

Nevada's Three-Tier System: Still Strong, Still Being Refined

BY JESSE WADHAMS, ESQ.

Since the original publication of this article in *Nevada Lawyer* in 2015, Nevada has made a number of significant changes to its liquor law. These updates are reviewed throughout.

When the 21st Amendment to the U.S. Constitution repealed Prohibition in 1933, a three-tier system developed throughout the U.S. to govern regulation of alcohol sales. This approach was widely adopted due to its straightforward regulatory structure and ease of revenue collection. In Nevada, the three-tier system is found at NRS 597.120 et seq., and it regulates the manufacture and distribution of alcohol in the state. The stated purpose of this method of regulation is to “protect locally owned and operated business enterprises and those residents whose livelihoods and investments are dependent on their freedom to manage their businesses without economic and coercive control by nonresident suppliers of alcoholic beverages.” *See*, NRS 597.190.

In its most essential form, the three-tier system places suppliers such as wineries, breweries and distilleries on one level; distributors on another; and retailers on a third. Broadly speaking, the three-tier system prohibits the creation of a vertically integrated company as no single entity is permitted to operate on two levels. This requirement is intended to provide a more even playing field for the various participants in the marketplace. For example, a major brewery that manufactures beer will operate as a supplier and have a supplier’s license; however, that same brewery cannot distribute its product to a retailer for sale. In exchange for market participation, the distributors help with compliance and revenue collection.

Under this system, suppliers can sell only to a distributor located in Nevada, and a distributor is specifically prohibited from direct sales to the general public. *See*, NRS 369.130. A distributor is required to possess a state license and takes the first right of ownership once the product enters the state. While there is not a “distributor” license *per*



se, there are two avenues for licensure as a distributor in Nevada – as an importer or a wholesaler. Importers, unlike wholesalers, can only bring the product into the state; they are not permitted to sell to retailers, only to licensed wholesalers. *See*, NRS 369.488. Further, retailers must purchase only from wholesalers (NRS 369.487) and may not legally purchase for resale from other retailers or directly from suppliers. A wholesaler will typically also be a licensed importer, but an importer will not necessarily be a licensed wholesaler.

Alcoholic beverages may be transported into the state of Nevada only by a licensed common carrier: a regularly operating contract carrier or a licensed Nevada importer/wholesaler with a special permit for the transporting vehicle. Importation into Nevada must be made directly to a licensed importer/wholesaler warehouse. Wholesale liquor business and storage must be conducted only from a licensed, designated importer/wholesaler warehouse.

Nevada law has a number of specific protections for distributors in Nevada. Suppliers may only grant one franchise in the state unless specifically agreed to by the parties. *See*, NRS 597.160(4). Among other prohibited acts, suppliers cannot condition their contract with the distributor on sales or other incentives intended to promote one supplier over another, and suppliers cannot set the prices on the products that the distributor will use for sales to retailers. *See*, NRS 597.162.





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of malt beverages it may produce. Under legislation passed in 2017, this limit was raised from 15,000 barrels of malt beverages across all locations owned by the brew pub to 40,000 barrels *See*, NRS 597.230(1)(d).

The 2017 legislation made a number of additional changes to the operation of brew pubs that don't track across the other "craft" licenses. A brew pub may transport its products to a licensed retailer who

Despite the rigidity of the three-tier system, there has been a trend toward more locally produced liquors and beer during the past 30 years. In Nevada, several new exceptions have been created in the law to allow a single entity

to operate on all three levels of the three-tier system in limited capacity. These "craft" licenses: brew pubs, craft and estate distilleries, wineries and instructional wine-making facilities are all permitted to make and sell their own alcoholic products in order to spur local innovation and manufacturing. Because these businesses blur the lines of the three-tier system, they have special licensing requirements and obligations under the law.

The first, and oldest, exception: a brew pub specifically operates under NRS 597.230. A brew pub, unlike a brewery, crafts its own products *and* sells them on-premise directly to the general public. Because of its special status as a supplier and a retailer, an operator of a brew pub is limited in the quantity

is not the operator of the brew pub for the limited purpose of selling products at a special event, such as a farmers market. Additionally it may sell and transport the malt beverages manufactured on the premises under a special permit obtained from the Department of Taxation for the transportation of the malt beverages. It may also sell its products both on sale (at the bar) and off-sale (typically a "packaged liquor" license by local government ordinance). *See*, NRS 597.230(3), *Et seq.* In exchange for this flexibility, the Department of Taxation has sweeping regulatory authority (anything "necessary or convenient") to monitor brew pub production caps. *See*, NRS 369.150(2)(e).

Similarly, a craft distillery (NRS 597.235) may operate on multiple tiers. Licensees may manufacture spirits from agricultural raw materials through distillation, and blend, age, store and bottle the spirits so manufactured. Craft distilleries may serve samples of the spirits they manufacture, which are limited to two ounces per person per day. And they may sell their spirits on sale and off sale, limited to two bottles per person, per month. *See*, NRS 597.235(2)(e). A craft distillery is limited to a combined total of 10,000 cases of spirits per year in state and not more than a combined total of 20,000 cases of spirits for export. *See*, NRS 597.235(2)(b) and (c).

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In 2017, Nevada created a new class of distilleries — an Estate Distillery at NRS 597.237. Largely similar to their craft distillery predecessors, estate distilleries are intended to promote and reward the investment of capital into and use of Nevada agricultural products. If 80 percent of the ingredients used by an estate distiller are grown on land owned or controlled by that distiller in Nevada, there is a corresponding reward — higher production caps.

Estate distilleries can manufacture up to 400,000 cases of distilled spirits and up to 75,000 cases for in-state sales.

Additional benefits were added for estate distillers during the 2019 Legislative Session — now, they may receive bulk shipments of beer and wine from Nevada licensed brew pubs and wineries for further blending and distillation into new products. (See, Senate Bill 345 of the 2019 Legislative Session). This addition is intended to further foster investment into and creation of Nevada-made alcohol products.

Wineries, the third type of specialty license, most recently underwent significant reform during the 2015 legislature. In the past, these licensees were limited to operation in rural counties. The 2015 legislation opened them up to all counties, and if 25 percent of the grapes are grown in-state, these wineries have no production caps. Unlike other “craft” licenses, a winery may sell at retail or serve by the glass, on its premises and also at one other location — akin to an in-town tasting room away from the vineyard. See, NRS 597.240(2)(a).

A fourth type of license (NRS 597.245) is also available, though it differs in some significant ways from the previous ones. An instructional wine-making facility may make wine on the premise, and it may charge a fee to persons of legal age for the purpose of providing those persons with instruction and the opportunity to participate directly in the process of wine making on the premises of the facility. It may then serve wine produced on the premises of the facility by the glass for consumption on the premises of the facility.

This license is separate and distinct from the winery license of NRS 597.240. Wine produced on the premises of an NRS 597.245 instructional wine-making facility must be used, consumed or disposed of on the premises of the facility, or it must be distributed from the facility to a person of legal age who has directly participated in the process of wine making on the premises of the facility for the person's own household or personal use.

Nevada's three-tier system remains robust for the foreseeable future. Because distributors

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underpin the tax collection, reporting and enforcement, the cost of administration needed for the Department of Taxation to maintain compliance is kept low. As “craft” production appears to continue its upward trajectory, there will continue to be pushes for more exceptions, and the 2021 legislature will likely see new policies in this space, just as it has for the past eight sessions. **NL**

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