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COLORADO'S SHIFTING PACKAGE ALCOHOL LANDSCAPE: THE EMERGENCE OF THE CHAIN LIQUOR STORE

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(This article first appeared on the National Association of Licensing and Compliance Professionals website. If your liquor-licensed business has locations in multiple states, NALCP is a wonderful resource and organization for your compliance needs.)

Introduction

The alcohol beverage landscape is undergoing significant changes in Colorado in the coming years, particularly regarding package liquor sales. Colorado has two licenses permitting the package sale of beer, wine, and spirits: the Liquor-Licensed Drugstore; and the Retail Liquor Store. In addition, Colorado is among a handful of states that continue to license Fermented Malt Beverages, more commonly known as 3.2% Beer or "near" beer.

Historically, Colorado limited entities and individuals, whether through direct or indirect ownership, to own only one package liquor license. (This is in contrast to 3.2% Beer licenses which permit multiple ownership.) As a result, the Colorado package alcohol landscape includes thousands of independently-owned liquor stores together with chain convenience stores, grocers, or bulk retailers offering 3.2% Beer. In practice, most grocery stores offer 3.2% beer and have an independently-owned package liquor store located within their commercial development or even as a unit within their own building.

There have been numerous attempts over recent years to eliminate these restrictions and permit retailers to hold multiple package liquor licenses. Those attempts regularly failed until this past year when the Colorado General Assembly passed Senate Bill 16-197 ("SB-197") on May 11, 2016. As one might imagine, a number of industry participants were involved in the creation of SB-197 in an effort to reach a compromise protecting existing operators but also allowing expansion of "chain" liquor stores within the State. The result was a 33-page bill that includes three primary components: (1) it expands the number of Liquor-Licensed Drugstores that an entity may own; (2) it expands the number of Retail Liquor Stores that an entity may own; and (3) it eliminates Fermented Malt Beverages by 2019.

This article gives a brief overview of those primary components of SB-197.

Liquor-Licensed Drugstores

The most significant impact of SB-197 is to existing Liquor-Licensed Drugstores. Colorado has less than two dozen Liquor-Licensed Drugstores, several of which are operated by national grocers or bulk retailers. Put simply, a Liquor-Licensed Drugstore is a drugstore licensed by the state board of pharmacy that is also granted a license to sell beer, wine, and spirits for off-premises consumption.

A cause of much confusion and consternation among Colorado licensees is the expansion of the number of Liquor-Licensed Drugstores that a company may operate. Beginning January 1, 2017, SB-197 provides that a company operating a Liquor-Licensed Drugstore, licensed prior to February 21, 2016, may qualify for additional licensed locations as follows:

- Between January 1, 2017 and December 31, 2021, up to 5 total Liquor-Licensed Drugstores;
- Between January 1, 2022 and December 31, 2026, up to 8 total Liquor-Licensed Drugstores;
- Between January 1, 2027 and December 31, 2031, up to 13 total Liquor-Licensed Drugstores;
- Between January 1, 2032 and December 31, 2036, up to 20 total Liquor-Licensed Drugstores; and,
- After January 1, 2037, an unlimited number of Liquor-Licensed Drugstores.

But expansion comes at a cost. For every new location the Liquor-Licensed Drugstore owner seeks to add, it must purchase at least two existing Retail Liquor Store licensees within the new location's community, including all such licensees within a prescribed radius. SB-197 also creates a new application process to transfer, merge, and convert the purchased Retail Liquor Store licenses into a single Liquor-Licensed Drugstore. As with all retail liquor licenses in Colorado, this process is largely overseen by the local authorities and is subject to a public hearing, during which the "reasonable requirements" and "desires" of the surrounding neighborhood must be considered for approval.

In addition to expanding the number of Liquor-Licensed Drugstore outlets that a company may operate, SB-197 places new requirements upon such licensees. Beginning January 1, SB-197 mandates that a Liquor-Licensed Drugstore must show, either for new applications or as part of its renewal, that "at least twenty percent of the licensee's gross annual income [from the prior 12 months]" is derived from "the sale of food items[.]" SB-197 also places new operating conditions upon such Liquor-Licensed Drugstores, including:

- Prohibiting self-checkout of alcohol products;
- Prohibiting the sale of clothing or accessories "imprinted with advertising, logos, slogans, trademarks, or messages related to alcohol beverages";
- Prohibiting any employee, under 21 years of age, from selling, delivering, or having any contact with alcohol beverages.
- Requiring cashiers request – and verify – valid identification from any patron appearing below the age of 50; and,
- Obtaining and maintaining certification as a Responsible Alcohol Beverage Vendor.

Another significant requirement of SB-197 is that Liquor-Licensed Drugstores must qualify at least one "Permitted Manager" to be in control of the alcohol beverage operations of the facility and purchase alcohol for the Liquor-Licensed Drugstore. These Permitted Managers must pass a criminal background check and will be disqualified due to particular criminal convictions. In an interesting interpretation, the Colorado Liquor Enforcement Division has determined that

Permitted Managers will only be required for new Liquor-Licensed Drugstores licensed after January 1, 2017, thus creating a confusing dichotomy between established Liquor-Licensed Drugstores and new licensees. The Division has further required that new Liquor-Licensed Drugstores must always have a Permitted Manager on duty, thus (most likely) requiring the registration of multiple Permitted Managers per store.

Retail Liquor Stores

Colorado's second package license permitting the sale of beer, wine, and spirits is the Retail Liquor Store. Historically, Retail Liquor Stores were only permitted to sell alcohol and a limited supply of approved items, such as ice, mixers, and tobacco. SB-197 eliminates those restrictions by permitting a Retail Liquor Store to carry nonalcohol products, "but only if the annual gross revenues from the sale of nonalcohol products does not exceed twenty percent of … annual gross revenues."

Existing Retail Liquor Store owners were also provided an opportunity to expand, though not at the rate of Liquor-Licensed Drugstores. Beginning January 1, SB-197 provides that a Retail Liquor Store, licensed prior to January 1, 2016 and whose license holder is a Colorado resident, may qualify for additional Retail Liquor Store licenses as follows:

- Between January 1, 2017 and December 31, 2021, up to 2 total Retail Liquor Stores;
- Between January 1, 2022 and December 31, 2026, up to 3 total Retail Liquor Stores; and,
- After January 1, 2027, up to 4 total Retail Liquor Stores.

Unlike Liquor-Licensed Drugstores, a Retail Liquor Store owner is not required to purchase any existing stores in order to expand. The Liquor Enforcement Division has not taken a position clarifying the "Colorado resident" requirement for a license holder, however it proposed – and later rejected – a rule requiring that 50% of the ultimate owners reside with the State. There is federal case law holding that such restrictions are unconstitutional, however the law is unsettled on this point. As a result, Colorado may very well become the next battleground regarding these Commerce Clause arguments.

SB-197 also creates new operating conditions for Retail Liquor Stores, though they are not as extensive as those for Liquor-Licensed Drugstores. Specifically, a Retail Liquor Store may not employ persons under 21 years of age to sell alcohol within its store. Additionally, Retail Liquor Stores are now required to request – and verify – valid identification from any patron appearing below the age of 50.

Distance Restrictions

Another important component of SB-197 applying to both Liquor-Licensed Drugstores and Retail Liquor Stores is the creation of distance restrictions between such licensees. SB-197 provides two separate distance restrictions, based upon the population of the surrounding community: (1) a new Retail Liquor Store or Liquor-Licensed Drugstore may not be situated within 1,500 feet of another off-premises liquor retailer; and (2) in a municipality of 10,000 or fewer people, a new Retail Liquor Store or Liquor-Licensed Drugstore may not be situated within 3,000 feet of another off-premises liquor retailer.

Fermented Malt Beverages (3.2% Beer)

The final primary component of SB-197 includes changes to the 3.2% Beer industry, including the future elimination of this classification in Colorado.

As an initial matter, SB-197 immediately shortens the permitted hours of operation of 3.2% Beer licensees to between 8:00 a.m. and midnight. These regular operating hours are now the same as full-strength package retailers.

Beginning January 1, 2019, SB-197 aligns the definitions for Fermented Malt Beverages and malt liquors (full strength beer) by defining both as beverages created by the fermentation of grains, with an alcohol content greater than one half of one percent by volume. SB-197 goes on to create an Industry Working Group to implement a "process for grocery and convenience stores to apply for a license to sell malt liquor and fermented malt beverages … starting January 1, 2019." Recommendations by this Industry Working Group must be submitted to the respective State Senate House Committees by January 1, 2018.

At this time, no one really knows what this future process may look like. It is anticipated that existing 3.2% Beer licensees will be provided some conversion process, however that process may include additional application requirements and, potentially, additional public hearings to determine the "reasonable requirements" and "desires" of the surrounding neighborhood.

A final tidbit buried within SB-197, which has yet to generate much coverage, is the future prospect of growlers in Retail Liquor Stores. Currently, Retail Liquor Stores may only sell packaged liquors in sealed containers received from wholesalers. But SB-197 mandates that the Industry Working Group "examine and make recommendations regarding … the ability of Retail Liquor Stores … to sell growlers containing malt liquors." This mandate will, almost certainly, raise a great deal of discussion and debate over the next two years.

Conclusion

The fallout from SB-197 will continue for decades. Already, many Retail Liquor Store owners are lining up in their efforts to sell their stores to national chains while others (generally those with locations near existing Liquor-Licensed Drugstores) are free to make substantial sale demands because their proximity prohibits the grocer's expansion. Further clouding the picture is the anticipation of future legislation and rule-making regarding SB-197's implementation, expansion, or narrowing as well as possible lawsuits regarding the legality of certain aspects of the new law. What is – and will almost definitely remain – certain is that chain expansion of package liquor stores is coming to Colorado.