

# From Vineyard to Vintner

By Sara Schorske and Alex Heckathorn

At the end of last year's crush the grape growing community was sobered by the news that in California 75,000 tons of grapes had been left on the vine. Industry analysts, pointing to the fact that vineyards planted in the last few years are now coming into full production, predicted that this year, once again not all grapes would find a home by harvest time.

At times like these, it may seem that there is no option but to leave unsold the fruit in the vineyard. But there is another choice: turning those grapes into wine—a far less perishable commodity.

There are several good reasons to consider crushing your own grapes. Think of it as an inexpensive and effective form of crop insurance! Converting your crop into wine lengthens your window of opportunity to sell your product. If you don't make wine from your unsold grapes, your opportunity to market them ends abruptly when autumn rains commence or when the grapes become overripe. Making your grapes into wine also increases your universe of potential customers. For instance, there are many companies which never buy grapes, but DO buy hundreds of thousands of gallons of bulk wine every year. And if you bottle and label your wine, you can market it to even more customers.

Selling grapes requires no license, but the production and sale of wine is highly regulated. Therefore, the more you know and the longer in advance you begin planning, the more options you have. The necessary licenses can take 60 days or more to obtain.

There are four main approaches people take to entering the wine business:

- the Piggyback way
- the Custom Crush way
- the Alternating Proprietor way
- the Bricks 'n' Mortar way.

## The Piggyback way

You may already be a Piggybacker without knowing it. Piggybackers are usually grapegrowers who have had grapes custom crushed by a local winery and have made arrangements for the winery to market the wine for them. In this arrangement, the winery makes the wine, invoices the buyer, and collects the proceeds. Piggybackers don't obtain their own governmental approvals; they "hitch a ride" on the winery's alcoholic beverage licenses.

If crush is upon you and you don't have the licenses you need to custom crush, piggybacking is an appealing option, but it is only legal under certain conditions. If done carelessly, you may be accused of selling wine without a license, and you may expose the crushing winery to ABC and CDFV violations too.

To avoid problems, structure the relationship to the winery so that you are paid for grapes, not wine. That may sound like a brain-teaser, but here's a simple way to convert wine sales into a grape purchase. Agree with the winery that

1) you will not be paid until the wine is sold, and

2) the price per ton will be retroactively computed, based upon the proceeds from the wine at the time of sale.

This agreement must be put in writing, because in the absence of a written contract specifying otherwise, California law requires payment for grapes thirty days after delivery. And if that isn't a good enough reason to make a written agreement, do it just to

make sure the terms of sale are clearly understood, strictly followed, and able to be documented if questioned by a State ABC official.

Although tempting, the Piggyback approach is not a long-term alternative for getting your own license. Many wineries may not want to be that involved with the marketing and sale of your wine, or have that much of an ongoing liability to you. Also, this approach gives you no control or legal title to the wine, although you do have your grower's lien.

## The Custom Crush way

Fortunately, you don't have to become a winery to have the option of selling your grapes as wine instead of fruit. Growers in California can legally have their grapes custom crushed and sell the resulting wine to wineries. If you've dreamed of developing your own brand or building your own winery in the future, custom crushing is a perfect way to get your feet wet before jumping into the deep water.

California Custom Crushers can choose from several types of licenses, depending on your plans. The most common, and easiest, license for a grower is a Winegrape Grower's Storage License (a "Type 29" license). Only growers are eligible for a Winegrape Grower's Storage License; this license does not authorize sales of wine made from grapes not grown by the licensee.

The Type 29 license allows the grower to store bulk wine made from his own grapes at a winery and to sell that wine in bulk to wineries, distilled spirits manufacturers, and vinegar producers within California. (If you have an opportunity to sell your bulk wine to a wholesaler or retailer, who cannot legally purchase directly from you, you can probably make an intermediate sale to the crushing winery, who can legally sell to your customer.) At \$64 a year, the Type 29 license is your most inexpensive way to go.

This license has another unique advantage: In California, licensees are generally required to hold a separate license at every location where privileges are exercised. Typically, this includes the licensee's office, as well as any site from which sales and shipments are made. This requirement posed special challenges to growers, who frequently do not know until the last minute how much tonnage they need crushed, or what wineries could accommodate their grapes. Fortunately, a kindly interpretation by the California ABC now allows growers to cover all their custom crush operations by obtaining a single Type 29 license at the grower's office premises. This means you do not need to know which winery will make your grapes into wine at the time you apply for the license. Also, you may use as many wineries as you choose and even move your bulk wine from one bonded premise to another. This flexibility can be a boon in times when tank space is at a premium.

If you wish to actually develop your own label, the Type 29 license doesn't have enough privileges for you. You will need either a Beer and Wine Wholesale License ("Type 17") or an Importers General License ("Type 10"), depending on your marketing plans. With these licenses you can also buy other wine, to blend with yours or bottle separately, if that seems advisable to improve your wine or extend your product line. Unlike the Type 29 license, grow-

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ers will need separate licenses at their office location and at any storage facility from which they ship, if those places are different.

The California Wholesale and Importer licenses do not allow you to sell wine to consumers. If that privilege is important to you, you may be able to obtain a restricted retail license for mail order sales. However, the retail license requires that your location be properly zoned for retail activity, and the public notice mailed to nearby residents as part of the retail license application process can cause significant problems.

In addition to State licenses, custom crushers need to obtain a Wholesaler's Basic Permit from the federal agency formerly known as the Bureau of Alcohol, Tobacco and Firearms ("ATF"), now called the Alcohol and Tobacco Tax and Trade Bureau ("TTB" for short). While this permit is relatively easy to obtain, it can take up to three months to issue, so planning ahead is crucial. You will also have to pay Special Occupational Tax, which is an annual tax collected by the Bureau.

A Custom Crusher's life is pretty simple. Production responsibilities—both practical and legal—are delegated to a bonded winery. As a result, the investment required is quite low, and recordkeeping and reporting requirements are also minimal. The biggest disadvantages to this approach are (1) Custom Crushers don't have all the promotional privileges that wineries have and (2) Custom Crushers can direct but not completely control the winemaking process.

The third and fourth options solve these disadvantages. Both involve becoming a bona fide winery, conferring all the privileges and control, and requiring all the recordkeeping and reporting, that goes along with winery licenses.

### **The Alternating Proprietor way**

Alternating Proprietors get to have their own bonded winery and their own wine-stained feet at bargain basement prices. The way they avoid the usual million dollar price tag for these privileges is by sharing space and equipment with an established winery. The challenges of this way of operating are (1) the licensing paperwork is more complicated and (2) operating this way can be confusing to everyone involved. But since 1991 when wineries first started operating as Alternating Proprietors, this way has become well established and usually works smoothly.

### **The Bricks 'n' Mortar Way**

The Bricks 'n' Mortar way is the time-honored method of starting a winery. Those who take this option build, buy, or lease a premise and set up an independent winery operation of their own. When buying an existing winery, alcoholic beverage licensing and local permits are already in place and can readily be transferred to the new owner. But when starting from scratch, all of these approvals must be taken care of by the aspiring winery owner.

Below is a list of names and functions of agencies that a follower of the Bricks 'n' Mortar way will most likely deal with. This list is general and not necessarily exhaustive. Specific agency names and functions vary from place to place, so you must adapt the list for use in your locality.

- California Dept. of Alcoholic Beverage Control issues State alcoholic beverage licenses
- Alcohol and Tobacco Tax and Trade Bureau issues federal alcoholic beverage permits and grants label approval
- IRS assigns federal employer identification numbers
- County Clerk registers fictitious business names
- Trademark Office and TTB provide information on previous uses of chosen names
- State Board of Equalization collects employer, income, and excise tax accounts
- County or city planning department provides information on zoning suitability and issues conditional use permit if required
- Building Department issues building permits
- State or county transportation authorities, depending on whether access is from state or county roads, administer parking and access requirements, may require possible improvements or encroachment permits
- Forestry/Fire services department regulates fire protection requirements and hazardous materials use
- State, county, or city water agencies regulate stream setbacks, underground tanks, wastewater monitoring and issues required permits
- Public/environmental health department regulates waste water disposal and issues a variety of permits relating to health concerns
- Federal, state, county, agricultural agencies issue weigh-master licenses and grape purchase licenses, and oversee pesticide use
- City business license tax office, if site is in city limits, issues business license

### **Taking the plunge**

You may need help deciding what course of action is best for you, and oftentimes nearby wineries and local business advisors aren't familiar enough with the legalities to help you. We recommend seeking advice from a compliance expert or from the regulators themselves.

Once you decide on a course of action, you have the option of doing all the paperwork processing yourself, or hiring help. The choice is much like doing your own income taxes, or using the services of a tax preparer. The decision is yours. The cost of getting help varies widely, depending on the expertise of the helper, the type of licenses you want, and the ownership structure of the licensed business.

Whatever you do, it's best to put your plans in place well before harvest—your crop may depend on it.

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