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# Avoiding Growing Pains

*Getting straight on the routines involved with winery expansion and regulation*

It's a happy moment in any winery's history when you realize that consumer demand for your product exceeds your production capacity. Congratulations! Wineries respond to this situation in a variety of ways, the easiest of which is purchasing bulk wine or outsourcing production through one or more custom crush contracts, where legal. But the Cadillac way to go, if quality assurance and control are priorities, is to expand your winery.

Sure, the expansion route brings along a few growing pains to endure, especially if new construction involves jumping through county planning hoops. But the TTB and ABC requirements are relatively routine—especially if you know about them in advance. And that is why we are dedicating this column to giving you all the tips you need to know to get regulatory approvals for your winery expansion. Armed with this knowledge, you can raise a toast to growth and savor the moment all the way to the ribbon-cutting day.

## REPORTING WHAT AND WHEN

Of course, you already know that if you move your winery from one address to another or open an additional facility, you must file applications with the federal and state regulatory agencies. But what if you expand your cellar area or make other changes in the layout or use of your winery while staying

### SHORT COURSE

- ▶ Because of different regulatory mandates, state and federal authorities will require different information when you expand your winery.
- ▶ The key to TTB premise change reporting is keeping your bonded premises description and bond coverage amount accurate and up to date.
- ▶ The focus of ABC premise change reporting is notifying regulators of changes to all areas where license privileges are exercised.
- ▶ Non-contiguous extensions allow wineries to add distant buildings to their existing bond and permit, but usually additional state licenses are required.
- ▶ Time is of the essence in reporting premise changes, many of which must be approved before operations start in the enlarged or new locations.

at the same location? Those changes, too, must be reported in advance. You may also need to increase the amount of your bond or secure the consent of your bond company for this premises expansion.

Some of the kinds of growth that wineries often forget to report include extension of the bonded winery premises into other parts of the building that had been used for non-winery operations, such as the storage of farming equipment; enlarging outdoor crush pads, barrel work areas, or mobile bottling areas; tasting room expansions or remodeling; enlarging caves; and remodeling of the winery building that results in changes in use of various areas.

### REPORTING TO WHOM AND WHY

As we said, winery expansion changes

must be reported to both TTB and your state alcohol regulators. But, because the state and federal regulatory mandates differ significantly, the timing and types of reporting required by each are not the same.

TTB is primarily concerned with issues affecting tax collection and the ultimate taxable activity, alcohol production. It is of utmost importance to TTB that your bonded area be properly defined and adequately covered by your bond. Many winery folk don't realize the regulatory significance of the winery bond: it guarantees the bond company's obligation to pay your winery taxes should the winery default on them. But bond companies insist that their liability extends only to the limits of your officially approved "bonded premises" (as well as covering any wine in transit to your winery). Thus, if a winery possesses un-taxpaid wine outside of its approved bonded premises, the tax value of that wine is uninsured—something TTB never wants to happen. Therefore, for TTB it is crucial to keep up to date on any changes of the size, location, and use of your bonded premises, while they care very little about your off-bond tasting room and other non-bonded areas.

On the other hand, state regulators are relatively relaxed about production operations; they know TTB is on top of those. State regulators are typically most concerned about regulating your use of your license privileges relating to promotional activities and sales. So, they may not want notification about certain changes in your winery production area. But if you open a new sales office or

warehouse building across the road from your winery and start shipping wines from that new location before obtaining a license there, they may cite you for selling without a license. The local ABC authorities might require you to stop using the new building until a license is issued, and even fine you.

As you read the rest of this article, keep these principles in mind. If you can remember the state and federal rationales for requiring notifications, their reporting requirements will actually start to make sense!

### PREMISE REPORTING BASICS

If you propose to make simple changes to your wine premises, those changes can be reported in a letter sent to TTB's National Revenue Center (NRC) in Cincinnati. TTB will notify you if an application or other documents are required. Your state ABC should also be notified of your intended changes. In California, changes to the licensed

premises should be reported by filing a revised diagram form and letter describing the change.

Your licensed premises for ABC purposes does not need to exactly match the bonded area for TTB purposes. For instance, a public tasting room can be on or off bond for TTB purposes; it's just a matter of whether you want to pour tastes from tax-paid or in-bond wine. If your tasting room is "off-bond," tasting room changes will not need to be reported to TTB.

However, in California, for example, your tasting room must be part of the ABC licensed premises, since tasting is a highly regulated state privilege. Every area where ABC license privileges, such as production, tasting, and sales, are exercised should be encompassed in the licensed premises—including portions of patios and lawns if used for winery events that feature public tasting—even if they are not included in your bonded winery premises for TTB purposes. Therefore, the California ABC will want to

approve any and all proposed changes to the interior or layout of your tasting area.

### BUILDING A NEW WINERY?

If you're moving to a new winery facility at a different location, you will need to plan well in advance. When a winery moves, TTB requires an application to amend the basic permit and an application to establish new bonded premises at the new location. You will need a new wine bond for the new winery location. Your state ABC will require a change of location application. In California, it is called a "premise-to-premise transfer." Unlike changes of ownership, which can get processed after the fact, premise-to-premise transfers must be fully processed and approved before moving in. The so-called "temporary permits" that allow new owners of California wineries to operate while their applications are being processed cannot be issued on a premise-to-premise transfer application.

No matter where you are located, you should assume that the winery cannot begin operations at the new location or move wine onto the premises until the applications are approved, a new TTB registry number is assigned, and the state license is issued. The application processing period can take 90 days—perhaps longer.

### NON-CONTIGUOUS EXTENSIONS

An easier way to expand, if space is available, is to locate another building near your existing winery and add it to your existing TTB bonded premises as a non-contiguous premises extension. A non-contiguous extension is an area that is separate from the main winery location, but near enough that TTB allows both locations to be covered by one bond, basic permit, and registry number. This privilege allows wineries to operate bonded areas at different locations as a single winery as long as (a) both locations have the same post office (town) in their physical address and (b) the two locations are no more than five miles apart.

To apply for a non-contiguous premise extension the winery files an amended Application to Establish and Operate Wine Premises (TTB

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F 5120.25) and a Consent of Surety with TTB. The Consent of Surety is like a rider to an insurance policy and extends the existing bond coverage to this new building without redoing the bond.

Even though the new non-contiguous building is covered by the same TTB bond and permit as your original location, a separate Special Tax Stamp is needed for each location in most cases. (Only one Special Tax Stamp is required when the two separate areas are divided only by (1) intervening real property which is all owned by the winery, or (2) a street, highway, rail crossing, waterway, or building partition, where the two areas are otherwise contiguous.) Fortunately, the required annual payments for Special Tax Stamps have been suspended for three years starting July 1, 2005, but wineries still need to register any new locations with TTBs SOT unit. (See the accompanying: A Word About the Suspension of Special Occupational Tax.)

Even if TTB extends your existing bond and permit to include a second location, your local ABC is likely to require another license for the additional building. In California, the ABC does not allow two different locations or physical addresses to be covered by one license. The only exception to this rule is several buildings that are separated only by space controlled by the licensee, such as on a single parcel of land or on contiguous commonly owned parcels, or in a complex where two or more buildings are separated only by a shared parking lot or driveway. Check with your local ABC about adding a new building to your license, and start early enough to have licensing in place when you want to start using it.

#### MAJOR ADDITIONS AND CHANGES TO YOUR EXISTING BUILDING

Unless all of your expansion is occurring on ground previously included within the footprint of your bonded area, if you are going to make major changes or substantially enlarge your existing winery buildings, it is likely that TTB will request that you file an application to update your winery permit. Start by notifying TTB with a let-

ter describing your plans. It is always helpful to include a diagram showing the new areas. If the changes are major enough, or your prior winery description was minimal, it is likely that TTB will request the filing of an amended Application to Establish and Operate Wine Premises with a description of the new areas. We recommend preparing a description of

your entire winery premises, not just the new part, so it remains perfectly clear exactly what is covered by your permit and bond. We have observed that TTB is now requesting that winery descriptions be more thorough and complete than in the past.

It is likely that TTB will also ask whether you need to increase your bond amount. Enlarging your win-

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## A Word About the SPECIAL OCCUPATIONAL TAX

YOU MAY HAVE SEEN NEWS reports that the Special Occupational Tax ("SOT") has been temporarily suspended. For the next three tax years, industry members can re-allocate the money normally expended for this annual tax as they choose.

Of course, the industry is happy with this small windfall. But it's too soon to forget about SOT altogether. Here are two important details the news reports did not explain:

1. The law's effective date of January 1, 2005, falls in the middle of the SOT tax year, which runs from July 1 to June 30 annually. TTB is still collecting special taxes until the beginning of the next tax year, which starts on July 1, 2005. Therefore, new businesses and/or locations established before June 30, 2005, still owe the prorated tax due from the start of business to June 30, 2005.

2. TTB is still keeping track of taxable locations dur-

ing the tax suspension. So, until further notice, permittees, licensees, etc. will still need to file renewal returns and register new locations, even while the SOT tax payments are temporarily suspended.

In May, all wineries will receive a SOT renewal notice from TTB listing your locations. As in the past, it should be returned to TTB with any changes noted. The only difference from previous years is that you will not enclose a check for the taxes. TTB will even continue to issue a Special Tax Stamp for each of your locations, and they should still be posted on your premises.

The three tax years during which the tax is suspended end June 30, 2008. Payment of the SOT tax will resume on July 1, 2008, unless Congress takes further action to either extend the suspension or eliminate the tax. Until then, enjoy the tax savings!


ery means more capacity, and more capacity means you will have more un-taxpaid wine on the winery premises. Unless you already have a \$50,000 or \$100,000 bond (which covers tax liabilities up to \$250,000 and over \$250,000 respectively), an increase in the tax value of your in-bond inventory will require increased bond coverage. If you do have to increase your bond, you can either replace it with a larger "superceding" bond, or simply add onto it with a "strengthening" additional bond. (A superceding bond makes it easier for

both TTB and you to keep track of the amount of your bond.)

Remember that you will also need to notify your state ABC of the proposed additions to your winery premises. What should be filed will depend on the extent of your expansion and where it is located. It may be as simple as filing a new diagram form or it may need an application.

### A PROBLEM YOU WANT TO HAVE

It may seem like a hassle to comply

with all the requirements described in this article, but this is one problem most business people would love to have. After all, when you are expanding your production capacity in response to "popular demand," you're trading in the problems of establishing a reputation and struggling to build market share in exchange for the much more rewarding problems of growth. But to keep your new problems as painless as possible, remember that it might take some time to get your new premises approved, so plan ahead. 

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