

Virginia Winery
distribution company

10/07/2022
10:00 AM
VDACS – Conference Room 220
102 Governor Street
Richmond, VA 23219

Agenda

- Call to Order
- HB1336 draft report review
- Public Comment
- Adjourn

**REPORT OF THE VIRGINIA WINERY DISTRIBUTION COMPANY (VWDC) ON THE FINDINGS AND
RECOMMENDATIONS OF THE WORK GROUP TO EVALUATE THE NEEDS RELATED TO THE DISTRIBUTION
OF WINE AND BEER**

PUBLICATION YEAR 2022

Document Title

Report of the Virginia Winery Distribution Company (VWDC) on the Findings and Recommendations of the Work Group to Evaluate the Needs Related to the Distribution of Wine and Beer

Author

Department of Agriculture and Consumer Services

Legislative Mandate

Chapter 334 of the 2022 Acts of Assembly

Executive Summary

As required by Chapter 334 of the 2022 Acts of Assembly, the Virginia Department of Agriculture and Consumer Services (VDACS) convened a work group (Work Group) consisting of representatives of the Virginia Alcoholic Beverage Control Authority, the Virginia Wineries Association, the Virginia Wine Wholesalers Association, the Virginia Beer Wholesalers Association, the Virginia Craft Brewers Guild, and other relevant stakeholders to (i) conduct research to determine the appropriate fee structure and general fund appropriation necessary to adequately address staffing needs and perform information technology system upgrades for the purpose of accommodating winery, farm winery, and limited brewery licensees that wish to utilize the services of the Virginia Winery Distribution Company (VWDC); (ii) evaluate the number of barrels of beer allowed to be distributed by a limited brewery licensee over the course of one year; and (iii) review and evaluate alternative avenues of distribution, other than distribution through the VWDC, that could be made available to limited brewery licensees. The bill directs the Work Group to report its findings and recommendations to the VWDC Board of Directors (VWDC Board) for approval and directs the VWDC Board to report any such approved findings and recommendations to the Chairmen of the Senate Committee on Rehabilitation and Social Services and the House Committee on General Laws no later than October 1, 2022. Through presentations and discussions from Work Group participants during three meetings, the Work Group considered the history and operation of the VWDC, the legislation responsible for the VWDC's creation, agricultural component requirements, distribution limitations, alcoholic beverage control regulations and tax structure, and associated costs as a benchmark for comparison.

The Work Group consisted of the following members, representing organizations as required by Chapter 334:

- Joseph Guthrie, Commissioner, Virginia Department of Agriculture and Consumer Services (VDACS)
- Marc Haalman, Special Agent, Virginia Alcoholic Beverage Control Authority (VABC)
- George Hodson, Veritas Vineyards, representing Virginia Wineries Association
- Doug Zerbst, Republic National Distributing Company, representing Virginia Wine Wholesalers Association
- Philip Boykin, Virginia Beer Wholesalers Association
- Paige Wernig, Virginia Craft Brewers Guild
- Courtney Mailey, Owner, Blue Bee Cider and Chairman of the Board, Virginia Winery Distribution Company (VWDC)
- Staci Saunders, VWDC Operations Manager
- Kendra Shifflett, Director of Administrative and Financial Services, VDACS
- Parker Slaybaugh, Chief Deputy Secretary of Agriculture and Forestry, Office of Governor Youngkin
- Burnie Gaskill, VABC
- Melissa Assalone, Virginia Food Industry Association

This report summarizes information presented and discussed during Work Group meetings held on June 1, 2022; July 14, 2022; and August 18, 2022.

Background

In 1980, the General Assembly exempted farm wineries from the three-tier system of distribution and allowed farm wineries to sell wine directly to VABC's retail licensees. However, on July 1, 2006, a U.S. district court invalidated Virginia's alcohol distribution laws, and farm wineries were then also required to use the three-tier distribution system to sell their wines. The financial impact of this decision was felt by many of the wineries. They were either too small for a wholesale distributor to consider, or the cost to participate in the distribution system was too high. In 2007, the General Assembly enacted legislation that required the Commissioner of Agriculture and Consumer Services (Commissioner) to establish and operate a non-profit, non-stock corporation to promote, develop, and sustain markets for licensed Virginia wineries and farm wineries and to provide wholesale wine distribution services to wineries and farm wineries. The Commissioner subsequently established the VWDC.

VWDC is governed by a board of directors that includes the Commissioner and four members appointed by the Board of Agriculture and Consumer Services, including (i) one owner or manager of a winery or farm winery licensee that is not served by a wholesaler when the owner or manager is appointed to the VWDC Board, (ii) one owner or manager of a winery or farm winery licensee that produces no more than 10,000 cases per year, and (iii) two owners or managers of wine wholesaler licensees. In making appointments to the VWDC Board, the Board of Agriculture and Consumer Services must consider nominations of winery and farm winery licensees submitted by the Virginia Wineries Association and wine wholesale licensees submitted by the Virginia Wine Wholesalers Association. VWDC is required to report to the Commissioner at least annually on its activities, including reporting the quantity of wine distributed for each winery and farm winery during the preceding year.

Many wineries in the Commonwealth use VWDC to distribute up to 3,000 cases of their wine products each year. These wholesale products are sold to retailers through the VWDC's website and subsequently delivered to the purchaser by the member wineries. Today, more than 200 wineries in the Commonwealth are signed on with VWDC.

From 2008 to 2012, VDACS contracted with a third party to conduct the operations functions of the VWDC. By 2012, the complexity of regulatory compliance and mandated reporting responsibilities made it necessary for VDACS to directly administer VWDC operations. The General Assembly appropriated additional general fund support in 2012, and VDACS hired a full time Operations Manager to serve as the VWDC Program Director. The agency also implemented an enhanced online order system and reporting software.

VWDC provides the following benefits to participating wineries:

- ☐ Allows smaller wineries and cideries to market their products in a cost-effective manner to a broader audience of business customers.
- ☐ Offers retailers 24-hour access to local wineries and cideries online at www.vwdc.org.
- ☐ Allows wineries and cideries to deliver their own wine directly to retail stores and restaurants.
- ☐ Increases the ease of conducting business for wineries and cideries – VWDC files, collects, and pays wine or cider taxes monthly directly to VABC for each licensed operation.

VWDC's operations model consists of the following key elements:

- Licensing – Wineries complete an online registration request for VWDC to obtain a wholesaler's license for their products. VWDC works with the winery to obtain all necessary information for the two-part application process with VABC and requires the signature of the VWDC Operating Agreement, which outlines all of the required procedures and regulations.
- Ordering – Retailers submit an order via the online ordering system. Wineries are electronically notified of the order and work directly with the retailer to coordinate delivery and payment.
- Financial – VWDC pays winery partners monthly for all completed and paid transactions occurring during the previous month. VWDC calculates, pays, and reports the taxes for processed transactions and collects a per-transaction fee.
- Compliance – VWDC files and pays liter taxes directly to VABC monthly for each licensee, processes annual renewals, and works with VABC to ensure each licensee is in compliance with current regulations.
- VWDC collects a fee of \$6 per transaction processed, as established by the VWDC Board.
- The general fund allocation covers approximately 85 percent of VWDC operations costs.

The 10-year growth data for the VWDC is as follows:

| Year | Annual Sales | Transaction Qty | Case Sales |
|------|--------------|-----------------|------------|
| 2012 | \$2.2m | 6,900 | 18,000 |
| 2022 | \$6.2m | 9,876 | 39,000 |

Work Group Discussion Objectives

In order to address the questions posed by the General Assembly and reflect the discussions held during the Work Group meetings, the group agreed on the following parameters:

1. No recommendation could be made that would harm or detract from the existing VWDC model.
2. Any recommendations made must realistically account for any anticipated operation cost, technology challenges, regulatory complexities, and staffing requirements needed to be sustainable.
3. All recommendations must include a realistic timeline for implementation.

Discovery

The initial meeting on June 1, 2022, began with discovery. Following a presentation summarizing the VWDC history and operations, VABC delivered a presentation that provided legal definitions related to beer and wine and explained the regulatory differences between winery and brewery licenses. Key differences include:

- *Agricultural requirements:*
 - **Farm winery licenses**, which shall authorize the licensee to **manufacture wine containing 21 percent or less of alcohol by volume and to sell, deliver, or ship the wine, in accordance with VWDC Board regulations**, in closed containers, to (i) the VABC Board, (ii) persons licensed to sell the wine so manufactured at wholesale for the purpose of resale, or (iii) persons outside the Commonwealth. In addition, the licensee may (a) acquire and receive deliveries and shipments of wine and sell and deliver or ship this wine, in accordance with VABC Board regulations, to the VABC Board, persons licensed to sell wine at wholesale for the purpose of resale, or persons outside the Commonwealth; (b) operate a contract winemaking facility on the premises of the licensee in accordance with VABC Board regulations; and (c) store wine in bonded warehouses located on or off the licensed premises upon permits issued by the VABC Board. For the purposes of this title, a farm winery license shall be designated either as a Class A or Class B farm winery license in accordance with the limitations set forth in Va. Code § [4.1-219](#). A farm winery may enter into an agreement in accordance with VABC Board regulations with a winery or farm winery licensee operating a contract winemaking facility.
 - **Such licenses shall also authorize the licensee to sell wine at retail at the places of business designated in the licenses, which may include no more than five additional retail establishments of the licensee. Wine may be sold at these business places for on-premises consumption and in closed containers for off-premises consumption, provided that any brand of wine not owned by the farm winery licensee is purchased from a wholesale wine licensee.** In addition, wine may be pre-mixed by the licensee to be served and sold for on-premises consumption at these business places.
 - There are two classifications of farm winery licenses:
 - **Class A - At least 51 percent of fruits or agricultural products used by licensee to manufacture wine are grown or produced on such farm.** No

more than 25 percent of the fruits, fruit juices, or other agricultural products shall be grown or produced outside the Commonwealth.

- **Class B – 75 percent of fruits or agricultural products used by licensee to manufacture wine are grown or produced in the Commonwealth.** No more than 25 percent of the fruits, fruit juices, or other agricultural products shall be grown or produced outside the Commonwealth. Must have operated under an existing Virginia farm winery license for **at least seven years.**

- **Limited brewery licenses**, to breweries that **manufacture no more than 15,000 barrels of beer per calendar year, provided that (i) the brewery is located on a farm in the Commonwealth on land zoned agricultural and owned or leased by such brewery or its owner and (ii) agricultural products, including barley, other grains, hops, or fruit, used by such brewery in the manufacture of its beer are grown on the farm.** The licensed premises shall be limited to the portion of the farm on which agricultural products, including barley, other grains, hops, or fruit, used by such brewery in the manufacture of its beer are grown and that is contiguous to the premises of such brewery where the beer is manufactured, exclusive of any residence and the curtilage thereof. However, the VABC Board may, with notice to the local governing body in accordance with the provisions of Va. Code § [4.1-230](#), also approve other portions of the farm to be included as part of the licensed premises. For purposes of this subdivision, "land zoned agricultural" means (a) land zoned as an agricultural district or classification or (b) land otherwise permitted by a locality for limited brewery use. For purposes of this subdivision, "land zoned agricultural" does not include land zoned "residential conservation." Except for the limitation on land zoned "residential conservation," nothing in this definition shall otherwise limit or affect local zoning authority. Limited brewery licensees shall be treated as breweries for all purposes of this title except as otherwise provided. There are 321 breweries in Virginia, of which 47 are limited license breweries.

- *Volume classifications:*

- Farm wineries – there are two classifications of farm winery licenses:
 - 5,000 or less gallons
 - Over 5,000 gallons
- Limited breweries – there are three classifications of limited brewery licenses:
 - Up to 500 barrels
 - 501 to 10,000 barrels
 - 10,001 to 15,000 barrels

- *VABC reporting and tax payment – farm wineries, breweries, and wholesalers*

- Wineries – reports and payment due by 15th of each month, for the preceding month.
 - Wine Excise Tax = \$.40/liter
 - Cider Excise Tax = \$.08/liter
- Breweries – reports and payment due by 10th of each month, for the preceding month.

- Twenty-five and sixty-five hundredths cents per gallon per barrel;
 - Two cents per bottle on bottles of not more than seven ounces each;
 - Two and sixty-five hundredths cents per bottle on bottles of more than seven ounces each but not more than 12 ounces each; and
 - Two and twenty-two one hundredths mills (a mill is equivalent to a tenth of a cent) per ounce per bottle on bottles of more than 12 ounces each.
- *Other distinctions between wine and beer*
 - The distribution model in place for beer wholesalers has a strict franchise agreement that does not allow distribution territories contained in agreements to overlap.
 - The shelf life for beer is much shorter than for wine, and this will result in higher transaction volumes for any distribution model.
 - Breweries produce a high volume of seasonal varieties, meaning the variety of beers offered can change with greater frequency, whereas wineries do not change varietal production as often.
 - Grains needed for brewing beer are challenging to grow cost effectively in Virginia due to the climate.
 - One barrel of beer equals 31.5 gallons, and one case of wine equals 2.25 gallons.
 - The most restrictive brewery license allows for up to 500 barrels, which would equal 7,000 cases of wine.

In the discussion following the overview of the VWDC and its creation, the Virginia Wineries Association and the Virginia Beer Wholesalers Association felt strongly that the promotion and increase in sale of Virginia agricultural products was the reason the General Assembly created the VWDC and provided general fund support for the distribution of Virginia wines. The necessary grains and other inputs used in producing beer are difficult to grow cost effectively in Virginia and, therefore, are often acquired from outside of the Commonwealth. Beers manufactured in Virginia, including those manufactured by limited license breweries, may contain a lower percentage of Virginia agricultural products as compared to wines manufactured in Virginia. Therefore, supporting breweries similarly to wineries by incorporating them into the VWDC or a similar distribution mechanism does not necessarily promote Virginia agriculture, which makes it difficult to equate wine and beer. The agricultural product component difference between the two industries presented a consistent divide throughout the three Work Group meetings.

The Virginia Craft Brewers Guild stated that its organization's objective is to provide a distribution vehicle for Virginia's craft breweries because larger distribution companies are not accessible. The intent of a governmental distribution vehicle is to gain brand recognition, "test the waters" of distribution, allow breweries to experiment with seasonal varieties, and provide a path to working with a larger traditional distributor.

Work Group Discussions

Chapter 334 of the 2022 Acts of Assembly directed the Work Group to:

- (i) Conduct research to determine the appropriate fee structure and general fund appropriation necessary to adequately address staffing needs and perform information technology system upgrades for the purpose of accommodating winery, farm winery, and limited brewery licensees that wish to utilize the services of the VWDC;
- (ii) Evaluate the number of barrels of beer allowed to be distributed by a limited brewery licensee over the course of one year; and
- (iii) Review and evaluate alternative avenues of distribution, other than distribution through the VWDC, that could be made available to limited brewery licensees

Organizational Structure

The Work Group's discovery process determined that breweries and wineries may be too different to consider combining the distribution under the existing VWDC. The differences guided the discussion towards the creation of a separate entity, with a separate board of directors (including the Commissioner) and operations manager, operating under the umbrella of VDACS and benefiting from shared administrative resources.

All participants of the Work Group agreed that the VWDC should continue as it was created and intended and that the Work Group discussion would concentrate on using the VWDC as a model where applicable and not as the vehicle for beer distribution.

The Work Group determined that, if created, a newly formed entity for the limited license breweries should have the same structure as the VWDC. The board of directors of such corporation should be composed of the Commissioner and four members appointed by the Board of Agriculture and Consumer Services, including one owner or manager of a limited license brewery that is not served by a wholesaler when the owner or manager is appointed to the board; one owner or manager of a brewery that produces no more than 100,000 barrels per year; and two owners or managers of brewery wholesaler licenses. In making appointments to the board of directors, the Board of Agriculture and Consumer Services should be required to consider nominations of breweries submitted by the Virginia Craft Brewers Guild and brewery wholesale licensees submitted by the Virginia Beer Wholesalers Association.

Membership – Size and Qualifications

Chapter 334 required the Work Group to gather information and report on results for limited license breweries; however, the group felt it important to consider options that would include the other breweries in Virginia. Expanding participation may allow for economies of scale and increased fee revenue that may limited the appropriation needed for continued operation.

The group's discussion regarding membership was varied. Below are the ideas captured from the statements of various Work Group members:

- The set-up cost for a distribution company would be the same regardless of the number of participating breweries, making a case for including a broader membership beyond limited license breweries in order to generate nongeneral fund revenue to support operations.
- The VWDC model was created to support Virginia agriculture, and wineries are required to include a specific percentage of Virginia grown products in their wine products. The licensing requirements for breweries do not require a specific percentage of Virginia agricultural inputs.

- If the intent is to incentivize Virginia grown products within the existing brewery licensing structure, it may be possible to create an agricultural requirement for membership or tiers of membership based on the level of agricultural ingredients included in the products.
- As another option, higher transaction fees could be captured for breweries not using Virginia agricultural ingredients.
- The Virginia Beer Wholesalers Association suggests initially only allowing limited licensees to participate, and after two years (or an appropriate timeframe as determined by the board), open participation to all Virginia breweries.

Volume/Transaction Limitations

In an effort to determine an appropriate volumetric limitation for the distribution of beer, the group reviewed the VWDC case limit for wine (as established by Va. Code § 4.1-206.2) as well as historical sales data and attempted to create a model of comparison. Because of certain similarities between cider and beer, including shelf life, typical packaging, and seasonal variety production, it was suggested by some members that cider, which is classified and regulated as a wine by Virginia law, may be more analogous to beer. The group reviewed and discussed several comparison models to generate a sales volume maximum, ranging from volume in gallons to annual revenue generated.

The ideas captured in this discussion are as follows:

- The primary purpose of this distribution company should be to provide breweries with a distribution model in order to assist their growth and eventual graduation to an established, traditional wholesale distribution company. The limitations set forth should be in the spirit of this goal.
- The 3,000 case limit for wineries may be very close to a farm winery's entire production for the year. Without a Virginia agricultural requirement, the production capabilities for breweries are limited only by the production resources of each brewery.
- If approved to be created, the beer barrel volume needs to be clearly expressed in legislation, as the VABC code does not clearly identify beer barrel volume. For the purposes of this discussion, a barrel of beer is equal to 31 gallons.
- The Virginia Beer Wholesalers Association would support a 250 barrel distribution limit for breweries participating in the newly formed distribution company. This volume equates to 500 kegs per year, or 40 kegs per month.
- The Virginia Craft Brewers Guild is requesting the limitation to be established at no less than 1,500 barrels per year but prefers a limit of 2,000 barrels per year. The volume of 1,500 barrels equates to 3,000 kegs per year, or 250 kegs per month.
- The Virginia Wineries Association expressed concern over the ability of small breweries to self-distribute 1,500 barrels of beer and noted that these quantities seem out-of-scope for the requested report.
- As a volume comparison to the 3,000 case limit for wine distribution under the VWDC, 230 barrels of beer are equivalent in volume to 3,000 cases of wine or cider.

| Using Revenue as the UOM for Comparison (Cider) |
|---|
| <p>Avg Wholesale Price for Case of Cider = \$60</p> <p>3,000 Cases of Cider @ \$60/each = \$180,000</p> <p>Avg Wholesale price for Barrel of Beer = \$240</p> |
| 750 Barrels of Beer \$ 240/each = \$180,000 |

- As a revenue comparison to the data from VWDC for cider sales, 750 barrels of beer are equivalent to the estimated revenue produced by 3,000 cases of cider.

| Using Revenue as the UOM for Comparison |
|---|
| <p>Avg Wholesale Price for Case of Cider = \$60</p> <p>3,000 Cases of Cider @ \$60/each = \$180,000</p> <p>Avg Wholesale price for Barrel of Beer = \$240</p> |
| 750 Barrels of Beer \$ 240/each = \$180,000 |

- As an estimated revenue comparison to the data from VWDC for wine sales, 2,000 barrels of beer are equivalent to the revenue produced by 3,000 cases of wine.

| Using Revenue as the UOM for Comparison (Wine) |
|---|
| <p>Avg Wholesale Price for Case of Wine = \$161</p> <p>3,000 Cases of Wine @ \$160/each = \$480,000</p> <p>Avg Wholesale price for Barrel of Beer = \$240</p> |
| 2,00 Barrels of Beer \$ 240/each = \$480,000 |

Services Provided to Members

The Work Group reached consensus that services similar to those offered by VWDC to its members should be provided to breweries through a beer distribution company. The benefits of these services include:

- ☐ Allow smaller breweries to market and sell their products in a cost-effective manner to a much larger audience.
- ☐ Provide retailers with 24-hour access to local breweries at the push of button via an online ordering platform.
- ☐ Allow breweries to deliver their own beer directly to stores and restaurants.
- ☐ Increase the ease of conducting business for breweries – distribution company files, collects, and pays brewery taxes monthly directly to the Virginia ABC for each licensed operation.

Proposed Fee Structure – Anticipated Revenue

The Work Group reached consensus that the fee structure for the proposed beer distribution company should be set by the distribution company board of directors. This will allow for the greatest flexibility to respond to changes in markets and participant needs and is consistent with the VWDC model.

There are some features of beer distribution that may limit the ability of the fee structure to capture the costs of program administration. The transaction volume may be higher due to the shorter shelf life of beer (three months average), and breweries may produce many different seasonal products, thus increasing the administrative burden required to manage VABC label approvals for each catalog. In addition, the tax structure is more complicated for beer than for wine and the differing agricultural requirements may add to administrative complexity.

Below are the ideas captured from the Work Group discussion regarding an appropriate fee structure:

- The less clear link with agriculture may make sustained general fund support less desirable, so the fee structure should be determined based on the goal of producing a self-sustaining organization.
- It may be possible to have two different fee structures to incentivize the inclusion of Virginia agricultural products in beer. The cost to administer and monitor should be considered.
- The Virginia Craft Brewers Guild suggested that fees be based on a percentage of sales.
- If participation is expanded beyond limited license breweries, it may be possible to differentiate through the fee structure with lower fees charged for limited license brewery participants.
- For parity with the VWDC, the fee structure should support at least 15 percent of the operating costs in year two, with the intention to move toward a greater percentage and possible self-sufficiency. Based on the estimated costs of operations in year two of \$373,800 (discussed below), then 15 percent equals \$56,070.

Anticipated Operating Costs – Licenses/Infrastructure/Staffing

The anticipated costs of creating a distribution vehicle for limited license breweries are based on the following:

- Past and current operations costs for the VWDC.
- VABC license fees for brewery licenses.
- VABC tax structure for beer.

- The estimated infrastructure costs for software development are significant and based on discussions with current information technology providers. The differences in container sizes, seasonal products, and tax reporting required for beer cannot be accommodated with the existing software used by the VWDC.
- Startup costs for initial setup of the beer distribution function exist whether there is parallel structure for beer and wine or not.

The chart below shows the anticipated startup costs as well as year two operating costs after the infrastructure is developed.

| Category | Year 1 | Year 2 | Notes |
|---------------------------|------------------|------------------|---|
| Agency Support / Overhead | \$25,000 | \$25,000 | |
| Banking/Insurance | \$30,000 | \$30,000 | |
| Infrastructure | \$400,000 | \$40,000 | Year one includes initial system implementation and monthly hosting. Year two includes monthly hosting and additional software development if needed. |
| Licensing | \$56,400 | \$6,000 | Year one : Application fees @ \$195 each, Initial License Fees @ \$1005 for 47 Breweries. Year two: Estimate 5 new Breweries (Application fee & initial license fee)* |
| Marketing | \$47,000 | \$47,000 | |
| Reserve | \$20,000 | \$20,000 | |
| Staffing | \$205,800 | \$205,800 | Includes Operations Manager and Financial Specialist position |
| Total | \$784,200 | \$373,800 | |

Notes:

- Year 1 – General Fund to cover 100% of costs. Year 2 – General Fund to cover 85% of costs, based on roughly 15% coming from transaction fee revenue.
- Year 2 transaction fees should equal approximately \$56,070 to serve as 15% of overall budget
- *Initial application fee and license fee to be paid by Distribution Company. Renewals to be paid by brewery.

The below calculation may provide an illustration of the required participation to generate revenues equaling 15 percent of operations costs.

If 30 limited license breweries chose to participate in a newly formed distribution company with a distribution limitation of 250 barrels per year and each of the 30 breweries reached that maximum distribution, that would equate to 7,500 barrels distributed. Using the average wholesale pricing of \$240 per barrel, the necessary fee would be 3.125 percent of sales, or \$7.50 per barrel, in order to generate the 15 percent of operations costs, estimated to be \$56,070.

Timeline for implementation

VDACS estimates that the necessary infrastructure for such a distribution company could be developed approximately 12-18 months following the provision of the necessary resources to support the endeavor. If legislation is introduced and passed to establish a brewery distribution company during the 2023 Session of the General Assembly, it is estimated that operations would begin in July 2024 or January 2025.

Conclusion

This report presents an accurate and complete documentation of the Work Group's findings, discussions, recommendations, and points of consensus. All three Work Group meetings were well attended by the participants listed above, who each demonstrated their commitment to participating in the group.

The topics on which the Work Group reached consensus are:

- The existing VWDC model should not be disrupted.
- The differences between beer and wine, including practical and regulatory differences, make the combination of distribution under the existing VWDC unacceptable to all parties.
- The agricultural requirements for Virginia wine production is the basis for the existing general fund appropriation and support for the VWDC.
- Should a policy decision be made to allow for distribution of beer in a similar manner to VWDC, then parties agree that a separate entity should be formed for the limited distribution of Virginia beers.
- The following operating parameters were discussed with general agreement by the group: organizational structure, services provided, estimated costs, and implementation timeline.

The areas in which consensus was not reached are:

- Membership and size qualifications
- Volume and transaction limitations
- Fee structure

APPENDIX A

VWDC Background Presentation



Virginia Winery Distribution Company Operations Overview

OUR STORY

■ 1980

The General Assembly exempted farm wineries from the three-tier system of distribution and allowed them to sell directly to ABC licensees.

■ 2006

A U.S. district court invalidated Virginia's distribution laws, and farm wineries were then required to use the three-tier distribution system to sell their wines. The financial impact of this decision was felt by many of the wineries. They were either too small for a wholesale distributor to consider, or the costs were too high.

■ 2007

The General Assembly approved legislation allowing small farm wineries to distribute as many as 3,000 cases of their own wine each year to stores and restaurants through the state agriculture department.

■ 2008

Virginia Winery Distribution Company (VWDC) was born and brought wholesale distribution back to the farm wineries. For the first years of the corporation's existence, the daily activities were managed through a contract with a private wholesaler.



OUR STORY - CONTINUED

■ 2010

The complexity of compliance and reporting responsibilities made it necessary to discontinue contractual services for VWDC operations and VDACS assumed daily management.

■ 2012

- VDACS submitted a budget amendment and was appropriated funding to support a dedicated staff position for VWDC winery assistance, training, compliance, and decision making. VDACS hired a full time Operations Manager to serve as the VWDC Program Director.
- Transition to our current online ordering platform performed

■ 2022

Today, more than 250 wineries in the Commonwealth of Virginia are signed on with VWDC. It is a non-profit, non-stock corporation created by the Virginia Department of Agriculture and Consumer Services (VDACS) to provide wholesale wine distribution services for Virginia farm wineries. Many wineries in the Commonwealth use VWDC to distribute and personally deliver their wines to local retailers.



A

VWDC BOARD

The board of directors of such corporation shall be composed of the Commissioner and four members appointed by the Board, including one owner or manager of a winery or farm winery licensee that is not served by a wholesaler when the owner or manager is appointed to the board; one owner or manager of a winery or farm winery licensee that produces no more than 10,000 cases per year; and two owners or managers of wine wholesaler licensees. In making appointments to the board of directors, the Board shall consider nominations of winery and farm winery licensees submitted by the Virginia Wineries Association and wine wholesale licensees submitted by the Virginia Wine Wholesalers Association (§ 3.2-102.B.2, Code of Virginia).








SERVICES PROVIDED TO MEMBERS

- Allows smaller wineries and cideries to market their products in a cost-effective manner to a much larger audience.
- Gives retailers 24-hour access to local wineries and cideries at the push of button @ vwdc.org.
- Wineries and cideries are able to deliver their own wine directly to stores and restaurants.
- Ease of doing business – VWDC files, collects and pays wine or cider taxes monthly directly to the Virginia ABC for each licensed operation.



OPERATIONS - LICENSING



- 1. REGISTER** Wineries complete online at www.vwdc.org using their farm winery license number. 
- 2. SUBMIT**  VWDC will submit the initial application and pays the application fee to ABC. VWDC notifies wineries of initial ABC approval.
- 3. DOCUMENTS** Wineries submit operating documents to VWDC including products for sale, floor plan, and delivery counties. 
- 4. POSTING & PUBLISHING** Wineries post the required ABC notice at their winery location for two weeks. VWDC publishes a corresponding legal notice in your local newspaper. 
- 5. LICENSE ISSUANCE**  VWDC pays the initial license fee and ABC issues the license to VWDC. VWDC will send the license to the winery, to be displayed in the approved VWDC space.



OPERATIONS - ORDERS



1. CREATE ORDER

A purchase order is created in the system by either the winery or the retailer.



2. ACCEPTANCE

Winery reviews and accepts the order, then contacts the retailer to work out delivery logistics.



3. DELIVERY

Winery moves products to the approved VWDC space before delivery. Upon delivery of goods, wineries collect payment and have the retailer sign the invoice.



4. PAYMENT

Payment received upon delivery. Checks mailed to VWDC lockbox for payment processing. Payments also received via Fintech or iControl (third party payment processor).



OPERATIONS - FINANCIAL



1. PAYMENT



VWDC pays out winery partners for all transactions no less than once a month. Transactions received after the last date of the month are paid in the subsequent month.

2. FEES AND TAXES



Winery payments are reduced by transaction fees and ABC taxes.

3. REPORTING



VWDC performs monthly bank reconciliations, monthly ABC tax reporting, completes monthly and annual financial reporting.



OPERATIONS - COMPLIANCE



1. TAXES

VWDC files and pays liter taxes directly to ABC monthly for each VWDC license.



2. RENEWALS

ABC bills VWDC for license fees. VWDC notifies wineries of license renewals and processes fee payments. Wineries are responsible for renewal fees.



3. ACTIVITIES

Compliance with applicable laws and regulations in maintaining VWDC license (documentation, licensed space, wine sales activities, agents).

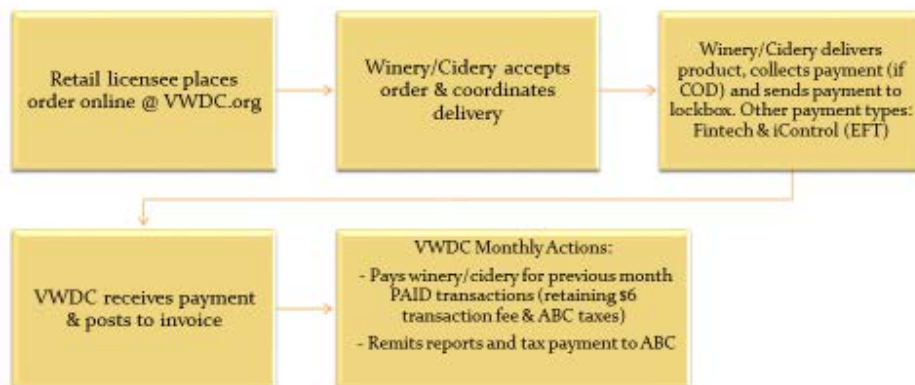


4. AUDIT

Relationship with ABC Law Enforcement to strengthen compliance efforts of VWDC (on-site audits, site visits, new licensees).



VWDC PROCESS



MONTHLY REPORTING

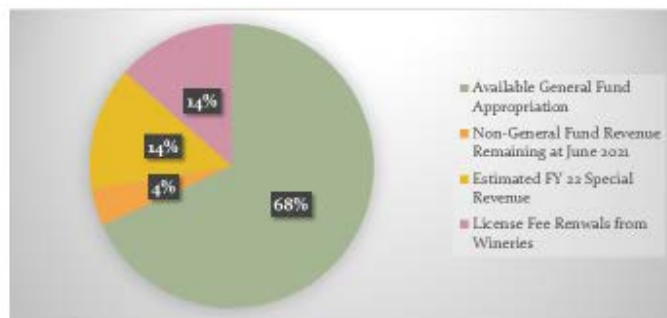
- ABC Tax report & payment – due by the 15th of each month
 - For previous month transactions
- Winery / Cidery payments – due by the 15th of each month
 - Payments are disbursed for paid transactions occurring in the previous month
- VWDC Financial reporting
 - Bank Reconciliation
 - Financial Statements



4

FUNDING

| Resource | Total |
|--------------------------------------|-----------|
| General Fund Appropriation | \$242,399 |
| Non General Fund remaining June 2021 | \$15,000 |
| Estimated FY22 Special Revenue | \$50,000 |
| License Fee Renewals from Wineries | \$48,220 |
| Total | \$355,619 |



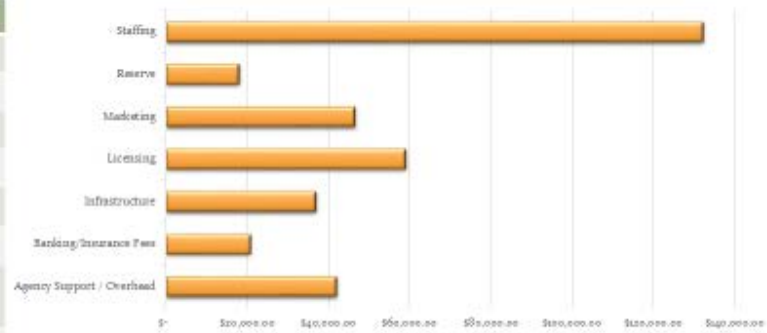
Special Revenue – Generated by collecting fee of \$6 per transaction



5

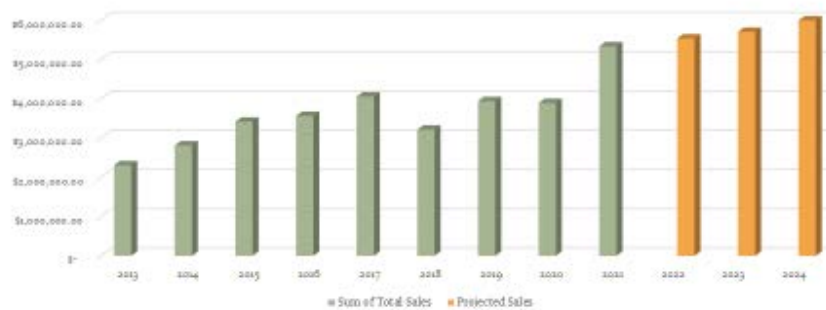
OPERATIONS COSTS (BUDGETED)

| Category | Total |
|-------------------------|------------------|
| Staffing | \$132,269 |
| Reserve | \$18,000 |
| Marketing | \$46,600 |
| Licensing | \$59,000 |
| Infrastructure | \$37,000 |
| Banking/Insurance | \$20,750 |
| Agency Support/Overhead | \$42,000 |
| Total | \$355,619 |



SALES BY FISCAL YEAR

(REPORTING BASED ON FISCAL YEAR BEGINNING IN JULY AND ENDING IN JUNE)

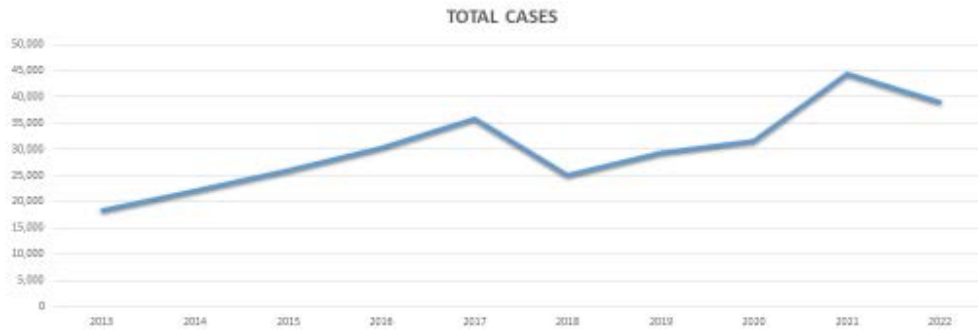


- Sales \$2.3 million (2013) grew to \$5.3 million in (2021). Current FY22 Sales - \$5.1 million (July 2021 – April 2022)
- Sales are projected to reach \$6 million by 2024



CASE SALES BY FISCAL YEAR

(REPORTING BASED ON FISCAL YEAR BEGINNING IN JULY AND ENDING IN JUNE)



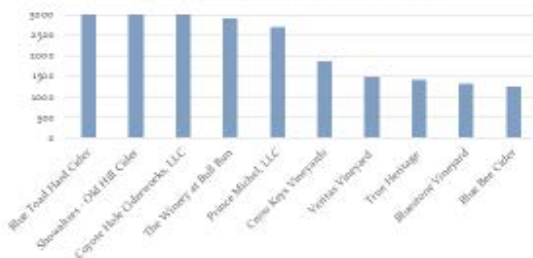
Cases sold grew from 18,000 (2012) to 39,000 (2022)



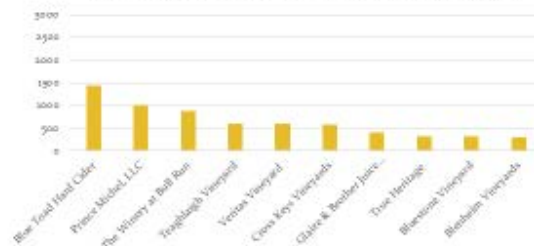
TRANSACTION LIMITS / CURRENT UTILIZATION

The Board may grant a wholesale wine license to a nonprofit, nonstock corporation created in accordance with subdivision B 2 of § 3.2-102, which shall authorize the licensee to provide wholesale wine distribution services to winery and farm winery licensees, provided that no more than 3,000 cases of wine produced by a winery or farm winery licensee shall be distributed by the corporation in any one year.

Top 10 Case Sales – CY 2021



Top 10 Case Sales – CY 2022 (as of 4/30/22)



TRANSACTIONS



While the Transaction qty has stayed within the range of 7,000 to 10,000, the average transaction total has more than doubled (\$317 in 2013 to \$636 in 2022)

ANTICIPATED VWDC NEEDS

- Infrastructure – Existing online ordering platform approaching end of life, needs redesign
- Marketing – Wineries have requested additional marketing assistance
- Staffing – Increasing membership will require additional staffing



ASSUMPTIONS FOR BREWERIES

- Winery funding is not subsidizing the addition of Breweries
- General Fund Appropriation
- Transaction Fees will generate the same percentage of the budget as wine model (Approximately 15%)
- Brewery operating budget will cover expenses of necessary staffing



BREWERY COST ESTIMATES

| Category | Year 1 | Year 2 | Notes |
|---------------------------|------------------|------------------|---|
| Agency Support / Overhead | \$25,000 | \$25,000 | |
| Banking/Insurance | \$30,000 | \$30,000 | |
| Infrastructure | \$310,000 | \$40,000 | Year one includes initial system implementation and monthly hosting. Year two includes monthly hosting and additional software development if needed. |
| Licensing | \$50,400 | \$48,210 | Year one : Application fees @ \$195 each, License Fee @ \$1005 for 43 Breweries. Year two: License fee renewals and estimate 5 new Breweries |
| Marketing | \$47,000 | \$47,000 | |
| Reserve | \$20,000 | \$20,000 | |
| Staffing | \$205,800 | \$205,800 | Includes Operations Manager and Financial Specialist position |
| Total | \$688,200 | \$416,010 | |

Notes:

- Year 1 – General Fund to cover 100% of costs. Year 2 – General Fund to cover 85% of costs, based on roughly 15% coming from transaction fee revenue.
- Year 2 transaction fees should equal approximately \$63,000 to serve as 15% of overall budget (10,500 transactions @ \$6 each)



APPENDIX B

Virginia Alcoholic Beverage Authority Presentation

Virginia Alcoholic Beverage Authority

HB1336 Work Group



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VA ABC Farm Winery Licenses

Farm winery licenses, which shall authorize the licensee to manufacture wine containing 21 percent or less of alcohol by volume and to sell, deliver, or ship the wine, in accordance with Board regulations, in closed containers, to (i) the Board, (ii) persons licensed to sell the wine so manufactured at wholesale for the purpose of resale, or (iii) persons outside the Commonwealth. In addition, the licensee may (a) acquire and receive deliveries and shipments of wine and sell and deliver or ship this wine, in accordance with Board regulations, to the Board, persons licensed to sell wine at wholesale for the purpose of resale, or persons outside the Commonwealth; (b) operate a contract winemaking facility on the premises of the licensee in accordance with Board regulations; and (c) store wine in bonded warehouses located on or off the licensed premises upon permits issued by the Board. For the purposes of this title, a farm winery license shall be designated either as a Class A or Class B farm winery license in accordance with the limitations set forth in § 4.1-219. A farm winery may enter into an agreement in accordance with Board regulations with a winery or farm winery licensee operating a contract winemaking facility.

- Such licenses shall also authorize the licensee to sell wine at retail at the places of business designated in the licenses, which may include no more than five additional retail establishments of the licensee. Wine may be sold at these business places for on-premises consumption and in closed containers for off-premises consumption, provided that any brand of wine not owned by the farm winery licensee is purchased from a wholesale wine licensee. In addition, wine may be pre-mixed by the licensee to be served and sold for on-premises consumption at these business places.
- There are two classifications of farm winery licenses:
- Class A** – At least 51% of fruits or agricultural products used by licensee to manufacture wine are grown or produced on such farm. No more than 25 percent of the fruits, fruit juices or other agricultural products shall be grown or produced outside the Commonwealth. —\$245
- Class B** – 75% of fruits or agricultural products used by licensee to manufacture wine are grown or produced in the Commonwealth. No more than 25 percent of the fruits, fruit juices or other agricultural products shall be grown or produced outside the Commonwealth. NOTE: Must have operated under an existing Virginia farm winery license for at least seven years. —\$4,750



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Winery Licenses

Winery licenses, which shall authorize the licensee to manufacture wine and to sell and deliver or ship the wine, in accordance with Board regulations, in closed containers, to persons licensed to sell the wine so manufactured at wholesale for the purpose of resale, and to persons outside the Commonwealth for resale outside the Commonwealth. In addition, such license shall authorize the licensee to (i) operate distilling equipment on the premises of the licensee in the manufacture of spirits from fruit or fruit juices only, which shall be used only for the fortification of wine produced by the licensee; (ii) operate a contract winemaking facility on the premises of the licensee in accordance with Board regulations; (iii) store wine in bonded warehouses on or off the licensed premises upon permit issued by the Board; and (iv) sell wine at retail at the place of business designated in the winery license for on-premises consumption or in closed containers for off-premises consumption, provided that any brand of wine not owned by the winery licensee is purchased from a wholesale wine licensee and any wine sold for on-premises consumption is manufactured on the licensed premises.

- There are two classifications of Farm winery licenses:
- 5,000 or less gallons—\$215
- Over 5,000 gallons—\$4,210



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Brewery License

Brewery licenses, which shall authorize the licensee to manufacture beer and to sell and deliver or ship the beer so manufactured, in accordance with Board regulations, in closed containers to (i) persons licensed to sell the beer at wholesale and (ii) persons outside the Commonwealth for resale outside the Commonwealth. Such license shall also authorize the licensee to sell at retail at premises described in the brewery license (a) the brands of beer that the brewery owns for on-premises consumption, provided that not less than 20 percent of the volume of beer sold for on-premises consumption in any calendar year is manufactured on the licensed premises, and (b) beer in closed containers, which shall include growlers and other reusable containers, for off-premises consumption.

- There are three classifications of Brewery licenses:
- Up to 500 barrels—\$380
- 501 to 10,000 barrels—\$2,350
- Over 10,000 barrels—\$4,690



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Limited Brewery License

Limited brewery licenses, to breweries that manufacture no more than 15,000 barrels of beer per calendar year, provided that (i) the brewery is located on a farm in the Commonwealth on land zoned agricultural and owned or leased by such brewery or its owner and (ii) agricultural products, including barley, other grains, hops, or fruit, used by such brewery in the manufacture of its beer are grown on the farm. The licensed premises shall be limited to the portion of the farm on which agricultural products, including barley, other grains, hops, or fruit, used by such brewery in the manufacture of its beer are grown and that is contiguous to the premises of such brewery where the beer is manufactured, exclusive of any residence and the curtilage thereof. However, the Board may, with notice to the local governing body in accordance with the provisions of § [4.1-230](#), also approve other portions of the farm to be included as part of the licensed premises. For purposes of this subdivision, "land zoned agricultural" means (a) land zoned as an agricultural district or classification or (b) land otherwise permitted by a locality for limited brewery use. For purposes of this subdivision, "land zoned agricultural" does not include land zoned "residential conservation." Except for the limitation on land zoned "residential conservation," nothing in this definition shall otherwise limit or affect local zoning authority.

- Limited brewery licensees shall be treated as breweries for all purposes of this title except as otherwise provided in this subdivision.



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Limited Brewery Licenses cont.

- There are three classifications of Limited Brewery licenses:
 - Up to 500 barrels—\$380
 - 501 to 10,000 barrels—\$2,350
 - 10,001 to 15,000 barrels—\$4,690



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Reporting Excise Tax

- Farm Wineries and Wine Wholesale
 - Due 15th of each month, for the preceding month.
- Breweries and Beer Wholesale
 - Due 10th of each month, for the preceding month.
- Wineries
 - Due when product is moved from bonded location.



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Reporting Excise Tax cont.

- Pursuant to **§ 4.1-236. Excise tax on beer and wine coolers; payment of tax; exceptions.**
- A. There is levied on all beer and wine coolers sold in the Commonwealth an excise tax at the rate of:
 - 1. Twenty-five and sixty-five hundredths cents per gallon per barrel;
 - 2. Two cents per bottle on bottles of not more than seven ounces each;
 - 3. Two and sixty-five hundredths cents per bottle on bottles of more than seven ounces each but not more than twelve ounces each; and
 - 4. Two and twenty-two one hundredths mills per ounce per bottle on bottles of more than twelve ounces each.



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