

MINISTRY OF SMALL BUSINESS AND RED TAPE REDUCTION  
AND MINISTER RESPONSIBLE FOR THE LIQUOR DISTRIBUTION BRANCH  
**MEETING NOTE**

Cliff #: 37203

Date: November 13, 2015

**PREPARED FOR:** Honourable Coralee Oakes – BC Craft Distilling Association meeting

**DATE AND TIME OF MEETING:** November 17, 2015

**ATTENDEES:** Charles Tremewen (Long Table Distillery); Peter Hunt (Victoria Spirits)

**ISSUE:** Craft Distilling

**BACKGROUND:**

**The BC Craft Distilling Association**

- The BC Craft Distilling Association is a relatively newly formed association with an interest in the Liquor Distribution Branch (LDB)'s Craft Distillery Policy.
- According to the Association, their mission is to provide an inclusive platform for distillers licensed in BC that promotes responsible growth of an innovative and vibrant craft spirits industry within the province.
- The Association has members that are designated as both 'craft' and 'commercial' distilleries by the LDB, as well as two that are designated a hybrid (meaning, they can direct-deliver, but are not mark-up exempt).
- The Association is made up of the following members:
  - Victoria Spirits – Victoria (hybrid)
  - Long Table Distillery – Vancouver (hybrid)
  - Island Spirits – Hornby Island (commercial distillery)
  - Urban Distilleries – Kelowna (craft distillery)
  - Arbutus Distillery – Nanaimo (craft distillery)
  - Shelter Point – Campbell River (craft distillery)

**History of the LDB's Craft Distillery Policy**

- The purpose of the LDB's Craft Distillery Policy is to encourage the development of an industry of small distilleries that produce premium spirits, from scratch, using traditional spirit-making techniques and local BC inputs.
- The LDB first introduced a craft distillery policy in 2010, following requests from the Artisan Distillery Guild (now called the Craft Distillers Guild of BC). Under the original policy, only four distilleries met the criteria to qualify for benefits.
- In April 2013, the original policy was replaced with the current policy, following requests from industry for Government to provide benefits to BC's distilleries along the same lines of the benefits provided to BC's wineries.

- For the criteria and benefits associated with each of the original and current policies, please see Appendix A.
- The criteria limit the extent to which government revenue could be negatively impacted, due to the 50,000 litre production cap and the requirement to use 100% BC agricultural inputs in order to receive the full mark-up exemption.
- This full mark-up exemption, and the ability to sell direct to private retailers and the hospitality industry, provides a lucrative incentive for distilleries to meet the criteria set out in the policy.
- There are currently 31 distilleries that have qualified for benefits under the current Craft Distillery Policy and nine applications for the craft designation in progress.

## DISCUSSION:

The BC Craft Distilling Association has made the following requests for changes to the LDB's Craft Distillery Policy and other policies:

### a) Allow for the Use of Neutral Grain Spirits (NGS)

- The Association requests that the LDB's Craft Distillery Policy be expanded to permit the use of NGS.
- NGS is food-grade ethanol produced in bulk at large refinery/distillery plants outside of BC and sold for use in the manufacturing of spirit products. Most of the time, NGS is corn-based and used as a base for a spirit, or simply redistilled (rectified) then bottled.
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- This is not to say that products produced with NGS cannot be of high quality (Victoria Gin, for example), but NGS use is not consistent with the intent of the LDB's policy.
- Since the introduction of the current policy, a number of distilleries that previously used NGS have chosen to no longer do so and have qualified to be designated as craft distilleries under the current policy.

### b) Increase Production Threshold

- Currently, the first 50,000 litres of finished product from a craft distillery qualifies for a mark-up exemption on direct sales to private retailers and the hospitality industry. This mark-up benefit is phased out between 50,000 and 100,000 litres.
- The Association requests the production threshold be changed from 50,000 litres of finished product to 50,000 litres of absolute alcohol (approx. 100,000 litres of finished product).
- The production threshold in the current policy was doubled from that in the previous policy. The phase-out provision up to 100,000 litres is a new addition

that provides for supported growth of the industry,

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c) Apply Production Threshold Only to Sales Within BC

- The Association requests that the production threshold only apply to sales within BC – i.e. not exported product.

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d) Eliminate the Requirement to Use 100% BC Agricultural Inputs

- The Association has requested the requirement that craft distillers use 100% BC agricultural inputs be eliminated.

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- During the development of the current Craft Distillery Policy, industry expressed concern that meeting this requirement would be very difficult once the industry expands because BC has a limited supply of crops that could be used to make spirits. These limitations would be compounded when crop yields are poor, or if there is a crop failure.

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e) Provide Mark-up Reductions for LDB Sales in a Manner Similar to those BC Wineries Receive on Sales through the LDB

- The Association requests a reduction in the mark-up payable on craft distilled spirits sold through the LDB.
- The LDB has a VQA program that provides for rebates on BC VQA wine sold through BC Liquor Stores.

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- The wine industry is highly concentrated in the Okanagan Valley. The close proximity of hundreds of wineries is an ideal situation for drawing tourists and therefore contributing to significant indirect economic activity in the tourism and hospitality industries, such as through restaurants, hotels, tour companies, etc.

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f) Wholesale Pricing Structure for Commercial Distillery Tastings

- Tasting rooms, where commercial distilleries promote their products and in many cases give complimentary tastings for customers, used to pay retail price for the products used for tastings and received a 30% commission on those sales from the LDB.
- As of April 1, 2015, commercial distilleries pay the wholesale price for the products used for tastings and receive a 7% commission – which they suggest puts them at a loss, to supply their tasting rooms with alcohol that is made on-site and never leaves the premises.
- A manufacturer's retail sales are now like any other private retailer's sales – they can now set their retail prices according to the marketplace and keep their retail profits.
- Even though the liquor is made on site and never leaves the premises, commercial distilleries are still required to collect and remit the 124% mark-up on behalf of the LDB.
- Commercial distilleries feel that 'craft' distilleries have an unfair advantage under this model, as craft distilleries keep 100% of the proceeds from sales in their tasting rooms, and can sell directly to the private retailers and the hospitality industry without remitting mark-up to the LDB.

## SUMMARY

- The current Craft Distillery Policy was introduced in April 2013. It is relatively new and its impacts are still being assessed.
- The intent of the policy is to support small BC distillers whose products are made using traditional spirit-making techniques, with BC grown products.

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**ATTACHMENTS:** Appendix A – Comparison of Criteria and Benefits under Original Versus Current Craft Distillery Policies

Contact: Caeli Turner, A/Director, Policy & Communications  
Telephone: 604 252-3196

Reviewed by				
Dir: CT	ED: AW	ADM:	DM:	MIN:

## **Appendix A: Criteria and Benefits – Original vs. Current Craft Distillery Policies**

### *Original craft distillery policy (2010):*

#### Criteria:

- Ferment and distill all products at the licensed distillery site, using traditional distilling techniques, and have production of less than 25,000 litres of finished product annually.
- Production of spirit-based cooler products or other highly processed products were not permitted.

#### Benefits:

- Qualifying distilleries were able to sell their products directly to licensees (bars, restaurants, private liquor stores) and receive a 7% commission based on the retail value on those sales.
- All distilleries that sold products directly to the public at the distillery site received a 30% commission.

### *Current craft distillery policy (2013):*

#### Criteria:

- Ferment and distill all products at the licensed distillery site using 100% BC agricultural inputs, traditional distilling techniques, and have production of less than 50,000 litres of finished product annually.
- The use of neutral grain spirits is expressly prohibited, as is the production of highly processed spirit-based cooler products.

#### Benefits:

- Qualifying distilleries are permitted to sell their products directly to licensees (bars, restaurants, private liquor stores) and the public, with no mark-up applied to the products they sell directly.
- The policy also includes a tiered mark-up once a craft distillery exceeds 50,000 litres, with gradual increases up to 100,000 litres before the full mark-up of 124% is applied.

MINISTRY OF SMALL BUSINESS AND RED TAPE REDUCTION  
AND MINISTER RESPONSIBLE FOR LIQUOR DISTRIBUTION BRANCH  
**INFORMATION NOTE**

Cliff #: 37230

Date: November 25, 2015

**PREPARED FOR:** Honourable Coralee Oakes, Minister of Small Business and Red Tape Reduction and Minister Responsible for Liquor Distribution Branch

**ISSUE:** Timeline of Events – Commercial Wineries

**BACKGROUND:**

- A briefing note sent to the Minister's Office (Attorney General and Minister of Justice, Suzanne Anton, at the time) on April 8, 2015, referred to an "overpayment" of commissions to commercial wineries. This reference was based on an LDB position that cannot be factually demonstrated.
- A complete timeline of events is provided below.

**DISCUSSION:**

- As part of the move to a new wholesale pricing model, the LDB reviewed all sales agreements in place prior to April 1.
- As stated in their pre-April 1 sales agreement, commercial wineries received a 7 per cent commission for their direct-delivery sales to wholesale customers.
- During the review, the LDB determined that the commission was paid based on retail price. The LDB did not think this approach was appropriate and characterized it at the time as a technical error because they believed the vague language in the agreement should be interpreted differently.
- The LDB then amended the sales agreements to clearly state the 7 per cent commission was to be based on wholesale price.
- The commercial wineries were informed of this change. The replacement sales agreements were sent to commercial wineries between March 27 and March 30, 2015.
- In response to this, Josie Tyabji (Constellation Brands) wrote a letter to the LDB's CFO, requesting that the commission rate be increased from 7 per cent to 8.2 per cent to account for the reduced commissions that commercial wineries would receive with the amendment. The LDB denied this request, taking the position with Ms. Tyabji that commissions should have been paid based on the actual price paid and any additional amounts were overpaid in error.
- On April 8, a briefing note was sent to the Minister's Office, informing her of Ms. Tyabji's request and the LDB's response.

- On August 20, the LDB received a freedom of information request from a political party. This request included the April 8 briefing note, along with a number of other briefing notes (FOI # LDB -2015-52718).
- On October 5, in response to the freedom of information request, the April 8 briefing note was sent to the applicant.
- On October 8, the topic was raised in Question Period. Following question period, the LDB was asked to review the matter.
- The LDB further reviewed the matter, including previous sales agreements, and determined that the LDB's original characterization that overpayments had been made in "error" was not factually demonstrable, as the commissions had been paid in this manner during the entire lifespan of the program.
- Given this, the LDB briefed the Minister on the different interpretations of the sales agreement and informed her that the LDB's statement in the briefing note should have been clearly qualified as a position versus a statement of fact.
- Notwithstanding the fact that historical arrangements were based on the retail price, the LDB continues to believe that the commission is more appropriately based on the wholesale amount going forward.

Contact: Melissa Tang, Senior Policy Analyst  
Telephone: (604) 252-3159

Reviewed by				
Dir: CT	ED: AW	ADM: BL	DM:	MIN: