August 20, 2013

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Barbara A. Darkes, Esquire
McNees Wallace & Nurick LLC

Re: Proposed Reorganization of Distributor License

Dear Ms. Darkes:

ISSUE: This is in response to your e-mail of July 22, 2013, in which you ask whether there are any interlocking business prohibitions or other legal impediments to a proposed business arrangement involving a current distributor licensee and a planned brewery and brewery pub licensee. Specifically, Rita E. Maloney, Inc. is currently a licensed distributor. Thomas Maloney ("Tom") is the current Pennsylvania Liquor Control Board ("Board")-approved Manager, sole shareholder, sole Director and President, Secretary and Treasurer of Rita E. Maloney, Inc.

The property/real estate where the business is operated is owned by Thomas and Laurie (wife) ("Laurie") Maloney. The current property is larger than what is needed for the distributorship, so consideration is being given to renovating the property and opening a brewery and a brewery pub in a portion of the building.

The real estate would be transferred from Tom and Laurie to Tom individually or to a limited liability company ("LLC") in which Tom would be the sole Member ("Tom LLC"). The stock of Rita E. Maloney, Inc. would be transferred to Laurie. Additionally, Tom would no longer serve as an Officer or Director of Rita E. Maloney, Inc., as Laurie would assume all of those roles. The brewery and brewery pub will both be owned and operated by another LLC, of which Patrick Maloney (Tom and Laurie's son) ("Patrick") will be the Sole Member ("Patrick LLC").

Construction and renovations would be done on the property, including constructing a wall to separate the distributorship from the remainder of the building. There would be no interior connection between the distributorship and the remainder of the building. The owner of the property (Tom or Tom LLC) would be paying for all of the construction/renovations. Additionally, Tom or Tom LLC also intends to own all furnishings, fixtures and equipment needed for the operation of both the distributorship and the brewery and brewery pub.

Tom would be employed by Rita E. Maloney, Inc. and would continue to be responsible for the day-to-day operations of the distributorship. It is intended that Tom would remain the Board-approved Manager of the distributor license.

The goal is for the property owner (Tom or Tom LLC) to lease turnkey properties to both Rita E. Maloney, Inc. (the distributor) and Patrick LLC (the future brewery and brewery pub licensee). As such, it will be Tom/Tom LLC that incurs the cost of renovations and also the cost of purchasing the furnishings, fixtures and equipment needed for both operations. You also ask a series of questions regarding the source of funding for the relevant expenses, which questions will be addressed *seriatim* below.

Records of the Board indicate that Rita E. Maloney, Inc. holds Malt Beverage Distributor License No. D-3488 (LID 31881) for use by it at premises located at 575 Walnut Street, Danville, Pennsylvania. The manager/steward of record is Thomas Maloney. The current licensed premises includes five thousand one hundred eighty-seven (5,187) square feet of space, including sales area, storage, and administrative space.

<u>OPINION:</u> There would be no interlocking business prohibition on the proposed arrangement so long as Tom, the Board-approved manager, is not an officer or director of the brewery licensee, the brewery pub licensee or the distributor licensee. Section 443 of the Liquor Code, which sets forth the various prohibited interlocking business arrangements, is silent on the issue of a Board-approved <u>manager</u> of a distributor acting in the capacity of a lessor or investor. [47 P.S. § 4-443]. As described, Tom would be the lessor of all the licenses (distributor, brewery and brewery pub), as well as the manager of the distributor.

There would likewise not be a legal impediment with the proposed financing of the deal, in that Tom/Tom LLC would not have an unlawful pecuniary interest in each

of the three (3) licenses, at least insofar as the courts and the legislature have defined that term. To wit, the Liquor Code prohibits any entity other than the licensee from having a pecuniary interest in the licensed business. [47 P.S. § 4-404].

Section 1.1 of the Board's Regulations defines "pecuniary interest" as "an interest that sounds in the attributes of proprietorship." [40 Pa. Code § 1.1]. Such an interest is one of substantial control of a licensed premises, evidenced by elements such as participation in the profits, assumption of liability, decision-making authority and purchasing, employment and other elements of ownership. Appeal of E-J Westside Inn, Corp., 68 Pa. Cmwlth. 323, 449 A.2d 93 (1982) (emphasis added)]. The licensee's discretion includes control of the manager's hiring, firing, discipline, salary and duties. The manager must be an agent of the licensee. [40 Pa. Code § 5.23(j)].

Next, section 436(e) of the Liquor Code [47 P.S. § 4-436(e)] prohibits an officer or director of a corporate distributor or importing distributor licensee from having any pecuniary interest, either directly or indirectly, in the profits of any other class of license. Similarly, the Liquor Code prohibits the holder of a retail liquor license from having any interest in the ownership of a distributor or importing distributor. Specifically, section 411(e) of the Liquor Code provides:

> (e) Except as herein provided, no hotel, restaurant, retail dispenser or club licensee, and no officer, director or stockholder, agent or employe of any such licensee shall in any wise be interested, directly or indirectly, in the ownership or leasehold of any property or the equipment of any property or any mortgage lien against the same, used by a distributor, importing distributor, or by an importer or sacramental wine licensee, in the conduct of his business; nor shall any hotel, restaurant, retail dispenser or club licensee, or any officer, director, stockholder, agent or employe of any such licensee, either directly or indirectly, lend any moneys, credit, or give anything of value or the equivalent thereof, to any distributor, importing distributor, importer or sacramental wine licensee, for equipping, fitting out, or maintaining and conducting, either in whole or in part, an establishment used in the conduct of his business.

[47 P.S. § 4-411(e) (emphasis added)].

There is a rebuttable presumption of a pecuniary interest when a person receives ten percent (10%) or more of the proceeds of the licensed business or when control is exercised by one (1) or more of the following:

i. Employing a majority of the employees of the licensee.
ii. Independently making day-to-day decisions about the operation of the business.
iii. Having final authority to decide how the licensed business is conducted.

[40 Pa. Code § 1.1].

An analysis of the facts of the proposed scenario reveal that Tom will only be an employee of the distributor license, and will not be an officer, director, shareholder, agent or employee of the brewery or brewery pub licenses. Tom will have significant decision-making authority, purchasing responsibilities (for the furnishings, fixtures and equipment of all three (3) licenses), and, by virtue of his continued ownership of these furnishings, fixtures and equipment, he will assume liability for loss or damage to them. Although the budget for the renovation, construction and outfitting of the three (3) separate premises has not been disclosed, the very nature of a "turnkey property" indicates that the licensees will not have any substantial investment in the property.

Presuming that the costs of required changes to the building and outfitting the businesses are recouped by Tom/Tom LLC in the lease payments to be made by Patrick LLC and by Rita E. Maloney, Inc. in a *bona fide*, arms-length transaction, then the provision of such a "turnkey property" by Tom/Tom LLC would not be in violation of section 13.51 of the Board's Regulations, which prohibit the giving of something of value to a licensee by any other licensee, its servants, agents or employees. [40 Pa. Code § 13.51]. Alternatively, if Tom/Tom LLC gifts Patrick LLC with renovations, equipment, furnishings, fittings, or the like, then Tom/Tom LLC would be in violation of section 13.51. [Id.].

These facts notwithstanding, there is currently no statutory prohibition against this type of interest being held by an employee or manager of a distributor licensee. As proposed, Tom/Tom LLC will not be a hotel, restaurant, retail dispenser or club licensee, or an officer, director, stockholder, agent or employe of any such

licensee, and so his financial contribution to the distributor, brewery and brewery pub licenses is not precluded under section 411 of the Liquor Code. [47 P.S. § 4-411(e)]. Likewise, Tom/Tom LLC will not be a distributor licensee, or an officer, director or shareholder of such a licensee, and so his financial contribution to the distributor, brewery and brewery pub licenses is not precluded under section 436(e) of the Liquor Code. [47 P.S. § 4-436(e)]. Furthermore, there is no different result if the project is undertaken by Tom LLC as opposed to Tom as an individual.

With regard to the expenses incurred by Tom or Tom LLC in the renovation of the property and for the furnishings, fixtures and equipment for all three (3) of the licenses, you ask whether Rita E. Maloney, Inc. and Patrick LLC will have to report these expenditures on the Individual Financial Disclosure Affidavits (PLCB Form 1842). No, assuming that Tom/Tom LLC provides the turnkey properties in the manner described above that avoids violation of section 13.51 of the Board's Regulations, the affected licensees will not need to disclose this information in the investors/source of funds section of the form. [40 Pa.Code § 3.6].

You next ask whether the fact that Tom or Tom LLC owns the subject property will be an impediment to the issuance of the licenses, given that Tom or Tom LLC will be the source of funds. No, for the reasons stated above, so long as Tom is not an officer, director, or shareholder of the licensees, and so long as the transaction is a *bona fide*, arms-length transaction with competitive values, there is no impediment to his financial investment as proposed.

Your final two (2) questions regarding overcoming licensing concerns are rendered moot since there is no legal impediment involving the property ownership or source of funding issues, as proposed.

If you have any further questions or concerns regarding the Liquor Code or the Board's Regulations, please do not hesitate to again contact this office.

THIS OPINION APPLIES ONLY TO THE FACTUAL SITUATION DESCRIBED HEREIN AND DOES NOT INSULATE THE LICENSEE OR OTHERS FROM CONSEQUENCES OF CONDUCT OCCURRING PRIOR TO ITS ISSUANCE. THE PROPRIETY OF THE PROPOSED CONDUCT HAS BEEN ADDRESSED ONLY UNDER THE LIQUOR CODE AND REGULATIONS. THE LAWS AND POLICIES ON WHICH THIS OPINION IS

BASED ARE SUBJECT TO CHANGE BY THE LEGISLATURE OR THE PENNSYLVANIA LIQUOR CONTROL BOARD.

Very truly yours,

FAITH S. DIEHL
CHIEF COUNSEL

cc: Pennsylvania State Police,
Bureau of Liquor Control Enforcement
Jerry W. Waters, Director of Office of Regulatory Affairs
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LCB Advisory Opinion No. 13-395