

Department of Legislative Services
Maryland General Assembly
2018 Session

FISCAL AND POLICY NOTE
First Reader

House Bill 518

(Chair, Economic Matters Committee)(By Request -
Departmental - Comptroller)

Economic Matters

Alcoholic Beverages - Reform on Tap Act of 2018

This departmental bill makes numerous changes to the regulation of Class 5 breweries, Class 6 pub-breweries, Class 7 micro-breweries, and Class 8 farm-breweries in the State. **The bill takes effect July 1, 2018.**

Fiscal Summary

State Effect: General fund revenues increase to the extent that the bill results in additional tax revenues from the manufacturing and sale of alcoholic beverages beginning in FY 2019; however, any such impact cannot be reliably estimated. The Comptroller's Office can handle the bill's requirements using existing resources.

Local Effect: Local governments can handle the bill's requirements using existing resources. Revenues are not affected.

Small Business Effect: The Comptroller's Office has determined that this bill has a meaningful impact on small business (attached). The Department of Legislative Services (DLS) generally concurs with this assessment, as discussed below.

Analysis

Bill Summary: The Beer Franchise Fair Dealing Act does not apply to any licensed beer manufacturer that, in conjunction with an affiliate, only produces 300,000 barrels of beer or less each year. The amount of beer that may be distributed by any brewery that holds a Class 7 limited beer wholesaler's license is increased from 3,000 barrels to 300,000 barrels.

In addition, a brewery may obtain this wholesaler's license if it produces no more than 300,000 barrels annually, instead of no more than 22,500 barrels annually.

Class 5 Breweries

The bill makes the following changes to the manner in which Class 5 breweries are regulated.

- A brewery may serve samples of beer to anyone of legal age that is visiting the brewery, instead of only during tours and events.
- A brewery is expressly authorized to conduct a guided tour of the brewery, promotional event, or other organized activity at the brewery.
- An individual of legal drinking age may purchase any amount of beer for off-premises consumption directly from the brewery each visit, instead of only 288 ounces per visit.
- A brewery may obtain an on-site consumption permit if it has a Class B beer license.
- A local licensing board must grant a brewery an on-site consumption permit if the applicant also has a Class B or Class D beer license.
- A brewery can sell, for on-premises consumption, beer that was brewed in part at the brewery under contract with a Class 5 brewery or Class 7 micro-brewery.
- A brewery may sell any amount of its own beer, brewed at the brewery, for on-premises consumption.
- The total amount of beer that was brewed at a location other than the licensed premises that can be sold for on-premises consumption is simplified so that the brewery may sell up to 1.2% of the total amount of beer brewed each year in this manner.
- The hours of sale for on-premises consumption at all breweries are those set by the underlying Class B beer license, Class D beer license, or equivalent license.
- The Comptroller is no longer required to annually report specified information about on-premises consumption at breweries to specified committees of the General Assembly.
- For up to two years after a brewery obtains a Class 5 license from the Comptroller's Office, the brewery may produce beer entirely or in part at a location other than the licensed premises. However, if the brewery is not fermenting and brewing at least 50 barrels of beer annually after this two-year period, the Comptroller must revoke the brewery's license.

Class 6 Pub-Breweries

The Comptroller may no longer issue a Class 6 pub-brewery license beginning on October 1, 2018. However, the holder of a Class 6 license may continue to renew the license after that date.

Class 7 Micro-Breweries

The bill makes the following changes to the manner in which Class 7 micro-breweries are regulated.

- The production limit of 22,500 barrels per year is repealed. Therefore, a Class 7 micro-brewery may brew, bottle, or contract for any amount of beer.
- The on-premises consumption limit of 4,000 barrels of beer per year is repealed. Therefore, a Class 7 micro-brewery may sell any amount of its own beer for on-premises consumption.

Class 8 Farm Breweries

A Class 8 farm brewery may produce an unlimited number of barrels of beer each year, instead of only 15,000 barrels.

Current Law:

The Three Tier System of Regulation

Alcoholic beverages in the State are regulated through a three tier distribution system. The system separates ownership and operations among (1) manufacturers; (2) wholesalers; and (3) retailers. The system authorizes manufacturers (tier one) to sell only to wholesalers (tier two); wholesalers only to retailers (tier three); and retailers only to consumers; however, there are some statutory exceptions. For example, certain breweries are authorized to distribute up to 3,000 barrels of their own beer if they obtain a Class 7 limited beer wholesaler's license and meets other specified requirements. Generally in Maryland, the Comptroller issues statewide licenses to manufacturers and wholesalers, while each licensing jurisdiction issues licenses to retailers to operate within its boundaries.

Beer Manufacturers

Brewers (beer manufacturers) in Maryland are required to obtain one of four types of State licenses: a Class 5 brewery license; a Class 6 pub-brewery license; a Class 7 micro-brewery license; or a Class 8 farm brewery license. Each license is issued by the Comptroller for an annual fee of \$200 or \$500 depending on license class. Each class of

license specifies the amount of beer that may be brewed each year, the type of location that may be licensed, and the manner in which beer may be sold. Chapter 813 of 2017 made numerous changes to the on-premises sampling and sale of beer by a Class 5 brewery, and its major changes are discussed in more detail below.

The Beer Franchise Fair Dealing Act

Established in 1947, the Beer Franchise Fair Dealing Act regulates the agreements, franchises, and relationships between beer manufacturers and their distributors (wholesalers). Among other things, the Act prohibits a brewery from terminating a contract with a distributor without good cause.

Additionally, if a brewery wishes to terminate or refuse to renew a franchise agreement with one of its distributors, the brewery must provide the distributor with notice at least 180 days before terminating or refusing to renew the contract. The notice must state all the reasons for the intended termination or nonrenewal. If deficiency is claimed as the reason for the termination or nonrenewal, the distributor has 180 days after the notice is received to rectify the deficiency. If the distributor rectifies the deficiency within this time period, the brewery may not terminate or refuse to renew the contract with the distributor.

Class 5 Breweries

The holder of a Class 5 brewery license may (1) establish and operate a plant for brewing and bottling malt beverages at the location described in the license; (2) import beer from a holder of a nonresident dealer's permit; (3) contract to brew and bottle beer on behalf of other license holders; and (4) sell and deliver beer to a holder of a beer wholesaler's license. There is no limit to the amount of beer that a Class 5 brewery, also called a "production brewery," may produce.

A Class 5 brewery may also serve samples of beer to an individual who participates in a guided tour of the brewery or attends a scheduled promotional event. Generally, the beer brewed at the brewery may also be sold for off-premises consumption at retail in a container other than a keg to an individual participating in a guided tour of the brewery or attending a scheduled promotional event or other organized activity at the brewery. Each individual may purchase up to 288 ounces of beer per visit.

Local licensing boards in the State may issue on-premises consumption permits to applicants that hold a Class 5 brewery license and a Class D beer license. Accordingly, a brewery with a Class D beer license can operate like other bars, the most common type of Class D establishment, meaning that a brewery tap room can often stay open until 2 a.m. A local licensing board that does not issue a Class D beer license must establish an

equivalent license and require the applicant to obtain that license before issuing a permit for on-premises consumption.

Class 5 Breweries – Chapter 813 of 2017

Among other things, Chapter 813 of 2017 made three significant changes to the manner in which Class 5 breweries are regulated in the State. First, Chapter 813 increased from 500 barrels to 2,000 barrels the volume of its own beer that a Class 5 brewery may sell each year for on-premises consumption. A brewery may sell or sample an additional 1,000 barrels of its own beer if the additional beer is sold to and purchased back from a licensed wholesaler and the brewery receives permission from the Comptroller's Office. If a brewery produces more than 1 million barrels of beer each year, it must buy any beer it wishes to sell or serve for on-premises consumption back from a licensed wholesaler. Second, Chapter 813 expressly authorized contract brewed beer and allows the contract brewed beer produced at another location to be sold and sampled at the brewery in limited quantities.

Third, Chapter 813 made changes to the hours during which a brewery may sell and serve beer for on-premises consumption. A brewery that acquires the permit and license needed for on-premises consumption after April 1, 2017, is restricted by shortened hours of sale unless the brewery had already filed a brewer's notice form with the U.S. Department of Treasury by that same date. For such a brewery, beer may only be sold for on-premises consumption from 10 a.m. to 10 p.m. each day.

Other Classes of Brewery

A Class 6 pub-brewery license may only be issued to the holder of a Class B beer, wine, and liquor (on-sale) license that is issued for use at a restaurant. The pub-brewery must be located immediately adjacent to the restaurant, and it may brew up to 2,000 barrels of beer each year for consumption at the associated restaurant.

Generally, a Class 7 micro-brewery license may be issued only to the holder of a Class B beer, wine, and liquor (on-sale) license that is issued for use at a restaurant. A license holder may brew, bottle, or contract for up to 22,500 barrels of beer each calendar year. However, any beer produced under a contractual arrangement accrues to the license holder that owns the brand. The license holder is authorized to sell for on-premises consumption up to 4,000 barrels of beer brewed under the license, with specified restrictions.

In general, a Class 8 farm brewery license authorizes the license holder to brew, bottle, or contract for up to 15,000 barrels of beer each year; however, that beer must be manufactured with an ingredient from a Maryland agricultural product, including hops,

grain, and fruit, and produced on the licensed farm. The license holder may sell and deliver the beer to a licensed wholesaler or a person in another state authorized to acquire beer.

Background: In February 2018, there were (1) 41 Class 5 breweries; (2) 1 Class 6 pub-brewery; (3) 29 Class 7 micro-breweries; and (4) 20 Class 8 farm breweries. During that same month, 64 of these breweries had Class 7 limited beer wholesaler's licenses.

The bill is the result of the Reform on Tap Task Force, which was established by the Comptroller in April 2017. The stated goal of the task force was to modernize Maryland's beer laws and promote economic growth across the State. The task force's final meeting took place in November 2017, where the Comptroller's Office presented its [findings report](#). The report discussed the recent expansion of craft beer manufacturing in the country and its effect on the State's economy.

In November 2017, DLS published a report on [Regulation of the Alcoholic Beverages Industry in Maryland](#). The report summarizes the current manner in which alcoholic beverages are regulated in the State, with a focus on alcoholic beverages manufacturers.

Small Business Effect: DLS generally concurs that the bill has a meaningful positive impact on small business breweries in the State; however, DLS cannot independently verify the specific economic impact estimates provided by the Comptroller's Office.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Comptroller's Office; Baltimore County; Department of Legislative Services

Fiscal Note History: First Reader - February 19, 2018
nb/tso

Analysis by: Richard L. Duncan

Direct Inquiries to:
(410) 946-5510
(301) 970-5510

ANALYSIS OF ECONOMIC IMPACT ON SMALL BUSINESSES

TITLE OF BILL: Reform on Tap Act of 2018

BILL NUMBER: HB 518

PREPARED BY: Anne Klase

PART A. ECONOMIC IMPACT RATING

This agency estimates that the proposed bill:

WILL HAVE MINIMAL OR NO ECONOMIC IMPACT ON MARYLAND
SMALL BUSINESS

OR

WILL HAVE MEANINGFUL ECONOMIC IMPACT ON MARYLAND
SMALL BUSINESSES

PART B. ECONOMIC IMPACT ANALYSIS

An economic impact study conducted by the Bureau of Revenue Estimates (BRE) found that in 2016, Maryland's craft brewing industry had an overall economic impact of \$637.6 million, supported or created 6,541 jobs, and generated \$228.3 million in wages as well as \$53.1 million in state and local revenue.

It's worth noting that the aforementioned figures are limited to the economic impact resulting from craft beer exclusively produced by Maryland craft breweries. However, the distribution and sale of non-Maryland brand craft beer to consumers within the state also positively impacts the economy. When the sale and distribution activity of non-Maryland craft beer is included in the projection, the estimated economic impact of craft beer rises to \$802.7 million within Maryland in 2016. The positive impact on Maryland is 54% greater when the beer is produced by a Maryland craft brewery.

The report found that in 2016, Maryland craft breweries directly employed 430 Marylanders, and had an indirect and induced effect on 264 jobs – yielding a total of \$28.4 million in labor income and generating \$143.7 million in economic output. Maryland craft brewers supported more than 693 Maryland jobs.

Additionally, alcohol distributors in Maryland greatly benefited from the economic activity generated by Maryland craft brewers. Maryland craft brewers directly impacted 201 jobs in

Maryland’s alcohol distribution industry, indirectly impacted 114, and had an induced effect on 137. \$32.1 million in labor income and \$91.0 million in economic activity in the distribution industry were impacted by Maryland craft brewers.

Retailers, restaurants, and bars – which directly employ 4,322 Marylanders – are also positively impacted by Maryland craft brewers. In 2016, the Maryland craft beer industry had a direct, indirect, and induced effect on 5,395 jobs, \$167.7 million in labor income, and \$402.9 million in economic output on the alcohol retail and sale industry.

The report also analyzed the impact of revenue generated by craft beer production and sales. Craft beer production is fundamentally a labor-intensive industry, resulting in a high degree of local economic impact. The report found that for every \$20,000 in revenue that is generated or received by Maryland craft brewers (e.g., product sales, private investments, government subsidies), 1.36 jobs, \$47,410 in wages, and \$132,405 in economic output are created.

The economic impact of Maryland’s craft beer industry has not reached its full potential. This is demonstrated most clearly by Maryland’s status as a net importer of craft beer. While consuming an estimated 275,000 barrels of craft beer per year, Maryland produces only 247,000 barrels.

Based on Flying Dog’s testimony alone, because of the unfavorable law structure towards breweries in Maryland, they have decided to place expansion plans on permanent hold. This expansion would have increased the number of barrels produced in Maryland from 247,000 a year to 627,000 a year. If Flying Dog changed course as a result of the laws being amended by the passage of this bill and decided to go through with their expansion, it is estimated that state revenues would increase by \$15.8M between the general and special funds, and local revenue would increase by \$9.8M, both annually. This amount includes personal and corporate income tax, property tax, sales tax, as well as additional fines and fees from the breweries producing and selling more beer, the input industries providing additional input, and the workers in these industries going out and spending the wages from the additional jobs that would be created. A chart is below:

| | |
|----------------------|-----------------|
| State Revenue | |
| General Fund | \$12,029,720.45 |
| Special Fund | \$3,716,772.62 |
| State Total | 15,746,493.07 |
| | |
| Local Revenue | 9,836,721.93 |

The industry currently brings in an estimated \$32.9M in state revenue and \$20.2M in local revenue.