80% of the offering's net proceeds must be intended to be used, and actually used, in connection with the operation of a business or real property, the purchase of real property located in, or the rendering of services, within the state in which the offering is conducted.

In addition to complying with the Federal "intrastate" exemption, the issuer must also satisfy the requirements of the state crowdfunding exemption. The requirements vary on a state-by-state basis, but they often impose:

- i. Limits on the amount of money the issuer can raise;
        - ii. Limits on the amount of money that investors can invest (there are usually different limits for accredited investors vs. non-accredited investors);
        - iii. Disclosure requirements, including whether the issuer must provide purchasers with audited or reviewed financial statements;
        - iv. Escrow requirements;
        - v. Use of third party Internet portal; and
        - vi. Ongoing reporting requirements of the issuer.
- c. General Solicitation in Intrastate Crowdfunding Offerings: There is no prohibition in Section 3(a)(11) or Rule 147 regarding general solicitation as long as such solicitation:
  - complies with applicable state law; and
  - does not result in an offer or sale to nonresidents of such state.
- i. **SEC Guidance on Online Advertising:** In recent months, the SEC has provided guidance on how intrastate issuers can use the internet to publicize their offerings without having those online advertisements result in an offer or sale to nonresidents of that state.
  - a. **Limiting Access to Out of State Residents:** In April 2014, the SEC clarified in Questions 141.03-141.05 that issuers hoping to utilize the Rule 147 exemption could use the Internet for general advertising and solicitation if they implemented measures to limit the offers to people within the issuer's state. In the context of an offering conducted within state crowdfunding requirements, those measures have to include:
    - i. limiting access to information about a specific investment opportunity to persons who confirm they are residents of the

relevant state "(for example, by providing a representation...such as a zip code or residence address)" and

- ii. providing a disclaimer and restrictive legend clarifying "that the offer is limited to residents of the relevant state under applicable law." (Question 141.04).

**b. IP Address Blocking:** In recent years, the SEC suggested what might be a simpler method of limiting the offer to those within the relevant state. The issuer can "implement technological measures" that limit any offers to persons with an IP address originating within the issuer's state and prevent offers to any individuals outside of the issuer's state (Question 141.05). However, the offer should still contain a disclaimer and restrictive legend. Presumably, this clarification allows issuers to skip the opt-in step where the viewer must verify they are residents of the relevant state before viewing the solicitation or advertisement. The simplification could greatly increase the number of views and potentially improve the effectiveness of the communication.

## 6. Capital Raising Pitfalls

**a. Rights of Ownership:** When considering whether to engage in a private offering to raise investment capital, a company must consider that investors will be owners of the company following the offering (albeit likely constituting a minority stake in the entity) and as, such, those investors will have certain rights afforded to them by law.

### **b. Limited Liability Companies**

**i. Governance Rights:** A member's governance rights (i.e., the right to vote and control) in a limited liability company (LLC) depends upon whether the LLC is member-managed, board-managed or manager-managed. If the LLC is member-managed, each member has equal rights in the management and conduct of the company's activities. Even if the LLC is manager-managed, certain proposed

actions require consent of the members. In a board-managed LLC, while the board of governors manages the LLC's affairs, the board is selected by a majority vote of the members.

- ii. Right to Profits:** Unless otherwise provided in the LLC operating agreement, each member is entitled to participate in any distribution(s) of the company's profits (although as noted herein, some additional incentives may be necessary).
- iii. Right to Information:** Members have the right to access information from the LLC that is material to the member's interest as a member.
- iv. Minority Rights Regarding Oppressive Conduct:** A member does not have the right to dissent from a proposed course of action and require the LLC to purchase his/her membership interest. However, some states provide for certain rights and remedies upon a court finding of "oppressive conduct" towards a minority member or members. Note, however, that the LLC operating agreement can limit the remedies that a court may impose, including but not limited to a court-ordered buyout.

**c. Corporations**

- i. Voting Rights:** Unless otherwise provided within the corporation's articles of incorporation, a shareholder in a corporation has one vote per share. In addition, even if the articles provide that the holders of a particular class of shares are not entitled to voting rights, in some instances, these shareholders are entitled to voting rights as a matter of law.
- ii. Rights to Information:** Shareholders are entitled to inspect books and certain records of the corporation.
- iii. Dissenters Rights:** Most significantly, a shareholder of a corporation may dissent from, and obtain payment for the fair value of the shareholder's shares in the event of certain actions.

- d. **Maintaining Control:** Frequently in private offerings for startup ventures, the capital contributed by investors through the offering often exceeds the amount of capital contributed by the company's founders. This can prove problematic for the founders seeking to maintain control of the entity by offering a minority ownership stake in the company through the offering. However, various incentives can be employed to make ownership of a minority interest in the business more palatable for investors.
- e. **Changes to Terms of Offering; Rescission Offers:** Frequently a prospective investor will propose a counteroffer which differs from the terms outlined in the offering document. If accepted, be aware that changed terms for even a single investor will trigger an obligation to make a rescission offer to prior investors.

## 7. Other Sources of Funds

- a. **Debt Financing:** Before embarking upon a private offering, it is best to consult with one or more lending institutions regarding a small business loan. Banks offer several small business loan programs, ranging from their own private loan programs to those loan programs established by the U.S. Small Business Administration (SBA). These types of programs are particularly useful when seeking financing to acquire equipment and/or real estate, given the ability to pledge these assets as collateral. Personal guaranties of those owners holding 20% or more is also generally required.
- b. **"Gap" Financing:** "Gap" financing refers to state and local financing incentives that can bridge the gap between a bank loan and an equity capital investment.
  - i. **State Initiatives:** Some states have financing programs available for small businesses. These initiatives provide financing to help add new workers and retain high-quality jobs on a statewide basis. The focus is usually on industrial, manufacturing, and technology-related industries to increase the local and state tax base and improve economic vitality statewide.



- ii. Local Financing Incentives:** Some cities have financing programs and incentives available for small businesses that locate within those cities. For example, some cities have a "Two-Percent Loan" program. Two-Percent Loans provide financing to small businesses (retail, service or light manufacturing) to purchase equipment and/or to make building improvements. A private lender provides half the loan at market rate and the City provides the rest, up to \$50,000 at 2 percent interest (up to \$75,000 in designated neighborhood commercial districts). The loan term is set by the private lender and can be for up to 10 years. Bank fees vary, but the City charges a 1 percent origination fee with a minimum of \$150 due at closing.
- iii. Tax Increment Financing:** Tax increment financing, or TIF, is a public financing method that is used as a subsidy for redevelopment, infrastructure, and other community-improvement projects. Through the use of TIF, municipalities can dedicate future tax revenues of a "particular business or group of businesses toward an economic development project in the community.
- c. Kickstarter/Rewards Based Crowdfunding:** In recent years, websites such as Kickstarter.com have popularized "rewards-based" crowdfunding. Kickstarter.com is a web portal that allows individuals to make a contribution to a particular project in exchange for some reward, typically some type of tangible product. Other variations of rewards-based crowdfunding include "founders clubs" (often used by local breweries and distilleries) which offer a variety of member benefits (but not any voting rights or share of profits in the enterprise so as to steer clear of the definition of a "security") in exchange for payment of a one-time membership fee. These types of rewards-based incentives should be structured in a way that minimizes liability for the company; i.e., the terms and conditions of membership should be in writing and should specify what happens to the memberships if the company is sold or ceases to do business, that the

memberships are non-transferrable and that the membership does not carry with it the rights of ownership.

## **8. Practical Considerations in Structuring a Private Offering**

- a. Put Rights:** A put or put option is a device which gives the owner of the put the right, but not the obligation, to sell his/her shares, at a specified price (the put price), by a pre-determined date to a given party (typically the company).
- b. Call Rights:** In contrast to put rights, call rights or a call option refers to the right, but not the obligation, to buy an agreed number of shares within a certain time for a certain price (the "call price"). The seller is obligated to sell his/her shares to the buyer if the buyer so decides.
- c. Preferred Distributions:** In some instances, it may be necessary or advantageous to incentivize potential investors by including a preferred distribution for investors. Most closely held companies give their board the discretion to make (or not make) distributions of profits and the amount of such distributions. A preferred distribution constitutes the company's contractual obligation to pay a minimum amount to the holders of such preferred distribution rights ahead of making any discretionary distributions to all owners. Often times preferred distributions are "cumulative", meaning that a preferred distribution which is not made in one year cumulates and is to be paid when the company has funds available to pay it.
- d. Preferential/Accelerated Distributions:** In regards to general distributions of profits, in order to maintain governing control of the company following a private offering, and in addition or alternative to preferred distributions it may be necessary to offer investors a distribution preference. For example, suppose the investors as a group own 40% of the company. A distribution preference would be to make 60% of the company's operating distributions to the investor class for a period of years until the investors recoup their initial investment. Upon doing so,

distributions would then be made pro rata based upon ownership percentages.

- e. **Written Agreement.** All of these mechanisms should be included in a written agreement between the owners (an operating agreement for an LLC or a shareholder agreement for a corporation), and new investors should be required to execute a joinder to the agreement in order to bind themselves to the agreement.

## Appendix 2

### Summary of State Beer Self-Distribution Laws

<u>State</u>	<u>License to Self Distribute</u>	<u>Statutory Citation</u>
Alabama	No	Code of Ala. § 28-3A-6
Alaska	Yes	Alaska Stat. § 04.11.010
Arizona	Yes	A.R.S. § 4-205.08
Arkansas	Yes	A.C.A. § 3-5-1405
California	Yes	Cal Bus & Prof Code § 23357
Colorado	Yes	C.R.S. 12-47-402; C.R.S. 12-47-415
Connecticut	Yes	Conn. Gen. Stat. § 30-16
Delaware	No	4 Del. C. § 512C; Brewpubs at § 512B
District of Columbia	Yes	D.C. Code § 25-110
Florida	No	Fla. Stat. § 563.022
Georgia	No	O.C.G.A. § 3-5-32
Hawaii	Yes	HRS § 281-31
Idaho	Yes	Idaho Code § 23-1003
Illinois	Yes	235 ILCS 5/5-1; 235 ILCS 5/3-12

Indiana	Yes	Burns Ind. Code Ann. § 7.1-3-2-7
Iowa	Yes	Iowa Code § 123.124
Kansas	No	K.S.A. § 41-308b
Kentucky	No	KRS § 243.157
Louisiana	No	La. R.S. 26:273
Maine	Yes	28-A M.R.S. § 1355-A
Maryland	Yes	Md. Ann. Code art. 2B, § 2-208
Massachusetts	Yes	ALM GL ch. 138, § 19
Michigan	Yes	MCLS § 436.1401
Minnesota	Yes	Minn. Stat. § 340A.301
Mississippi	No	Miss. Code Ann. § 67-3-46
Missouri	No	§ 311.195 R.S.Mo.
Montana	Yes	Mont. Code Anno., § 16-3-214
Nebraska	No	R.R.S. Neb. § 53-169
Nevada	No	Nev. Rev. Stat. Ann. § 369.382
New Hampshire	Yes	RSA 178:12; RSA 178:12-a; RSA 178:13

New Jersey	Yes	N.J. Stat. § 33:1-10
New Mexico	Yes	N.M. Stat. Ann. § 60-6A-26.1
New York	Yes	NY CLS Al Bev § 51; NY CLS Al Bev § 52; NY CLS Al Bev § 64-c
North Carolina	Yes	N.C. Gen. Stat. § 18B-1104
North Dakota	Yes	N.D. Cent. Code, § 5-01-11; N.D. Cent. Code, § 5-01-14
Ohio	Yes	ORC Ann. 4303.02; ORC Ann. 4303.022; ORC Ann. 4301.24
Oklahoma	Yes	37 Okl. St. § 521
Oregon	Yes	ORS § 471.220; ORS § 471.200
Pennsylvania	Yes	47 P.S. § 4-431
Rhode Island	Yes	R.I. Gen. Laws § 3-6-1
South Carolina	No	S.C. Code Ann. § 61-4-940
South Dakota	No	S.D. Codified Laws § 35-8A-8
Tennessee	Yes	Tenn. Code Ann. § 57-5-101; Tenn. Code Ann. § 57-2-104
Texas	Yes	Tex. Alco. Bev. Code § 62.01; Tex. Alco. Bev. Code § 74.01 and 74.08
Utah	Yes	Utah Code Ann. § 32B-11-503

Vermont	Yes	7 V.S.A. § 230
Virginia	Yes	Va. Code Ann. § 4.1-208
Washington	Yes	Rev. Code Wash. (ARCW) § 66.24.244
West Virginia	Yes	W. Va. Code § 11-16-6; W. Va. Code § 60-4-3
Wisconsin	Yes	Wis. Stat. § 125.29; Wis. Stat. § 125.295
Wyoming	Yes	Wyo. Stat. § 12-2-201; Wyo. Stat. § 12-4-412; Wyo. Stat. § 12-5-401





**Intellectual Property, Marketing and Advertising:  
Hidden Dangers**

**Submitted by Natalie R. Walz**



**Intellectual Property, Marketing and Advertising:  
Hidden Dangers**

**Submitted by Natalie R. Walz  
Chestnut Cambronne PA**

## **A. Disputes Regarding Beer Names and Trademarks**

1. Purposes of trademarks
  - a. Indicate product source
  - b. Distinguish products from each other and competitors
  - c. Protect company's investment in its business and brand
  - d. Protect consumer expectations of quality
2. U.S. Breweries continue to increase with a 16 percent growth from 2016 to 2017
  - a. Saturation in the market leads to increased trademark infringement litigation and inter partes proceedings before the Trademark Trial and Appeal Board.

## **B. Issues with Protecting Trademarks and Characteristic Beer Bottle Trade Dress**

1. Nearly any matter that distinguishes the source of one product from another can qualify as a trademark, including, words, designs, color, product configurations, packaging and containers, sales environments, scents, sounds and touch.
2. Trade dress generally refers to the overall appearance or image of a product, including features such as size, shape, color, texture, or graphics. *John H. Harland Co. v. Clarke Checks, Inc.*, 711 F.2d 966, 980 (11th Cir. 1983). When considered in the context of breweries, trade dress generally applies to beer bottles, tap handles or a taproom's layout or design.
3. Issues in obtaining trade dress protection include issues with functionality and distinctiveness.
  - a. Functionality: A product or its attribute may not be protected as trade dress if it serves a functional purpose. The purpose underlying the non-functionality rule is to prevent producers from acquiring monopolies so as to ensure that functional characteristics are available to all competitors in the marketplace.
    - i. Functional means any attribute that makes the product more useful, or more easily used, or that contributes to the ease or economy of manufacture or distribution.

- ii. Courts apply two tests in determining functionality: utilitarian functionality and aesthetic functionality. Under the traditional utilitarian functionality test, a product feature will be considered functional if it is essential to the use or purpose of the article or if it affects the cost or quality of the article. *Inwood Labs., Inc. v. Ives Labs., Inc.*, 456 U.S. 844, 850 n.10 (1982). Under the aesthetic functionality test, a product feature will be considered functional if it is one, the exclusive use of which, would put competitors at a non-reputation related disadvantage. *Qualitex Co. v. Jacobson Products Co., Inc.*, 514 U.S. 159, 165 (1995).
- b. Distinctiveness: A product or its attribute's ability to identify a single source of goods or services, even if the source is unknown. Distinctiveness may be either inherent or acquired (known as secondary meaning).
- i. Inherently distinctive trade dress is immediately capable of identifying a source of origin for a good or service. *Two Pesos, Inc. v. Taco Cabana, Inc.*, 505 U.S. 763, 768 (1992). Courts vary in the test applied in determining whether trade dress is inherently distinctive with some applying the same spectrum used for assessing traditional word marks (generic, descriptive, suggestive, arbitrary, fanciful), *Abercrombie & Fitch Co. v. Hunting World, Inc.*, 537 F.2d 4, 9 (2d Cir. 1976), and others applying a four-factor test of whether the trade dress is common or basic, unique or unusual in a particular field, a mere refinement of a commonly adopted and well-known form of ornamentation for a particular class of goods or services viewed by the public as dress or ornamentation, and capable of creating a commercial impression distinct from any accompanying words, *Seabrook Foods, Inc. v. Bar-well Foods Ltd.*, 568 F.2d 1342 (C.C.P.A. 1977).
  - ii. Acquired distinctiveness is trade dress that has obtained distinctiveness through use or promotion over time. In determining whether dress has acquired distinctiveness, courts consider a variety of evidence, including, consumer testimony, surveys, exclusivity, manner and length of use, amount and manner of advertising, amount of sales, number of customers, establishment in the marketplace, and proof of intentional copying by an infringer.

**C. Trademark Difficulties With PTO Considering Beer in Same Class as Wine and Spirits**

1. In order to establish a likelihood of confusion, the goods or services at issue do not need to be identical or directly competitive, but instead merely “related in some manner and/or if the circumstances surrounding their marketing [be] such that they could give rise to the mistaken belief that [the goods or services] emanate from the same source.” *Coach Servs., Inc. v. Triumph Learning LLC*, 101 U.S.P.Q.2d 1713, 1722 (Fed. Cr. 2012).
  - a. The nature and scope of a party’s goods or services is determined based on the goods or services recited in the application or registration. The International Class identification “is wholly irrelevant” to a likelihood of confusion claim. *Jean Patou, Inc. v. Theon, Inc.*, 29 U.S.P.Q.2d 1771, 1774 (Fed. Cir. 1993).
2. The Trademark Trial and Appeal Board and courts have recognized that beer and wine and other alcoholic beverages are related. The Trademark Trial and Appeal Board and the courts’ finding of relatedness is often supported by evidence demonstrating that the same entity offers both products at issue thereby establishing that consumers are accustomed to seeing the goods emanating from the same source.
3. Clearance searches need to be conducted in order to determine whether a trademark is available. There are generally two types of clearance searches that can be performed: (1) a preliminary search and (2) a comprehensive search. Because the Trademark Trial and Appeal Board and the courts are finding that beer is related to other alcoholic beverages, including wine, a proper trademark clearance search for a mark that is going to be used in connection with beer needs to include a search of marks used in connection with other alcoholic beverages, including wine.
  - a. A preliminary search is a quick knock out search of the USPTO’s database to identify clear problems.
  - b. A comprehensive search looks at not only the USPTO’s database, but also common law uses, such as websites and state databases.
4. Adopt strong marks at the outset. Stronger marks provide a wider range of exclusivity and are immediately protectable.

**D. Intellectual Property Infringement: Difficulties in Protecting Breweries and Distilleries in a Competitive Market.**

1. To maintain trademark rights, trademark owners need to be diligent in protecting their marks against infringement and misuse by third parties as failure to do so may diminish the value of the marks.
  - a. Proper protection of a trademark owner's rights includes monitoring the marketplace for infringement or misuse of the mark and monitoring third-party applications. Trademark owners should develop, and follow, a trademark enforcement strategy prior to any potential infringement or misuse.
2. Formal action to enforce trademark rights include actions before the Trademark Trial and Appeal Board to oppose third party registrations and to cancel existing registrations. The Trademark Trial and Appeal Board can only address registration of the trademark; it cannot issue injunctions or monetary awards.
3. Formal action to enforce trademark rights also includes commencing litigation before the court. Claims may include trademark infringement and unfair competition. The court may award injunctive relief and monetary damages.
4. Before pursuing formal action, the trademark owner may consider whether the infringement or misuse may be resolved informally. This could include contact between the business owners or a cease and desist letter issued by an attorney.

#### **E. Challenges in Protecting and Copywriting Brewing Recipes and Processes**

1. Copyright protects original works of authorship. The works of authorship include literary works, musical works, dramatic works, pantomimes and choreographic works, pictorial, graphic and sculptural works, motion pictures and other audiovisual works, sound records and architectural works. 17 U.S.C. § 102(a).
  - a. Copyright does not protect ideas, procedures, methods, systems, processes, concepts, principles or discoveries.
2. A recipe is a statement of the ingredients and procedure required for making a dish of food or beverage. Copyright does not protect recipes that are mere listings of ingredients. However, a recipe that creatively explains or depicts how or why to perform a particular activity may be copyrightable. If registration is afforded in this instance, the registration will not extend to the list of ingredients that appear in the recipe or the underlying process for making the recipe.

**F. Brewery and Distillery Confidentiality/Non-Disclosure Agreements: Hidden Dangers that Make Them Unenforceable.**

1. Breweries and distilleries that share, receive and exchange confidential information with and from customers, suppliers and other parties would benefit from and should implement the use of confidentiality and nondisclosure agreements to protect their confidential information and data. Effective protection of confidential information and data, however, includes not only having confidentiality and nondisclosure agreements in place, but also having comprehensive policies and procedures regarding confidential information and data.
2. Confidentiality/Non-Disclosure agreements generally include the following provisions:
  - a. The parties to the agreement (business entities or individuals).
    - i. If a Confidentiality/Non-Disclosure agreement is signed by someone who does not have the power to execute a binding agreement, it could potentially invalidate the agreement.
    - ii. If the Confidentiality/Non-Disclosure agreement is entered into by a business entity, it is important to ensure that the correct legal name of the business entity is used in order to bind the correct party.
  - b. The business purpose of the agreement.
    - i. Identifying a business purpose limits the disclosure or exchange of confidential information to the specified business purpose.
  - c. The definition of confidential information.
    - i. Confidential information should be defined broadly enough to cover all of the confidential information that may be disclosed and to identify the type of information that is confidential. However, confidential information should not be so broadly defined that it is unenforceable.
  - d. Identification of what is excluded from the definition of confidential information.



- i. Generally information that is or becomes public other than through breach of the agreement, was already in the recipient's possession or was available to the recipient on a non-confidential basis prior to disclosure, is received from a third party not bound by the confidentiality agreement, or is independently developed by the recipient without use of the confidential information is excluded from the definition of confidential information.
  - e. Use and access restrictions.
    - i. Access to the confidential information may be restricted even within a business entity, such as, to those employees who have a "need to know."
  - f. Safekeeping and security requirements.
    - i. The Confidentiality/Non-Disclosure agreement may identify the manner in which the confidential information is stored, including, network security protections.
  - g. The term of the agreement and any survival provisions.
    - i. A Confidentiality/Non-Disclosure agreement may be perpetual or terminate on a specified date or event. If the agreement terminates on specified date or event, a set period can be defined during which the nondisclosure obligations remain in effect after expiration of the agreement.
  - h. Provisions relating to return or destruction of confidential information.
    - i. Intellectual property rights.
      - i. Confidentiality/Non-Disclosure agreements generally provide that the disclosing party retains the intellectual property rights in the confidential information being disclosed and disclaims any license to the recipient.

**G. Advertising Breweries and Distilleries: Mandatory Statement Challenges.**

- 1. The Alcohol and Tobacco Tax and Trade Bureau ("TTB") defines "advertisement" as any written or verbal statement, illustration, or depiction, which is in, or calculated to induce sales in, interstate or foreign commerce, or is disseminated by mail. 27 C.F.R. § 7.51.

- a. The definition includes any written, printed, graphic, or other matter accompanying the container; markings on cases, billboards signs, or other outdoor display; and broadcasts made via radio, television, or in any other media. *Id.* Examples include ads in newspapers or magazines, trade booklets, menus, wine cards, leaflets, circulars, mailers, book inserts, catalogs, promotional materials, or sales pamphlets. *Id.*
2. Advertisements for malt beverages need to include the following information:
- a. Name and address (city and State) of the permittee responsible for the advertisement; and
  - b. Class to which the product belongs, corresponding with the information shown on the approved label, *e.g.*, lager, ale, stout. 27 C.F.R. § 7.52.
3. The TTB also identifies what may not be included in advertisements for malt beverages. See 27 C.F.R. § 7.54 for a complete list of prohibited statements. From a trademark perspective, the most applicable prohibitions are:
- a. No names that are misleading with respect to the characteristics of the product;
  - b. No statements that are disparaging of a competitor's product; and
  - c. No statements, designs, devices or representations that are obscene or indecent.
4. The TTB monitors the advertising of malt beverages through pre-clearance of advertising materials, referrals and/or complaints and internal selections for review.
- a. The TTB offers business owners a voluntary, free of charge advertising pre-clearance service in which the TTB reviews an advertisement for compliance with applicable advertising regulations.

**Difficulties in Obtaining the Correct Licenses and  
Permits (Onerous Filings With the TTB, FDA, IRS,  
SEC and State and Local)**

**Submitted by Jeffrey C. O'Brien**



**Difficulties in Obtaining the Correct Licenses and  
Permits**

**Submitted by Jeffrey C. O'Brien  
Chestnut Cambronne PA**

## **The Regulatory Framework at the Local, State and Federal Levels**

### **A. Federal**

#### **i. Alcohol and Tobacco Tax and Trade Board (TTB)**

- a) The Alcohol and Tobacco Tax and Trade Board (TTB) regulates craft beer at the federal level. (Brew Law 101 at 59).
- b) Anyone brewing beer for sale must obtain a Brewer's Notice from the TTB. You can find the form online at their website but be aware the process can take on average 129 days. *Id.*
- c) The application requires a heavy amount of paperwork, including personal information for every officer, director, and shareholder who holds at least 10% interest in the company. *Id.*

#### **ii. Food and Drug Administration (FDA)**

- a) Federally regulates any "facility that manufactures, processes, packs, or holds food or beverages – including alcoholic beverages – for consumption in the United States." *Id* at 60.
- b) You must register with the FDA biannually, but there is no fee involved. *Id.*

### **B. State**

- i. Need to register with the Secretary of State to obtain a tax ID.
- ii. If you are 10 or more days late in filing or paying your taxes, you will be placed on the public Tax Delinquency Liquor Posting List. Being on this list means that no wholesaler, manufacturer, or brewer can sell or deliver any product to you. You cannot purchase beverages for resale if you are on the list. The state also has the power to revoke or deny a renewal of license.
- iii. Wholesaler/Manufacturer's Intoxicating Liquor License
  - a) In Minnesota, a brewery must obtain this license. This license must be renewed annually. Takes 30 days to process and can cost anywhere from \$20 - \$15,000 depending on the type of facility or license.
  - b) Requirements:

1. \$10,000 Surety Bond;
2. Be at least 21 years old;
3. Has not had a licensed issued under Minn. Stat. § 340A revoked within the past years; and
4. Not been convicted of a felony within the past 5 years or any willful violation of federal, state, or local ordinances governing the manufacture, sale, distribution, or possession for sale of distribution of alcoholic beverages.

**C. Local**

**a) Growlers**

**b) Tape Rooms/ Cocktail Rooms**

**State and Federal Registration Requirements**

**A. State-Level Registration**

**i. State Licensing Issues**

- a) While the TTB's licensing requirements and regulations apply for breweries and distilleries in any state within the U.S., state and local laws vary by jurisdiction.

**ii. Top Permitting/Licensing Issues**

- b) First and foremost, it is imperative to understand what permits and licenses must be obtained at each level of government before operations can legally begin.
- c) At the Federal level, when you are seeking a brewer's notice or distilled spirits plant license, be sure that your application is complete and accurate, as incomplete applications will not be reviewed and will ultimately be dismissed.
- d) At the state level, be aware of which agency or agencies are responsible for reviewing your application and provide such agency/agencies with all required and requested documentation in order to ensure expeditious review and approval.
- e) It is also imperative to understand what local requirements exist as to the brewery or distillery, be they taproom/cocktail room licenses or other issues

(such as growler sales restrictions and/or garden variety land use/zoning requirements).

#### **D. Navigating TTB Labeling Regulations – and Landmines to Avoid!**

- i. **TTB:** At the federal level, breweries and distilleries are regulated via the Alcohol Tobacco Tax and Trade Bureau, an agency falling under the U.S. Department of Treasury. Commonly referred to as the “TTB”, this agency grew out of the Bureau of Alcohol, Tobacco, Firearms and Explosives (“ATF”) in 2003. The TTB handles all federal liquor law issues including tax revenues, permits, licenses, tax audits, trade investigation and labels.
- ii. **Navigating Local, State and Federal Rules, Regulations and Requirements:** While the TTB’s licensing requirements and regulations apply for breweries and distilleries in any state within the U.S., state and local laws vary by jurisdiction.

#### **iii. State and Federal, TTB Registration Requirements**

##### **a. Federal**

1. The TTB requires anyone brewing beer for sale to acquire a Brewer’s Notice. Historically, the process for obtaining a Brewer’s Notice through the TTB was time consuming, but with the recent craft brewing and distilling boom, the TTB has streamlined the process through its Permits Online site, <https://www.ttonline.gov/permitonline>.
2. Information and documents to be submitted to the TTB in connection with the Brewer’s Notice application include the following:
  - Articles of Organization (LLC) / Articles of Incorporation Corp.)
  - Operating Agreement (LLC) / By Laws (Corp.)
  - Federal EIN (from IRS)
  - Owner Officer Questionnaires (for each owner of 10%+ and each officer)
  - List of all owners and officers identifying percentage of voting ownership, amount of funds invested, etc. (if owner is an entity, EIN)



- Source of Funds Documents (bank statements, loan documents, etc.)
- Diagram of Premises
- Description of Property (usually metes & bounds is best)
- Description of Equipment (more reviewers are requiring this, at least provide size of tanks)
- Description of the Building (walkthrough of the brewery premises)
- Environmental Questionnaire (number of employees, amount of waste, disposal of liquid and solid waste, electric/gas provider name, etc.)
- Supplemental (disposal of waste into navigable waterways, etc.)
- Brewer's Bond
- Consent of Surety (if using a non-contiguous warehouse, alternating premises between a brewery and a distillery, running an alternating proprietorship, etc.)
- Lease agreement or mortgage (with permission to use premises as a brewery/distillery)
- Assumed name registration (if applicable)
- Security statement
- Designation of a main contact person
- Copy of ID for main contact person
- Signing authority resolution for application contact
- TTB's Signing Authority Form
- Power of attorney (if being filed by an attorney)
- Other (historic buildings, variance request, etc.)

3. Similarly, anyone seeking to produce distilled spirits must obtain a distilled spirits plant license through the TTB with similar requirements as for the Brewer's Notice.

**b. State Licensing Issues**

- i. While the TTB's licensing requirements and regulations apply for breweries and distilleries in any state within the U.S., state and local laws vary by jurisdiction.

### **c. Formula Approvals**

#### **i. Beer Formulas**

1. Beers do not typically require a formula approval, unless they contain a non-traditional beer ingredient or are made using a non-traditional brewing method.
2. In 2015, TTB issued a ruling broadly expanding the definition of "traditional." Under the new rule, traditional ingredients and processes have been expanded, and are listed in the attachment on the next page.
3. If the beer includes a "non-traditional" fruit, spice (e.g., elderberry), or "sweetener" (e.g., aspartame), or contains a coloring (e.g., Blue No. 1), flavoring (e.g., an extract), or TTB limited ingredient (e.g., calcium chloride), or is made by a "non-traditional" process (e.g., "ice distilling"), the beer requires a TTB formula approval before TTB will issue a COLA approval. For more information on ingredient issues, see Appendix 1.

#### **ii. Spirits formulas**

1. Most traditional spirits do not require a formula approval, unless they contain a restricted product (e.g., thujone), or are infused with flavors or colored. Occasionally, a product must also be sent in to TTB's lab for analysis. Lab analysis is more typically required for imported products to make sure certain requirements are met. TTB's chart is attached hereto as Appendix 2, which shows if/when formula and/or laboratory approval is required for a distilled spirits product prior to label submission.

#### **iii. Labeling**

1. Another integral responsibility of the TTB is to regulate and approve labels for packaging beer and spirits. Section 105(e) of the Federal Alcohol Administration Act (27 USC 205(e)) authorizes the Secretary of the Treasury to issue regulations regarding product labeling that:
  - (1) ensure that consumers are provided with adequate information as to the identity and quality of alcohol beverages, and

- (2) prevent consumer deception. The Secretary has delegated to the Alcohol and Tobacco Tax and Trade Bureau (TTB) authority to administer the regulations promulgated under section 105(e). Section 105(e) and the TTB regulations require a Certificate of Label Approval (“COLA”) for each alcohol beverage product regulated by the agency. TTB issues COLAs on TTB Form 5100.31.

2. First, you must register for the COLA’s. Appendix 3 contains instructions on how to successfully register using the online system. If you choose not to file electronically, you must TTB Form 5100.3, in duplicate form, to the following address:

Advertising, Labeling and Formulation Division  
Alcohol and Tobacco Tax and Trade Bureau  
1310 G Street, NW, Box 12  
Washington, DC 20005

3. A copy of Form 5100.3 is included at Appendix 4.
4. NOTE: You must obtain label approval prior to bottling if you are shipping out of state.
5. For many alcohol beverage products, TTB requires a product evaluation to determine whether a proposed label identifies the product in an adequate and non-misleading way. Pre-COLA product evaluation entails a review of a product’s ingredients and formulation and also may include a laboratory analysis of the product. Laboratory analysis involves a chemical analysis of a product.
6. Such pre-COLA product evaluations ensure that:
  - No alcohol beverage contains a prohibited ingredient.
  - Limited ingredients are used within prescribed limitations or restrictions.
  - Appropriate tax and product classifications are made.

- Alcohol beverages labeled without a sulfite declaration contain less than 10 parts per million (ppm) of sulfur dioxide.
7. The type of pre-COLA product evaluation required for a particular product depends on that product's formulation and origin. TTB regulations require formulas most commonly when flavoring or coloring materials are added. Field investigations can be used to verify the accuracy of these documents. Since TTB does not have access to foreign plants, some imported products are subject to laboratory analysis or pre-import letter approval.
  8. The relevant Federal regulations for labeling and advertising of malt beverages can be found Part 7 of Title 27 of the Code of Federal Regulations. Processing times for COLA's can be found : <https://www.ttb.gov/labeling/processing-times.shtml>.

**§7.11 Use of ingredients containing alcohol in malt beverages; processing of malt beverages**

*(a) Use of flavors and other nonbeverage ingredients containing alcohol—*

- i. (1) *General.* Flavors and other nonbeverage ingredients containing alcohol may be used in producing a malt beverage. Except as provided in paragraph (a)(2) of this section, no more than 49% of the overall alcohol content of the finished product may be derived from the addition of flavors and other nonbeverage ingredients containing alcohol. For example, a finished malt beverage that contains 5.0% alcohol by volume must derive a minimum of 2.55% alcohol by volume from the fermentation of barley malt and other materials and may derive not more than 2.45% alcohol by volume from the addition of flavors and other nonbeverage ingredients containing alcohol.
- ii. (2) In the case of malt beverages with an alcohol content of more than 6% by volume, no more than 1.5% of the volume of the malt beverage may consist of alcohol derived from added flavors and other nonbeverage ingredients containing alcohol.

(b) *Processing.* Malt beverages may be filtered or otherwise processed in order to remove color, taste, aroma, bitterness, or other characteristics derived from fermentation.

#### **iv. Labeling Requirements**

**Permission to Re-label:** Application for permission to re-label shall be accompanied by two complete sets of the old labels and two complete sets of any proposed labels, together with a statement of the reasons for relabeling, the quantity and the location of the malt beverages, and the name and address of the person by whom they will be relabeled.



## **Other Issues**

**Submitted by Sarah B. Bennett and Jeffrey C. O'Brien**





## **Other Issues**

**Submitted by Jeffrey C. O'Brien  
Chestnut Cambronne PA**

## **A. Labeling Challenges**

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- iii.** A copy of Form 5100.3 is included at Appendix 4.
- iv.** NOTE: You must obtain label approval prior to bottling if you are shipping out of state.
- v.** For many alcohol beverage products, TTB requires a product evaluation to determine whether a proposed label identifies the product in an adequate and non-misleading way. Pre-COLA product evaluation entails a review of a product’s ingredients and formulation and also may include a laboratory

analysis of the product. Laboratory analysis involves a chemical analysis of a product.

- vi.** Such pre-COLA product evaluations ensure that:
- No alcohol beverage contains a prohibited ingredient.
  - Limited ingredients are used within prescribed limitations or restrictions.
  - Appropriate tax and product classifications are made.
  - Alcohol beverages labeled without a sulfite declaration contain less than 10 parts per million (ppm) of sulfur dioxide.
- vii.** The type of pre-COLA product evaluation required for a particular product depends on that product's formulation and origin. TTB regulations require formulas most commonly when flavoring or coloring materials are added. Field investigations can be used to verify the accuracy of these documents. Since TTB does not have access to foreign plants, some imported products are subject to laboratory analysis or pre-import letter approval.
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## **B. Choosing Distributors Carefully and Distribution Agreements**

## **State Distribution Laws**

### **Franchise Laws**

A majority of the states have enacted full-fledged beer franchise laws. Although it is not hard to detect a whiff of protectionism in these enactments, their stated purpose is to correct the perceived imbalance in bargaining power between brewers (who are presumed to be big and rich) and wholesalers (who are presumed to be small and local). Temperance concerns are also cited. A full-fledged beer franchise law will usually:

- Define franchise agreements to include informal, oral arrangements, making any shipment to a wholesaler the start of a franchise relationship.
- Prohibit coercive brewer practices, most often including actions in which a brewer (a) requires the wholesaler to engage in illegal acts, (b) forces acceptance of unordered beer, or (c) withholds shipments in order to impose terms on the wholesaler.
- Require “good cause” or “just cause” before a brewer can terminate a wholesaler.
  - The burden is generally on the brewer to demonstrate cause for termination.
  - “Good cause” is usually defined to include a significant breach of a “reasonable” and “material” term in the parties’ agreement.
- Dictate that a brewer give prior written notice (60 or 90 days is common) to a wholesaler before termination is effective, with the notice detailing the alleged deficiencies that justify termination.

- Grant wholesalers an opportunity to cure the deficiencies alleged in a termination notice, with termination ineffective if a wholesaler cures the defect(s) or presents a plan to cure the defect(s).
  - “Notice-and-cure” requirements usually are waived under certain circumstances. These most often include a wholesaler’s (a) insolvency, (b) conviction or guilty plea to a serious crime, or (c) loss of a license to do business. Many franchise laws also permit expedited termination where a wholesaler (d) has acted fraudulently or (e) has defaulted on a payment under the agreement despite a written demand for payment.
- Require wholesalers to provide brewers with notice of any proposed change in ownership of the wholesaler, giving the brewer an opportunity to object. The brewer’s approval of an ownership change cannot be “unreasonably” withheld.
  - Brewers usually have little or no right to block a transfer to a previously designated family successor.
- Create remedies for unfair termination, generally granting wholesalers the right to receive “reasonable compensation” following termination.
  - Most beer franchise laws grant wholesalers the right to seek an injunction that, if granted, would quickly halt termination proceedings pending the resolution of wrongful termination claims. The forum for such relief can be either a state court or the state’s alcohol control authorities.

- Although arbitration of the entire dispute is not required, and sometimes prohibited, disputes over what constitutes “reasonable compensation” often must be arbitrated at the request of a party.
- Even if the franchise law prohibits arbitration, an arbitration clause in the parties’ written agreement is likely enforceable under the Federal Arbitration Act if the parties reside in different jurisdictions.
- Declare any waiver of franchise law protections void and unenforceable.
- Set a date that the law becomes effective. Some franchise agreements may predate franchise acts’ effective dates, likely making the franchise law inapplicable to that agreement.

In addition to the extremely common provisions described above, other terms may:

- Require beer franchise agreements to be in writing.
- Mandate that sales territories be exclusive.
  - Wholesalers may face substantial penalties for making deliveries outside their designated territory, and such conduct may permit expedited termination by the brewer.
  - Territorial designations may need to be filed with state liquor control authorities.
- Restrict a brewer’s ability to dictate prices, with restrictions that often go beyond the strictures of antitrust law. Common provisions prohibit brewer

price fixing, require brewers to file and adhere to periodic price schedules, and ban price discrimination between wholesalers within the state.

- Provide that the prevailing party in a termination dispute will be compensated for its attorneys fees.
- Bind succeeding brand owners to existing franchise agreements, although some permit not-for-cause termination after a change in brand ownership, as long as compensation is paid.
- Impose a good faith obligation on both parties. Under modern contract law, this good faith obligation is already implied in all contractual relations.
- Impose specific obligations on wholesalers, occasionally specified to include a duty to properly rotate stock, maintain tap lines, and comply with other reasonable quality control instructions.

Most states have enacted at least a few laws that regulate brewer-wholesaler relations. In some, beer wholesalers are covered by a franchise law protecting all alcohol beverage wholesalers. In a few states, beer wholesalers are protected by franchise laws that apply to a variety of franchise relationships, from beer to burgers. Still others partially regulate beer franchise relationships through their alcohol control laws by, for example, requiring exclusive territories as a condition for licensing. Finally, a few states and the District of Columbia have, to date, left brewer-wholesaler relations essentially unregulated, thereby allowing the franchise relationship to be governed exclusively by the terms of the parties' agreement, to be enforced under general contract law principles. **Self-Distribution**

Many states permit breweries below a certain production threshold to distribute their product directly to retailers without the use of a distributor. While self-distribution can be a viable means around the complex and onerous franchise laws, the time and capital required to operate an effective distribution system is significant and tends to detract from other operations. Further, breweries that grow beyond the production thresholds are forced into the franchise system as they lose their rights of self-distribution.

#### **D. Neglecting Labor and Employment Issues**

Most states provide that employees are “at will” employees; that is, they can leave their employment whenever they wish, for any reason or no reason. If a business owner has a key employee that is integral to its success, that employee should have a written employment agreement that provides for a fixed term of employment. A covenant not to compete can be included to deter a key employee from leaving to work for a competitor. Absent this type of agreement, the key employee can leave at any time.

A written employment agreement is imperative for your head brewer who knows a brewery’s formulas could do the most damage to the business working for the competition. Hence, a master brewer employment agreement should include a covenant not to compete and provisions that clearly state that the beer formulas are “trade secrets” and thus the property of the brewery.

Covenants not to compete must be narrowly tailored to balance the interests of employer and employee. The employer must show (i) the covenant not to compete was supported



by consideration when it was signed (if the consideration for the covenant is the continued employment of the employee, then the covenant must be signed prior to the start of employment to be valid); (ii) the covenant protects a legitimate business interest of the employer; and (iii) the covenant is reasonable in duration and geographic scope to protect the employer without being unduly burdensome on the former employee's right to earn a living.

### **Use of “Volunteers”**

Many breweries take advantage of the abundance of people interested in helping their business grow by allowing them to volunteer at the brewery. Depending upon the nature of the duties they are performing, classifying an individual who ought to be treated – and compensated – as an employee as a “volunteer” can lead to significant penalties under Minnesota and federal law. In the past few years as both state and federal government have tried to get more revenue, they have focused on going after employers for misclassification of workers, whether they be independent contractors, interns or the use of volunteers.

### **Minnesota Law:**

There is a presumption anyone performing work for a “for-profit” enterprise is an employee. In Minnesota, the nature of the employment relationship is determined by using worker classification tests, similar to the manner in which employee status is determined under both workers’ compensation and unemployment insurance laws.

Compensation of Minnesota employees is determined under Minn. Stat. § 181.722, Subd. 3, and the federal Fair Labor Standard Act. Correctly assessing a worker as an employee, student/intern, independent contractor, or volunteer is critical.

Minnesota Statute Section 177.23 governs the use of volunteers. Minn. Stat. §177.23, Subd. 5 states that "Employ" means "to permit to work", and Subd. 6 states that an "Employee" means any individual employed by an employer, subject to certain enumerated exceptions. There is an exception for "any individual who renders service gratuitously for a nonprofit organization", but there is no exception for an individual who renders service gratuitously for a for-profit organization.

**Federal Law:**

The Fair Labor Standards Act (FLSA) defines employment very broadly, i.e., "to suffer or permit to work." However, the Supreme Court has made it clear that the FLSA was not intended "to stamp all persons as employees who without any express or implied compensation agreement might work for their own advantage on the premises of another." In administering the FLSA, the Department of Labor follows this judicial guidance in the case of individuals serving as unpaid volunteers in various community services. Individuals who volunteer or donate their services, usually on a part-time basis, for public service, religious or humanitarian objectives, not as employees and without contemplation of pay, are not considered employees of the religious, charitable or similar non-profit organizations that receive their service. Members of civic organizations may help out in a sheltered workshop; men's or women's organizations may send members or students into

hospitals or nursing homes to provide certain personal services for the sick or elderly; parents may assist in a school library or cafeteria as a public duty to maintain effective services for their children or they may volunteer to drive a school bus to carry a football team or school band on a trip. Similarly, an individual may volunteer to perform such tasks as driving vehicles or folding bandages for the Red Cross, working with disabled children or disadvantaged youth, helping in youth programs as camp counselors, scoutmasters, den mothers, providing child care assistance for needy working mothers, soliciting contributions or participating in benefit programs for such organizations and volunteering other services needed to carry out their charitable, educational, or religious programs.

Under the FLSA, employees may not volunteer services to for-profit private sector employers. On the other hand, in the vast majority of circumstances, individuals can volunteer services to public sector employers. When Congress amended the FLSA in 1985, it made clear that people are allowed to volunteer their services to public agencies and their community with but one exception - public sector employers may not allow their employees to volunteer, without compensation, additional time to do the same work for which they are employed. There is no prohibition on anyone employed in the private sector from volunteering in any capacity or line of work in the public sector.

**Student/Interns:**

Until recently, student/interns have not received the same close scrutiny as other groups of workers. Student/interns are not considered employees under both state and federal

law, if their use in the workplace generally passes six tests offered by the Department of Labor. The tests are:

1. The training experience is similar to what is provided at school;
2. The training experience is for the benefit of the student/interns;
3. The student/interns do not displace regular employees;
4. The employer providing the training receives no immediate advantage from the activities of the trainees;
5. Student/interns are not necessarily entitled to a job at the conclusion of the training; and
6. The employer and the student/interns understand the work is unpaid training.

Whether an employment relationship exists is not always clear. Instead, whether an intern or trainee is entitled to such things minimum wage and overtime compensation will often depend upon whether the individual is receiving training without displacing other employees or providing any real benefit to the employer. (Note: a reasonable stipend may be permitted)

**Independent Contractor:**

Independent contractors are hired to perform special services of a limited scope and duration, and they typically perform the same services for a variety of businesses. The standards in Minnesota to be considered in determining whether or not an individual is an

employee or an independent contractor depend upon the purpose for which such classification is to be considered but typically include factors such as:

1. The right to control the means and the manner of performance;
2. The mode of payment;
3. The furnishing of materials or tools;
4. The control of the premises where the work is done; and
5. The right of the employer to discharge the individual.

Generally, the more control, or right of control, an employer has over the individual performing the work, the work site, and the nature, quality, and manner in which work is performed, the more likely the relationship is an employer-employee relationship vs. an independent contractor arrangement.

## **E. Navigating the Complex Legal, Regulatory, and Policy Landscape**

### **i. Critical Recordkeeping, Production and Inventory Mistakes**

- a. Software options available to assist with record keeping - Only as accurate as the data entered
  1. Maintain daily records of activity
  2. Keep track of inventory adjustments
  3. Account for waste and disposal of product
  4. Have controls in place to ensure information entered and pulled for reporting is timely — i.e., daily rather than weekly
  5. Records should be retained for a minimum of 3 years

- b. Most common daily recordkeeping mistakes
  - 1. Accurately report the amount of beer returned to the brewery
  - 2. Properly maintain records regarding destruction of beer
  - 3. Appropriately record lab sample removals
  - 4. Appropriately report, record, or maintain supporting documents regarding losses or shortages
- c. Inventory Remedy
  - 1. Take inventory of product on the first of each month
  - 2. Document the inventory count(s)
  - 3. Required information:
    - a. Date taken
    - b. Quantity of beer and cereal beverage on hand;
    - c. Losses, gains, and shortages; and
    - d. Signature — under penalties of perjury — of the brewer or person taking inventory

**ii. Frequent Mishaps: Tanks and Measuring Devices**

- a. Recording beer that is removed for lab samples
- b. Every tank, vat, cask, or other container that a brewer uses or intends to use as a receptacle for wort, beer, or concentrate must be "durably marked with a serial number and capacity."
- c. All measuring devices must be tested periodically
- d. Records of these tests must be made available to TTB officers upon inspections
- e. Records required:
  - 1. Date of test
  - 2. Identification of device(s) tested
  - 3. Test results

4. Any corrective actions (adjustment/repair) taken

**iii. Conversion Factors in Calculating Barrel Equivalent Amounts**

- a. 1 Barrel (bbl) = 31 gallons
- b. 1 US Keg = 15 gallons
- c. 1 US sixtel (pony keg) = 5.166667 gallons
- d. 1 US case of beer = 2.25 gallons

**iv. Excise Tax Returns, Computation of Tax and Determination Mistakes**

- a. Tax is calculated on the beer which is reported to be removed for consumption or sale in the United States
- b. Reported tax amounts should match Brewer's Report of Operations
- c. Any adjustments should be documented/explained in the appropriate section on form

**v. Brewer's Report of Operations (BROP)- Top Blunders and Tips**

- a. Required form to report operations such as:
  - 1. Inventory levels
  - 2. Production and waste amounts
  - 3. Packaging amounts
  - 4. Removals of product
- b. Timely records are required to ensure reported data is accurate

**F. Difficulties in Choosing to Lease or Purchase Real Estate**

**i. Distribution Space Leases**

- i. As the old cliché goes, in real estate it's all about "location, location, location", and this is especially true for a brewery or distillery business.

If you're looking to be the neighborhood hangout complete with a taproom (for breweries) or cocktail room (for distilleries), you'll need to find a suitable space close to home. Should you have larger ambitions, you may seek a more strategic location amenable to later expansion. Whatever the case may be, you'll need to have a space secured in order to complete the licensing process.

- ii. A new brewery or distillery owner will most likely lease a building at the start, and negotiating a suitable lease is a crucial step in the process.
- iii. Commercial lease agreements typically come in one of two varieties: "triple net" and "gross."
- iv. In a triple net, the tenant pays rent to the landlord, as well as a pro rated share of taxes, insurance and maintenance expenses. In the typical triple net lease, the tenant pays a fixed amount of base rent each month as well as an "additional rent" payment which constitutes 1/12 of an estimated amount for taxes, insurance and maintenance expenses (also called CAM or common area maintenance expenses). At the end of the lease year, the estimated amounts are compared to actual expenses incurred and adjusted depending upon whether the tenant paid too much or too little through its monthly payments.
- v. In a "gross" lease, the landlord agrees to pay all expenses which are normally associated with ownership. The tenant pays a fixed amount each month, and nothing more.



## **G. Challenges in Satisfying Equipment and Inventory Needs**

### **H. Complicated Insurance and Liability Matters**

Breweries and distilleries, like most businesses, face a myriad of insurance requirements. In addition to the surety bond required to obtain their license, breweries and distillers will need several types of coverages including:

- General liability insurance;
- Workers compensation; and
- Dram shop (if the business is serving alcohol for on-premise consumption).

With respect to general liability coverage, given the growth in breweries and distilleries and the increase in trademark and other intellectual property related disputes, it is imperative to carry coverage for these issues.

Many insurance companies now have special “craft brewery programs” which provide breweries with a package tailored to the needs of the industry.



# **Ethical Challenges**

**Submitted by Gary K. Luloff**



# **Ethical Challenges**

**Submitted by Gary K. Luloff  
Chestnut Cambronne PA**

## **A. Business Law Ethical Issues**

Ethical issues facing businesses generally fall into four categories: (i) health and safety; (ii) technology; (iii) transparency; and (iv) fair working conditions.

### **i. Health and Safety**

The Department of Labor has taken steps to protect the health and safety of employees in the United States in the form of the Occupational Safety and Health Administration and The Fair Labor Standards Act. However, these agencies have limitations, leaving businesses with flexibility in the level of health and safety measures taken to protect their employees. This flexibility often presents ethical issues due to the high costs of health and safety safeguards. Management is presented with choosing between additional health and safety protections and expense control.

Although a business must comply with OSHA and the FLSA, in many situations, a business should go beyond the mandated health and safety requirements to protect their employees. For example, an office that requires employees to stand or sit all day, should take additional steps to ensure the health and safety of such employees, such as ergonomic chairs or cushioned flooring. A business that ignores these issues or cuts corners to save money is arguable engaging in unethical behaviors in the business environment.

Another health issue arises from the environmental impact of a business. Many believe that a business has a responsibility to protect the environment in which it operates and such beliefs have driven governmental regulations. However, some discretion is still given to the companies to determine the level of environmental impact it will have. Management is often conflicted because of the high costs associated with limiting a business's environmental impact. For example, waste management presents a tough issue for many companies, as less eco-friendly waste disposals cost less than the more eco-friendly options. Another example is eco-friendly supplies, which costs more than normal supplies that a business might ordinarily purchase.

However, there are some clear ethical lines, which if crossed, result in blatant ethical violations, such as wrongful disposal of toxic waste and water pollution violations. Aside from

these few exceptions, the ethical line for environmental impact may differ between companies, therefore, each company needs to determine what they feel is ethical for their industry and location.

ii. Technology

Technological advances have resulted in a slew of new ethical considerations for businesses. Although technology allows businesses to compete on a higher level, in some areas technology infringes on individual rights, creating an ethical issue. Privacy laws have been passed to help limit this infringement; however, many companies still struggle with this ethical dilemma.

The most common ethical violation regarding technology results from privacy issues. This area has been clearly identified as a pedestal for unethical business behavior. Through the use of technology companies have the ability to track Internet usage and consumer buying habits, as well as collect personal information about customers or potential customers. Some restrictions have been passed to limit the type of information that may be collected and stored; however, ultimately each company must determine what level of collection and retention they feel is ethical.

Another ethical violation concerning technology results from security issues. Companies have the ability to monitor employees and visitors, collecting information for which the company states is for security. This includes monitoring employees' activities as well as constant recording from security cameras. To be clear, there is a level of surveillance that is ethically acceptable and has been tolerated for the sake of security. However, companies need to determine what level of monitoring they find ethical, which is often based upon the level of monitoring for which a company can justify. However, it is difficult to justify extensive monitoring of non-employees, therefore, it has been generally accepted that the surveillance of non-employees should be limited to a lower level than that of employees to be considered ethically acceptable.

Lastly, businesses are faced with ethical issues arising from the monitoring of communications. With today's technology, companies can easily monitor typical methods of

digital communications such as e-mails or text messages. For example, one computer program can scan the text of millions of messages looking for specific designated words. Once those words are flagged, the program can identify the sender. Companies using this type of technology must consider the ethical issues that arise with this level of surveillance and it has become difficult for companies to justify this level of intrusion as ethical, without the knowledge or explicit agreement of employees. Therefore, to limit ethical violations, a company should only conduct a level of monitoring or surveillance for which the company can justify as necessary for the business.

### iii. Transparency

Transparency has become imperative to maintaining an ethical image in society. With the number of business scandals, the public has become weary to trust companies, requiring businesses to transition into a more transparent and open operational structure. This change requires companies to maintain honesty and complete accurate and comprehensive financial reports. However, this has continuously been an area of numerous ethical violations, including violations for fraud, conflicts of interest, lying, insider trading, and bribery.

Typically, these types of violations occur due to managements errors in putting their own interests ahead of those of the company. For example, violations for conflicts of interest occur from choosing personal gains over the well-being of the organization. Bribery is another example, where such actions might result in an immediate gain for the individual or even the organization, but such behavior exposes the organization to legal recourse from the U.S. government. Another common example of an individual putting their own interests ahead of the company's is insider trading, which occurs when an officer, who has information that is not available to the public, uses such information as a basis for buying or selling stock.

### iv. Fair Working Conditions

Although businesses are required by law to provide a certain degree of fair working conditions, gaps in legislation still provide large discretion to management. Unfortunately, this creates an area of ethical unrest as responsible employee treatment also typically comes with increased costs. However, this is the price a company must pay to remain ethical in the eyes of



society. Typical violations in this area include the use of child labor, sweatshops, violations of basic worker rights, ignoring health and safety of employees, discrimination, intimidation, and harassment.

However, some ethical violations are easier to spot than others. For example, management can generally ensure that children are not being employed in their facilities; however, it is harder to identify if a supplier abides by those same requirements. Although it is no longer the initial company engaging in the unethical behavior, continuing to use such a supplier after knowing of the violations is arguably unethical. This can be a difficult decision for management as suppliers who engage in unethical behaviors such as sweatshops and child labor often can provide products at lower cost.

Another hard to define area is the use of harassment or intimidating behavior. This is a difficult area because people view these behaviors differently. What one person may find intimidating, another may find entertaining. Therefore, ethical violations may be more common than a company anticipates. Violations may also occur without being identified as unethical. For example, a company that is dominated mainly by males, who then hires a female who is outcaste or “given a hard time” may likely arise to unethical behavior. To limit such ethical violations a company must establish clear company policies that outline what behaviors are prohibited and encourage an open work environment that promotes communication.

Therefore, a company must think comprehensively about its operations to ensure ethical compliance. Although it may appear a company is acting ethically, you must look to the third-party affiliates of the company to fully determine the ethics of a company as well as the internal operations.

### **Intellectual Property Ethical Issues**

As discussed below, conflict checking is a huge issue for an IP attorney. The alcohol industry may seem large at first, but after time you will come across the same players over and over again through time. Conflict checking is especially important in trademark law, where you may file a trademark for one client that is similar to a mark registered or owned by another client.

Confidentiality is a hugely important issue for patents, trademarks, and trade secrets alike. Often times, even before entering into an attorney-client relationship, a client must provide some highly sensitive information to the attorney. For patents, it is necessary for the client to provide a description of the invention or design in order the attorney to provide an estimate for the work to be performed. For trademarks, a client will often need to provide the desired mark to the attorney before engagement so the attorney can do a conflict check of the mark against other client marks.

Fee structuring is particularly relevant for intellectual property attorneys, who often opt to price work on a fixed fee rather than on an hourly basis.

### **Alcohol Law Ethical Issues**

Some of the most important ethical issues relating to alcohol law include: (i) unauthorized practice of law; (ii) conflicts of interest; and (iii) disclosure and honesty in dealing with TTB.

#### **i. Unauthorized Practice of Law**

The alcohol industry is unique in that it is highly regulated at the federal, state, and local level. Clients need to comply with countless laws and regulations, and they often look to attorneys to help navigate these troubled waters. Clients that are planning to offer products in multiple states will need help drafting and negotiating agreements with wholesalers in different states, registering brands with the state, obtaining state licenses, and more. Also, attorneys in this niche industry often help clients throughout the country and world.

Each state has its own definition for what constitutes legal advice. The American Bar Association (“ABA”) weighs in with their model rule 5.5(a), “A lawyer shall not practice law in a jurisdiction in violation of the regulation of the legal profession in that jurisdiction, or assist another in doing so.

North Carolina, N.C. Gen. Stat. § 84-2.1, defines “practice law” as “performing any legal service for any other person, firm, or corporation, with or without compensation, specifically including the preparation or aiding in the preparation of deeds, mortgages, wills, trust instruments, ... or assisting by advice, counsel, or otherwise in any legal work.” North Carolina

does allow out-of-state attorneys to draft legal documents, so long as a North Carolina reviews and approves the documents. “Legal Documents” include any deed, mortgages, trust instrument, contract or any document filed in any court, quasi-judicial or administrative tribunal. It is not wholly clear from this language whether an application for a Brewery/ Distillery permit is considered a legal document.

One clue to help determine whether a task is considered practicing law: whether non-attorneys can and do perform the work in question. Regarding registrations and permitting at many state alcohol control boards, it appears that there are non-attorney businesses offering this type of assistance to breweries and distilleries. Accordingly, it seems that such assistance may not fall within the purview of “legal service” in some or many states.

Some attorneys avoid the unauthorized practice of law issue entirely by only handling federal issues (which an attorney barred in any state may do). ABA model rule 5.5(d)(2) provides that an out-of-state attorney may provide legal services in his/her home state to clients in another state, so long as those services are authorized by federal law. This is effective strategy for a great deal of trademark and patent work as well, which are largely federal issues. In order to traverse this path, it is necessary for attorneys to establish a wide network of attorneys to whom they can refer these clients for their out-of-state needs.

## ii. Conflicts of Interest

Aside from the general conversation below relating to conflicts of interest, there are a few specific issues that come up relating to the alcohol industry. The ABA model rule 1.7(a) provides that “a lawyer shall not represent a client if the representation involves a concurrent conflict of interest. A concurrent conflict of interest exists if: (1) the representation of one client will be directly adverse to another client; or (2) there is a significant risk that the representation of one or more clients will be materially limited by the lawyer’s responsibilities to another client, a former client or a third person or by a personal interest of the lawyer.”

For instance, one production model that is becoming more and more common in both the brewing and distilling industries is contract brewing. Under these arrangements, a host brewery/distillery will agree to produce a certain amount of a product on behalf of the brand

owner. A conflict arises where a host brewery refers a brand owner to their attorney to review their contract. In order to take on such a client, the attorney should first obtain the informed, written consent of both parties.

Another increasingly common arrangement is the alternating proprietorship (“AP”). In an AP, a host brewery/distillery will allow a tenant to operate a “virtual brewery/distillery” on their premises. A tenant brewery is required to obtain their own state and federal permits in order to operate. Conflicts (and potentially confidentiality issues) may arise where a tenant brewery asks you to assist with their permits, labels, formulas, and more. The solution here, again, is to make sure all parties provide their informed consent to the arrangement.

### iii. Disclosure and Honesty in Dealing with TTB

Pursuant to ABA model rule 3.3, a lawyer shall not make a false statement of fact or law to a tribunal (extended to cover representation in a non-adjudicative proceeding before an administrative agency, under model rule 3.9), offer evidence that the lawyer knows to be false, and take remedial measures to correct and avoid criminal or fraudulent conduct by a client.

Further, for all/most TTB forms and submissions, TTB requires a declaration that the signing party authorize, “Under the penalties of perjury, I declare that I have submitted this claim, including supporting documents and statements, and to the best of my knowledge and belief, it is true, correct, and complete.”

In light of the above, it will likely be an ethical violation for an attorney to make a submission to TTB, where the attorney knows that the content submitted is inaccurate. This would also apply the client has already signed declarations indicating that the content provided therewith is true.

This particular issue is becoming more and more relevant in this practice area with the increasing amount of legal disputes for false advertising. For instance, extra care should be taken to insure that a product with a label declaring the product is HAND MADE is actually made by hand. Also, extra care should be given to make sure products are MADE IN THE USA, produced by Contract Production Brewery X, and the like. While these are probably grey areas from a legal perspective, they are certainly relevant for the companies being sued for false or

misleading advertising under the Lanham Act.

### **Civil Liability**

The Model Code of Professional Responsibility, created by the American Bar Association, sets forth ethical rules to guide lawyers in their behaviors and to provide a process of discipline for those who act improperly. Although language prefacing the ethical rules indicates that such rules are not to be used to impose civil liability upon violators, the majority of courts hold that evidence of an ethical violation is admissible evidence in a malpractice action. The rules were created to establish a minimum level of competency and any actions falling beneath that minimum are evidence that the required standard of care required was breached. Therefore, evidence of an ethical violation can be used to demonstrate that the attorney breached the standard of care owed to its client. However, an ethical violation by itself will not establish a cause of action, but rather, it may be used as “some evidence” of malpractice.

However, an attorney may also be sued for numerous other violations, other than just ethical violations. One common cause of action that is presented in legal malpractice claims is a claim for negligence. To be successful, the client must establish that the attorney took some type of action that a prudent attorney would not have taken, or that the attorney failed to take some type of action that a prudent attorney would have taken. Negligence can arise in various ways, such as giving incorrect advice, failing to file documents, or the creation of a conflict of interest.

Another claim that may be brought against an attorney is for breach of fiduciary duty. When an attorney enters into an attorney-client relationship, the attorney becomes a fiduciary of the client, owing the client a duty of utmost good faith. Such good faith requires the attorney to place the client’s interest before his or her own interests, and prohibits the attorney from using his position to gain a profit at the expense of the client. In a business situation, a breach of fiduciary duty often arises if the attorney has a relationship or history with one of the parties to the transaction. Typically, when a corporation hires an attorney, an officer chooses an attorney that he or she knows or is familiar with. However, the attorney must remember that its fiduciary relationship is with the company and not the individual. As such, the attorney must

do what is best for the company, even if it is not in the best interest of the officer or person whom the attorney has a relationship with.

Another area that is increasingly becoming an area of concern is when attorneys invest in the business of the client. When this occurs, the attorney still keeps its fiduciary relationship with the client and therefore, must put the interest of the business first, even if it is to the detriment of the attorney's investment. For example, an attorney may need to advise its client to file bankruptcy, even knowing that he or she will lose the investment in the company. This inherently creates an ethical issue and opens the attorney up to malpractice claims.

### **Ethical Issues for CPA's**

CPA licenses are issued and governed by individual state boards. The American Institute of Certified Public Accountants is a member based organization which has a professional code of conduct.

## **B. The Role of the Attorney as Advisor in Entity Formation**

### **1. Duties Owed to Investors**

The duty an attorney owes to investors, if any, depends on the relationship created between the investor(s) and the attorney. The general rule is that an attorney owes a duty of care solely to an entity itself and not to its constituents; however, some courts have expanded this rule to include shareholders or members. See, e.g., *Evans v. Blesi*, 345 N.W.2d 775 (Minn. Ct. App. 1984).

The Model Rules of Professional Conduct dictate that “[a] lawyer employed or retained by an organization represents the organization acting through its duly authorized constituents” and “[i]n dealing with an organization’s directors, officers, employees, members, shareholders or other constituents, a lawyer shall explain the identity of the client when the lawyer knows or reasonably should know that the organization’s interests are adverse to those of the constituents with whom the lawyer is dealing.” Rules 1.13(a) & (f).

Failure to identify who the client is may result in unintended representation. A duty may arise to an investor if the attorney agrees to be an investor’s lawyer, or under tort theory, if the

investor reasonably believes the attorney to be his or her attorney. This belief can arise from casual conversations where advice is given, regardless of the attorney's intentions.

In addition, if the attorney is trying to obtain investors for the entity, an attorney may have securities law obligations to the investors. However, regardless of the attorney's role in obtaining investors, if the entity is seeking investors, it is the attorney's duty to inform the entity of its security law obligations when speaking to investors.

## **2. Conflicts Between Organizers**

The discussion of conflicts between organizers is founded on the identification of the client. The attorney must be clear in who he or she is representing. If prior to the formation of the entity, the attorney must identify whether one or more of the organizers is the client. If more than one organizer is being represented by the same attorney a potential conflict of interest exists. Therefore, the attorney must discuss the advantages and disadvantages of joint representation and obtain informed consent to the representation from the organizers. Once this is completed, the attorney must independently determine if he or she can effectively represent the clients. If the attorney represents more than one organizer, the attorney has a duty to each client and cannot play favorites. Also, there is no attorney-client privilege amongst the group, meaning that information told to the attorney by one organizer can be shared with the other organizer.

An attorney should also establish at the outset, whether he or she will represent the entity once it is formed. If the attorney will represent the entity, the attorney must obtain informed consent from the organizers and the entity agreeing to the representation despite the conflict of interest existing between the representation of both the organizers and the entity. However, if the attorney does not want to represent the entity, he or she should be clear in his or her intentions and the best way to do so is to send a non-representation letter to the entity.

## **3. Taking an Ownership Stake in Exchange for Services**

Taking an ownership stake in a company in exchange for legal services can be very risky for an attorney. Some business transactions between attorney and client are prohibited by ethical rules; however, even if the transaction is not prohibited by the rules, it is often not

advisable to engage in such agreements due to its complexity. The Model Rules of Professional Conduct state that:

“[a] lawyer shall not enter into a business transaction with a client or knowingly acquire an ownership, possessory, security or other pecuniary interest adverse to a client unless: (1) the transaction and terms on which the lawyer acquires the interest are fair and reasonable to the client and are fully disclosed and transmitted in writing in a manner that can be reasonably understood by the client; (2) the client is advised in writing of the desirability of seeking and is given a reasonable opportunity to seek the advice of independent legal counsel on the transaction; and (3) the client gives informed consent, in a writing signed by the client, to the essential terms of the transaction and the lawyer’s role in the transaction, including whether the lawyer is representing the client in the transaction. Rule 1.8(a).

Therefore, under Rule 1.8 of the Model Rules of Professional Conduct an attorney may only enter into a business transaction with a client if the transaction is fair to the client, the terms are fully disclosed in a clear manner to the client, the client is advised and given an opportunity to seek independent legal counsel for the transaction, and the client gives informed written consent to the terms of the transaction and the lawyer’s role in such transaction. If these elements are not met, an attorney is prohibited from taking an ownership stake in the company in exchange for services.

However, even if the transaction is permitted, it creates a significant ethical concern resulting from the potential conflict between the attorney’s financial investment and the client’s interest. In addition, the disclosure requirements set forth in Rule 1.8 of the Model Rules of Professional Conduct may be difficult to prove in the event of future litigation.

#### **4. Ethics of Company Valuation**

Goal is to choose an independent valuation authority who knows the specific industry. Specific qualities include:

- Integrity



- Objectivity
- Competence
- Confidentiality
- Professional Behavior

## **C. Conflicts of Interest**

### **1. Conflict Checking**

The Model Rules of Professional Conduct prohibit a lawyer from representing a client “if the representation involves a concurrent conflict of interest.” The rules provide that a concurrent conflict of interest exists if: “(1) the representation of one client will be directly adverse to another client; or (2) there is a significant risk that the representation of one or more clients will be materially limited by the lawyer’s responsibilities to another client, a former client or a third person or by a personal interest of the lawyer.” Rule 1.7(a). To avoid conflicts of interest attorneys should engage in a “conflicts check” prior to beginning representation of a client. A conflicts check generally involves reviewing a list of clients and cases to determine whether the attorney has represented parties in the past that have interests which are adverse to those of the potential client’s.

To successfully conduct a conflicts check an attorney must have a system in place to conduct the check. To do so, an attorney should begin building a database from the day he or she begins to practice. The attorney should maintain records of all clients and engagements, including at a minimum: (1) the name, address, and contact information of the person; (2) the date of intake; (3) the nature of the representation; (4) who authorized the engagement; and (5) the name, address, and contact information of all involved parties. The database should be updated regularly to ensure all information is up-to-date.

A conflicts check should occur prior to forming an attorney-client relationship; therefore, prior to initial consultations, the attorney should conduct a conflicts check. In addition, whenever a new party is added, a new attorney is added, or new witnesses are added a conflicts check should be conducted. Failure to do so may result in a conflict of interest going unnoticed and result in further legal issues.

However, even if a concurrent conflict of interest does exist, a lawyer may still represent a client. The Model Rules dictate that a lawyer may still represent a client, regardless of a conflict of interest, if:

“(1) the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client; (2) the representation is not prohibited by law; (3) the representation does not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal; and (4) each affected client gives informed consent, confirmed in writing.” Rule 1.7(b).

Therefore, an attorney may use the conflicts check to determine if a conflict exists and if a conflict is present, the attorney may still represent the client if the exceptions established in Rule 1.7(b) are met. In small communities or with attorney’s changing job positions more often, conflicts checks have become imperative, as well as the Rule 1.7(b) exceptions, to ensuring proper representation.

## **2. When Does A-C Relationship Attach**

Typically, an attorney-client relationship arises when “(1) a person manifests to a lawyer the person’s intent that the lawyer provide legal services for the person; and either (a) the lawyer manifests to the person consent to do so; or (b) the lawyer fails to manifest a lack of consent to do so, and the lawyer knows or reasonably should know that the person reasonably relies on the lawyer to provide the services . . . .” Restatement (Third) “The Law Governing Lawyers” § 14 (2000). Therefore, an attorney-client relationship may arise, without the attorney consenting to such relationship if the attorney fails to decline the representation.

Therefore, attorney-client relationships may form when an attorney believes he or she is simply giving casual legal advice. For example, an attorney who gives legal advice in a social setting, but does not make clear that representation has not begun, may have formed an attorney-client relationship. Another example, is when a lawyer provides advice and answers questions to a pro-se litigant. It is the lawyer’s responsibility to be clear about whether any representation has begun and if the lawyer fails to do so, an attorney-client relationship may

form.

Some attorneys rely on the false assumption that an attorney-client relationship fails to exist unless it is documented in writing. However, the relationship does not need to be documented in writing and may be created implicitly. Therefore, it is important for an attorney to protect itself against surprise relationships and accidental clients. To do so, an attorney may provide a letter declining representation. The letter expressly declines representation and makes clear that no representation has begun. Another safeguard is to expressly communicate to the person that representation has not begun and no attorney-client relationship has formed. However, this may still be difficult to prove in the future, therefore, it is best to put the communication in writing.

### **3. Duties Owed to Non-Clients**

A lawyer owes a fiduciary duty to the client and typically, that duty is not extended to non-clients. However, the Model Rules of Professional Conduct speak to an attorney's duties owed to a non-client, specifically a non-client that is a party to a matter in which the attorney is involved as representation for the opposing party. The Model Rules state that:

[i]n dealing on behalf of a client with a person who is not represented by counsel, a lawyer shall not state or imply that the lawyer is disinterested. When the lawyer knows or reasonably should know that the unrepresented person misunderstands the lawyer's role in the matter, the lawyer shall make reasonable efforts to correct the misunderstanding. The lawyer shall not give legal advice to an unrepresented person, other than the advice to secure counsel, if the lawyer knows or reasonably should know that the interests of such a person are or have a reasonable possibility of being in conflict with the interests of the client." Rule 4.3.

In addition, an attorney may owe a duty of care to non-clients, even if the attorney does not believe an attorney-client relationship formed, if the attorney knows, or should know, that non-clients will rely on the attorney's representations and such non-clients are not too secluded from the attorney to be entitled to protection. As

discussed above in the section discussing when an attorney-client relationship attaches, an attorney can limit the risk of owing a duty to non-clients by explicitly informing the person that representation has not begun and an attorney-client relationship has not formed. Absent such explicit statements, an attorney may owe a fiduciary duty to the person, even though the attorney views such person as a non-client.

#### **4. Special Issues for Contract Drafting**

When drafting a contracts, an attorney must ensure that no conflict of interest is present, or if a conflict exists, approval must be obtained from the parties. However, even if an attorney gains approval from the parties, an attorney must maintain impartiality throughout the contract drafting process. For example, an attorney representing a partnership may have a personal relationship with one of the partners and in drafting the partnership agreement, the attorney must make certain that the agreement is drafted in an impartial manner and that no underlying biases or assumptions based upon personal knowledge affect the contract drafting. The attorney cannot allow his or her personal knowledge of a partner to play into the contract drafting process.

Issues also arise during dual representation of parties entering into a contract. The situation becomes complex because an attorney owes his or her client a duty of loyalty, meaning the attorney must act with the client's best interests in mind; however, during dual representation, the attorney is faced with a challenge because often what is best for one party to a transaction, comes at the detriment of the other. Therefore, any contract provision that is one-sided or even biased towards a specific party, would be a breach of the attorney's duty of loyalty. Therefore, during dual representation of parties, the attorney must make certain that both parties are satisfied with the drafted contract, and biases should be eliminated to decrease the potential for client complaints.

#### **5. Special Issues for CPA's**

TTB audits are usually randomly selected. You may be selected for audit due to repeated submission errors of the BRO and Excise tax.

If you are selected for audit:

- Comply with all request and deadlines
- Provide auditor copies of all support
- Be transparent with the auditor
- Be respectful to the auditor
- Ask questions to clarify any misunderstandings

Representation of a CPA or Lawyer should not be necessary. TTB auditors are not out to “get” a brewery, they job is to ensure you are doing your job. If the result requires extra tax to be paid, ask for a payment plan not to hurt the cash flow of the brewery.

## **D. Confidentiality**

### **1. Corporate Attorneys**

Confidentiality is the foundation to a successful attorney-client relationship as it encourages clients to make full disclosures and allows attorneys to give fully-informed advice, among other things. As such, confidentiality is embedded into the attorney-client relationship through the attorney-client privilege, work product doctrine, and the ethics doctrine of confidentiality. The Model Rules of Professional Conduct provide clear rules that “a lawyer shall not reveal information relating to the representation of a client unless the client gives informed consent, the disclosure is impliedly authorized in order to carry out the representation or the disclosure is permitted” as otherwise provided in the rules. Rule 1.6(a). Specific exceptions to the general rule of confidentiality are also explicitly established in the rules, providing that:

[a] lawyer may reveal information relating to the representation of a client to the extent the lawyer reasonably believes necessary: (1) to prevent reasonably certain death or substantial bodily harm; (2) to prevent the client from committing a crime or fraud that is reasonably certain to result in substantial injury to the financial interests or property of another and in furtherance of which the client has used or is using the lawyer's services; (3) to prevent, mitigate or rectify substantial injury to the financial interests or property of another that is reasonably certain to result or has resulted from the client's commission of a crime or fraud in furtherance of which the client has used the

lawyer's services; (4) to secure legal advice about the lawyer's compliance with these Rules; (5) to establish a claim or defense on behalf of the lawyer in a controversy between the lawyer and the client, to establish a defense to a criminal charge or civil claim against the lawyer based upon conduct in which the client was involved, or to respond to allegations in any proceeding concerning the lawyer's representation of the client; (6) to comply with other law or a court order; or (7) to detect and resolve conflicts of interest arising from the lawyer's change of employment or from changes in the composition or ownership of a firm, but only if the revealed information would not compromise the attorney-client privilege or otherwise prejudice the client." Rule 1.6(b)(1-7).

However, it is important to recognize that an attorney hired for the entity, typically represents only the entity, unless agreed otherwise. In such a situation, the attorney-client privilege attaches only to the entity, not individual employees of the company. As such, any personal information given to the attorney from someone other than the entity, including an officer, director, or employee, is not protected under attorney-client confidentiality. For example, if an officer admitted to that he or she was involved in embezzlement of company funds to the entity's attorney, such information is not protected under confidentiality. Rather, the attorney is required to disclose such information to the management of the entity.

Due to the often complicated nature of the relationship, when representing an entity, an attorney needs to be careful not to unintentionally waive the attorney-client privilege. One common test regarding the attorney-client privilege in a corporate setting is the Upjohn test, which was established by the U.S. Supreme Court in 1981. The test provides that an attorney may gather facts from employees of the company, of any rank, and any employee may seek legal advice from counsel, so long as the communication: (1) was made to counsel at the direction of corporate superiors; (2) concerned matters that are within the scope of the employees' duties; (3) the information was not available from any upper-level management; and (4) the employees were made aware that they were being questioned by the attorney in order for the company to receive legal advice. Although the Upjohn test is a common test,

some states still follow other tests. Therefore, it is important to understand the rules of the jurisdiction in which the attorney is operating in order to ensure attorney-client privilege is protected.

## **2. For CPAs**

From the Professional code of Conduct: A member in public practice shall not disclose any confidential client information without specific consent of the client.

## **E. Fees and Charges**

### **1. Retainer Agreements**

The purpose of a retainer agreement is to document the relationship between the parties. The Model Rules of Professional Conduct dictate that “[t]he scope of the representation and the basis or rate of the fee and expenses for which the client will be responsible shall be communicated to the client, preferably in writing, before or within a reasonable time after commencing the representation.” Rule 1.5(b). As such, the agreement does not need to be in writing, nevertheless, to avoid confusion or later litigation, it is advisable to put such an agreement in writing.

However, there are certain arrangements that require the agreement be in writing, such as a contingent fee arrangement. The rules require that a contingent fee arrangement “be in writing signed by the client and shall state the method by which the fee is to be determined, including the percentage or percentages that shall accrue to the lawyer in the event of settlement, trial or appeal; litigation and other expenses to be deducted from the recovery; and whether such expenses are to be deducted before or after the contingent fee is calculated.” Rule 1.5(c) In addition, the written agreement must “clearly notify the client of any expenses for which the client will be liable whether or not the client is the prevailing party.” *Id.*

Although there is no set format for a retainer agreement, it is advisable to leave nothing to memory or chance, and the best way to do so is having clients sign a written retainer agreement. To reduce confusion or misunderstandings, the attorney-client relationship should begin with a written agreement including, but not limited to, the following elements:

- Client’s identity;

- A description of the work covered by the fee or hourly rate (scope of the representation);
- The amount of the fee or hourly rate;
- Out-of-pocket costs (generally, the lawyer will want to represent that additional out-of-pocket costs may apply on top of the lawyer's hourly rate or fee);
- Agreement of the client to cooperate and be truthful;
- Either party's right to terminate services;
- Consequence of non-payment;
- No guarantee of particular results on behalf of the attorney; and
- Signature (of both the attorney and the client).



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