BEFORE THE ALCOHOLIC BEVERAGE CONTROL APPEALS BOARD OF THE STATE OF CALIFORNIA

AB-7730
File: 02-269104 Reg: 99045808

BROWN-FORMAN CORPORATION dba Jekel Vineyards
40155 Walnut Avenue, Greenfield, CA 93927,
Appellant/Licensee

v.

DEPARTMENT OF ALCOHOLIC BEVERAGE CONTROL,
Respondent

Administrative Law Judge at the Dept. Hearing: Jeevan S. Ahuja

Appeals Board Hearing: March 13, 2003
San Francisco, CA

ISSUED JUNE 6, 2003

Brown-Forman Corporation, a licensed winegrower, doing business as Jekel Vineyards (appellant), appeals from a decision of the Department of Alcoholic Beverage Control[1] which suspended its license for 15 days for its having furnished money and free advertising to Pebble Beach Company, a licensee engaged in operating, owning or maintaining multiple on-sale and off-sale retail licensed premises, in violation of Business and Professions Code sections 25500, subdivision (a)(2), and 25502, subdivision (a)(2).[2]

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[1]The decision of the Department, dated October 12, 2000, is set forth in the appendix.

[2] Section 25500, subdivision (a)(2) provides, in pertinent part:

(a) No ... winegrower ... shall,:
(2) Furnish, give, or lend any money or other thing of value, directly or indirectly, to ... any person engaged in operating, owning, or maintaining
(continued...)

Appearances on appeal include appellant Brown-Forman Corporation (hereinafter "appellant" or "Jekel"), appearing through its counsel, James M. Seff and J. Daniel Davis, and the Department of Alcoholic Beverage Control, appearing through its counsel, Nicholas R. Loehr.

FACTS AND PROCEDURAL HISTORY

Appellant's winegrower's license was issued on January 15, 1992. On March 5, 1999, the Department filed an accusation against it alleging that it gave things of value - free advertising and $100,000 - to Pebble Beach Company ("Pebble Beach"), a company engaged in the operation, ownership, or maintenance of on-sale and off-sale retail premises, in violation of Business and Professions Code sections 25500, subdivision (a)(2), and 25502, subdivision (a)(2).

An administrative hearing was held on March 23, 2000, at which time oral and documentary evidence was received. Testimony was presented by Steve Wille, a former senior marketing vice-president for Pebble Beach; David Wright, chief of the business practices unit of the Department of Alcoholic Beverage Control; Christian Albrecht, an investigator for the Department; Neal Hotelling, director of corporate affairs for Pebble Beach; and Andrew Varga, senior brand manager for the Jekel Wines division of Brown-Forman.

Subsequent to the hearing, the Department issued its decision which sustained

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[2](...continued)

any on-sale premises where alcoholic beverages are sold for consumption on the premises.

Section 25502, subdivision (a)(2), applies the same proscription with respect to off-sale licensed premises. For ease of reference, we will, as did appellant, use reference to section 25500 to encompass both it and section 25502.

the charge of the accusation, and suspended appellant's license for 15 days.

The Department concluded that advertisements placed by Jekel in two wine industry publications, at a total cost of $57,188.85, which depicted a photographic image of the "Lone Cypress Tree," a Pebble Beach trademark, accompanied by a reference to Jekel wines as "The Official Wine of Pebble Beach," resulted in free advertising to Pebble Beach in violation of the code sections cited above. The Department also concluded that a $100,000 payment by Jekel to Pebble Beach, purportedly for certain trademark rights, also violated those provisions.

Appellant has filed a timely notice of appeal, and in its brief raises the following issues: (1) an opinion of the California Attorney General and the plain language of the statutory sections at issue confirm that winery purchases from a retailer do not violate the law; (2) the Department's interpretation of section 25500 results in absurd consequences; (3) the Department is not entitled to rewrite the law with broad policy statements; (4) the Official Product Agreement does not support a finding of a violation; and (5) no retailer received any free advertising. Issues I through 4 all involve the legal consequences associated with the payment of $100,000 to Pebble Beach, and will be discussed together.

DISCUSSION

The Department is authorized by the California Constitution to exercise its discretion whether to deny, suspend, or revoke an alcoholic beverage license, if the Department shall reasonably determine for "good cause" that the granting or the continuance of such license would be contrary to public welfare or morals.

The scope of the Appeals Board's review is limited by the California Constitution, by statute, and by case law. In reviewing the Department's decision, the Appeals Board

may not exercise its independent judgment on the effect or weight of the evidence, but is to determine whether the findings of fact made by the Department are supported by substantial evidence in light of the whole record, and whether the Department's decision is supported by the findings. The Appeals Board is also authorized to determine whether the Department has proceeded in the manner required by law, proceeded in excess of its jurisdiction (or without jurisdiction), or improperly excluded relevant evidence at the evidentiary hearing.[3]

The facts which give rise to the issues in this case are, for the most part, not in dispute. However, there is much in dispute with respect to how they are characterized and what legal consequences are to be attributed to them. In reaching the result we do, we acknowledge the thoughtful and comprehensive decision of the administrative law judge to whom this case was assigned.

I

Jekel and Pebble Beach entered into two contracts, a "Participant Sponsorship Agreement" and an "Official Product Agreement," both executed by the same individuals and both having the effective date of May 1, 1997.[4]

According to the Department's findings, the Participant Sponsorship Agreement obligated Pebble Beach to provide Jekel access to lodging and golf at its facilities; the

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[3]The California Constitution, article XX, § 22; Business and Professions Code §§23084 and 23085; and *Boreta Enterprises, Inc. v. Department of Alcoholic Beverage Control* (1970) 2 Cal.3d 85 [84 Cal.Rptr. 113].

[4] Mr. Wille, who negotiated the arrangement on behalf of Pebble Beach, testified that there were two separate agreements "because that was the way to do it and keep it and have it be actually appropriate for the laws that pertained to the situation." Mr. Hotelling testified that the agreements were separated on the basis of legal advice and to avoid conflict with the alcoholic beverage laws.

use of Pebble Beach images, logos, and trademarks; tickets for events at Pebble Beach facilities; and the right to use Pebble Beach hotel rooms and golf rounds as sweepstake and contest prizes. Jekel was obligated to pay to Pebble Beach $100,000 per year under the agreement, and made such a payment on October 13, 1997.

The Official Product Agreement obligated Pebble Beach to promote Brown-Forman's wine products by designating them "Official Wine of Pebble Beach Resorts," and to serve certain of Jekel's wine products as "The Official House Pour" and "Concession Pour" at Pebble Beach restaurants and events. Without Jekel's consent, Pebble Beach was, with minor exception, barred by the agreement from entering into any new official product agreement with any company that manufactured, distributed, or sold wine.

Jekel was obligated to provide the services of its winemaker to train Pebble Beach's staff; to make its Jekel Vineyards facility available to Pebble Beach for barrel tasting and wine education; to sell wine to Pebble Beach at agreed upon prices; and to permit Pebble Beach to consult with Jekel with regard to the quality of its products.

The Department concluded that the term "furnish," as used in section 25500, subdivision (a)(2), "may lend itself to differing meanings in the abstract, as the parties contend, but when considered in the context of the legislative history and intent as described below, it becomes clear that the term includes payment for value received, as has occurred in this matter." In effect, the Department treated the payment of $100,000 under the Official Product Agreement as a quid pro quo for Jekel becoming the "Official House Pour" and the "Concession Pour" at all Pebble Beach facilities, to the exclusion of other winegrowers.

Appellant contends that its purchase of the right to use the "Lone Cypress Tree"

trademark and other trademarks, and preferential treatment for its employees and guests at Pebble Beach resorts and events is not prohibited by section 25500, subdivision (a)(2). Appellant argues that the proscription of section 25500, subdivision (a)(2), was never intended to apply to ordinary commercial transactions between a winegrower and a retailer, citing as examples of obvious legality the purchases of postcards, toothpaste, club memberships, hotel rooms, golf course and cart fees, etc., and that the position asserted by the Department will lead to absurd results. Additionally, appellant argues that the agreement giving rise to the "Official House Pour" and "Concession Pour" privileges was contractually separate from the purchase of trademark rights: "Respondent's purchases under the Participant Sponsorship agreement and respondent's sales under the Official Product Agreement were completely separate from one another. The decision to sell private label wine was an afterthought ...."

Appellant relies heavily upon a 1937 opinion of the California Attorney General which addressed the propriety, under the predecessor of section 25500, subdivision (a)(2), of a supplier's payment to a retailer for advertising space in a magazine distributed to members and friends of a licensed private club. Appellant quotes a portion of the opinion which recites that the statutory language would not cover "a bona fide purchase of [retailer services.]"

The Department contends that appellant's reliance on the opinion is misplaced, because it does not discuss the type of advertising, who paid for the advertising, the content of the advertising or the contractual arrangements which pertained to the advertisements. The Department describes the contracts in this case as "sophisticated," finding that they were developed "to try and avoid the Tied House laws,"

and totally different from the arrangement blessed by the Attorney General's 1937 opinion.

We think the Department has the better of the argument. The Attorney General's opinion addresses a factual situation completely unlike the one under scrutiny in this case, and, as the Department notes in its brief, failed to make even a rudimentary analysis of the tied house laws.

Indeed, the Attorney General's opinion has very recently been held not controlling in a case where the facts were much closer in kind to those addressed by the Attorney General than the facts in this case. In *Department of Alcoholic Beverage Control v. Alcoholic Beverage Control Appeals Bd.* (2002) 100 Cal.App.4th 1066 [123 Cal.Rptr.2d 278] (*Deleuze*),[5] a retailer made a payment to a printer for an advertisement to appear in a sales catalog being printed for an individual retailer and which was to be distributed to over 125,000 customers. The court rejected a defense based upon the Attorney General's opinion, concluding that the Department was justified in concluding that the arrangement violated section 25502, subdivision (a). Viewing the arrangement in the context of the tied house laws, the court saw a significant difference between an advertisement in a newspaper or magazine of general circulation and one in a catalog promoting the licensee exclusively:

> Thus, ZD [the winegrower] contributed a valuable and tangible benefit to Wally's [the licensee] by participating in paying for the production of its exclusive sales catalog.
>
> The Department's decision that this violated the prohibition against a winegrower furnishing anything of value to a retailer is consistent with the legislative purpose

[5] A request for depublication filed on behalf of Deleuze and other winegrowers affected by the decision was denied by the California Supreme Court on November 20, 2002.

> of the tied-house laws, as articulated in the *California Beer Wholesaler* [6] decision. There, the Supreme Court made clear that all "firms operating at one level of distribution were to remain free from involvement in, or influence over, any other level."

(Deleuze, *supra*, 100 Cal.App.4th at 1075.)

The court also rejected arguments very much like those made here, that the Department's position would lead to the absurd result of prohibiting winegrowers or suppliers from purchasing any goods or services from a licensed retailer: "But the purchase of a loaf of bread at a grocery store is not analogous to the placement of a wine advertisement in a retailer's catalog; the 'thing of value' furnished here related directly to the sale of alcoholic beverages." *(Deleuze*, *supra,* 100 Cal.App.4th at 1076). Rejecting the contention that the Department's action was arbitrary and beyond its jurisdiction, the court stated that "it is thus well within the Department's purview to determine that section 25502 applies to certain transactions and not to others." In other words, the closer the relationship that is created by the transaction between the supplier and the retailer, the greater will be the scrutiny.

The reasoning of the court in the decision just discussed applies with full force here. Appellant was not merely acquiring the right to use certain trademarks, and incidentally agreeing to sell wine to the owner of the trademarks. Instead, appellant and Pebble Beach consciously entered into a continuing relationship in which appellant would pay money to Pebble Beach and as part of the arrangement obtained a competitive advantage over other winegrowers. The arrangement is suggestive of vertical integration by contract, contrary to the intent and philosophy of the tied house

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[6] The case cited is *California Beer Wholesalers Assn., Inc. v. Alcoholic Beverage Control Appeals Board* (1971) 5 Cal.3d 402 [96 Cal.Rptr. 297].

laws: “Manufacturing interests were to be segregated from wholesale interests; wholesale interests were to be separated from retail interests. In short, business endeavors engaged in the production, handling and final sale of alcoholic beverages were to be kept ‘distinct and apart.’” *(California Beer Wholesalers Assn., Inc., supra*, 5 Cal.3d at 407.)

The operative words of the statute in question - “furnish, give, or lend” - when read together are virtually all-encompassing. It seems clear that more is prohibited than simply a transfer made with donative intent. The word “lend” implies the return of what was loaned. The word “furnish” means, among other things, to provide or supply. Taken together, these three terms appear to reach virtually any means by which a thing of value can move from one party to another. The possibility that the party furnishing, giving, or lending might receive something of value in return is not precluded. Thus, we think it consistent with the policy objectives attributed to the tied house legislation to construe section 25500, subdivision (a)(2), to reach, and ban, an arrangement such as presented in this case.

Appellant asserts that the Official Product Agreement should never have been at issue because the Department did not claim that it violated the law. This argument has little force. It is really appellant who put this agreement in issue, by artificially attempting to isolate its $100,000 payment to Pebble Beach from the balance of its arrangement with Pebble Beach.[7] Appellant wants the Department, and this Board, to ignore the reality of the transaction. True, appellant became entitled to use Pebble

[7] It is interesting to note that Mr. Hotelling was unable to identify any other official product agreement between a vendor and Pebble Beach where the vendor did not pay Pebble Beach for the right to use a phrase like “the official whatever of Pebble Beach.”

Beach's "Lone Cypress Tree" trademark. But the mere fact that appellant may in return have received something of value does not mean it did not expose itself to liability under section 25500.

Appellant argues that its purchases under the Participation Sponsorship Agreement and its sales under the product agreement were "completely separate and independent from one another," despite the fact that they were negotiated together and crafted as separate agreements on the basis of legal advice because of the tied house laws. Such an argument, we think, exalts form over substance, and was properly rejected by the Department.[8] Whether one contract or two, at the end of the day when the documents were signed, Jekel paid $100,000 to Pebble Beach and its wines had become the exclusive house pour and concession pour of Pebble Beach, to the exclusion, with minor exception,[9] of any other winegrower. As we have indicated, the arrangement flies directly in the face of the tied house laws.

We believe the Department's decision is consistent with the objectives attributed to the tied house legislation by the California Supreme Court in *California Beer Wholesalers Association, Inc.*, *supra*, at pages 407-408 (citations and footnotes omitted.):

> By enacting prohibitions against 'tied house' arrangements, state legislatures aimed to prevent two particular dangers: the ability and potentiality of

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[8] Section 1642 of the Civil Code provides that "several contracts relating to the same matters, between the same parties, and made as parts of substantially one transaction, are to be taken together." Whether section 1642 applies in a particular situation is a question of fact for resolution by the trial court. *(Brookwood v. Bank of America* (1996) 45 Cal.App.4th 1667, 1675 [53 Cal.Rptr.2d 515]; *Cadigan v. American Trust Co. (*1955*)* 131 Cal.App.2d 780 [281 P.2d 332, 336].)

[9] Pebble Beach remained free to enter into similar agreement with producers of champagne and sparkling wines.

> large firms to dominate local markets through vertical and horizontal integration ... and the excessive sales of alcoholic beverages produced by the overly aggressive marketing techniques of larger alcoholic beverage concerns ... .
>
> The principal method utilized by state legislatures to avoid these antisocial developments was the establishment of a triple-tiered distribution and licensing scheme. ... Manufacturing interests were to be separated from wholesale interests; wholesale interests were to be segregated from retail interests. In short, business endeavors engaged in the production, handling, and final sale of alcoholic beverages were to be kept "distinct and apart." ...
>
> [M]ost of the statutes enacted during this period (1930-1940) manifested a legislative policy of controlling large wholesalers; the statutes were drafted in sufficiently broad terms, moreover, to insure the accomplishment of the primary objective of the establishment of a triple-tiered system. All levels of the alcoholic beverage industry were to remain segregated; firms operating at one level of distribution were to remain free from involvement in, or influence over, any other level. ... [¶] ... [¶]
>
> California's alcoholic beverage control laws and tied house provisions effectuate the legislative objectives outlined above.

In *Harris v. Alcoholic Beverage Control Appeals Board* (1964) 61 Cal.2d 305, 309 [38 Cal.Rptr. 409], the Supreme Court earlier observed that the Legislature had "inferentially declared that the public policy is best served if all persons engaged in the handling of alcoholic beverages, whether manufacturing, wholesaling, importing or retailing be kept distinct and apart."

We think it consistent with the policy reasons attributed to the tied house legislation to construe section 25502, subdivision (a)(2), to reach, and ban, a payment arrangement such as presented in this case. We are compelled to agree with the Department that the transaction challenged by the Department falls within the broad proscription of the statute and not within any of the exceptions thereto.

The transactions to which appellant points as examples of obvious legitimacy - a

purchase of a tube of toothpaste, payment of green fees, or payment for a hotel room, are essentially one-time events, where there is no lingering or residual relationship. Unlike those examples, the arrangement between Jekel and Pebble Beach created a close and continuing relationship in which Jekel emerged as a favored supplier and Pebble Beach, the beneficiary of an annual payment of $100,000.

There is no bright line test. At best, we think the test must be whether the transaction in question is one which lends itself to the kind of abuse at which the statutes are directed. If so, it may well invite attack by the Department. This may well discourage licensees from transactions with other licensees at a different level of distribution where there is doubt about the applicability of the tied house laws. We can only say that their remedy, if one is needed, will have to be sought from the Legislature.

II

The Department also concluded that advertisements placed in wine industry publications by Brown-Forman at a cost of $57,000, which depicted a photographic image of the "Lone Cypress Tree," a Pebble Beach trademark, accompanied by a reference to Jekel wines as "The Official Wine of Pebble Beach," resulted in free advertising to Pebble Beach. The Department reasoned as follows (Determination of Issues I):

> Respondent argued that the advertisements described in Findings of Fact No. IV above do not mention any retailer's name or location; hence, no retailer could receive the benefit of the advertisement. However, as pointed out by the Department, the advertisements mention Pebble Beach; Pebble Beach is, in fact, a trademark of PBC, which is a partnership of Cypress I LLC and Cypress II LLC, owners of the licenses at PBC's resorts. Moreover, the "Lone Cypress Tree" depicted in the advertisement does evoke images of the Pebble Beach resort area, including its restaurants and other facilities. Respondent's argument that Pebble Beach is merely a post office designation and, thus, a reference to Pebble Beach in the advertisement cannot result in free advertisement to PBC, ignores the images associated with the name "Pebble Beach," and is not

> supported by the facts in this matter. Respondent does not appear to be disputing that if PBC has received free advertising as a result of the advertisements in the "Wine Spectator " and the "Wine enthusiast," it would violate sections 25500(a)(2) and 25502(a)(2). It is found that the advertisements in the "Wine Spectator" and "Wine enthusiast," on which Respondent expended over $57,000, did result in free advertisement to PBC, which operated, owned or maintained multiple on-sale and off-sale licensed premises, through Cypress I LLC and Cypress II LLC, general partners of Pebble Beach Company, as alleged in Counts 1 and 3 of the Accusation. See Findings of Fact Nos. IV and V.

Black and white copies of the advertisements in question are annexed hereto. Each of the original color advertisements contains a photograph of Pebble Beach's trademarked cypress tree, together with a few lines of text.

The advertisement which appeared in the trade publication Wine enthusiast (Ex. 4) contains, superimposed over the photograph of the cypress tree, the phrase "Artists the world over have been inspired by Monterey's rugged beauty. Or was it the wine?" Below the photograph is a small photograph of a bottle of Jekel Chardonnay wine, and additional text which states: "Monterey County, California. Awe is the only logical response to it. Followed by the desire for an equally inspiring glass of wine. Around here that's Jekel. Selected as the Official Wine of Pebble Beach. Created as Monterey intended. Consider every sip another snapshot from home." Below that, in slightly larger typeface, is another phrase: "Monterey is the place. Jekel is the wine."

The advertisement in Wine Spectator (Ex. 3), another trade publication, is similar, in that it also has text superimposed over the photograph of the cypress tree: "It's not Heaven, but it's definitely a suburb." Additional text at the bottom of the page states: "The closest thing to perfection this world will ever know is Monterey County, California. You can see it in the land. You can taste it in the wine. As long as it's Jekel. The one selected as the Official Wine of Pebble Beach, and a truly inspired product of its environment." Below, in slightly larger typeface is the phrase "Monterey is

the place. Jekel is the wine."

Pointing out that there is no reference to any specific retailer, appellant argues that the message of the advertisements is "Monterey is the place. Jekel is the wine." Appellant asserts: "These advertisements advertise wine, not retailers."

Thus, appellant contends, there is no evidence, let alone substantial evidence, of free advertising to any retailer.

The ALJ determined that each of the advertisements was an advertisement for Pebble Beach because it "mention[s] Pebble Beach, [and] Pebble Beach is, in fact, a trademark of PBC, which is a partnership of Cypress I LLC and Cypress II LLC, owners of the licenses at PBC's resorts. Moreover, the 'Lone Cypress Tree' depicted in the advertisement does evoke images of the Pebble Beach resort area, including its restaurants and other facilities."

True, Pebble Beach is a trademark of Pebble Beach Company, and the use of that name in an advertisement could be said to be an attempt to associate the advertised product with the prestige associated with the name. But, given that the name Pebble Beach also refers to a post office address, the name, by itself, does not strike us as telling the typical reader of a publication aimed at the alcoholic beverage trade that the advertisement is attempting to promote anything other than Jekel wine.

Nor are we persuaded that the second consideration relied upon by the ALJ is enough to carry the day. He rejected the argument that the reference to Pebble Beach could be a reference to a post office designation[10] because it "ignores the images

[10] Mr. Hotelling testified that the "Pebble Beach" trademark connotes "great golf." He also testified that Pebble Beach is a postal destination. He said the two words by themselves do not identify any specific place that sells alcoholic beverages.

associated with the name and is not supported by the facts in this matter." We think that the typical viewer of the advertisement will undoubtedly not be as steeped in the facts in this matter as was the ALJ, and, therefore, it is only speculation, not supported by substantial evidence, that he or she will make the associations that the ALJ made.

The dominant focus of the full page advertisement is Jekel wine. To a lesser extent, the advertisement seeks to capitalize on the scenic beauty of Monterey County, California. There is nothing in the advertisement that identifies the cypress tree as a trademark owned by Pebble Beach. Nor is there any evidence that any member of the general public, or of the potential viewing audience, believed that either of the advertisements was an advertisement for Pebble Beach.

Thus, while we have no trouble in concluding that the contractual arrangement between Pebble Beach and Jekel goes generally against the grain of the tied house laws, and that the payment of $100,000 to Pebble Beach specifically contravened sections 25500 and 25502 of the Business and Professions Code, we do think that the Department needs more than a small print reference to Pebble Beach in a full page advertisement to sustain its determination that Jekel paid for an advertisement for Pebble Beach. Nor do we think that whatever images the cypress tree evoked for the Department attorneys and the ALJ, already steeped in the facts of the case, they are necessarily those which would be evoked for a neutral, and presumably disinterested, audience, at least to the extent that audience would conclude it had viewed an advertisement for Pebble Beach.

ORDER

We affirm that part of the Department's decision which finds that the payment of $100,000 by Jekel to Pebble Beach violated Business and Professions Code sections

25500, subdivision (a)(2), and 25502, subdivision (a)(2); we affirm the penalty; we reverse that part of the decision which finds that Jekel paid for advertisements in Wine Spectator and Wine enthusiast magazines in violation of the same statutory provisions; and we remand the matter to the Department for such further proceedings as may be appropriate.[11]

TED HUNT, CHAIRMAN
E. LYNN BROWN, MEMBER
ALCOHOLIC BEVERAGE CONTROL
APPEALS BOARD

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[11] This final decision is filed in accordance with Business and Professions Code section 23088 and shall become effective 30 days following the date of the filing of this final decision as provided by section 23090.7 of said code.

Any party may, before this final decision becomes effective, apply to the appropriate district court of appeal, or the California Supreme Court, for a writ of review of this final decision in accordance with Business and Professions Code section 23090 et seq.