

BEFORE THE DEPARTMENT OF REVENUE
OF THE STATE OF MONTANA

In the matter of the amendment of) NOTICE OF AMENDMENT
ARM 42.12.132, 42.13.101,)
42.13.210, and 42.13.1003 pertaining)
to alcoholic beverage establishment)
location managers, compliance with)
laws and rules, the penalty schedule,)
consumer promotions, and contract)
manufacturing)

TO: All Concerned Persons

1. On November 25, 2016, the Department of Revenue published MAR Notice No. 42-2-968 pertaining to the public hearing on the proposed amendment of the above-stated rules at page 2170 of the 2016 Montana Administrative Register, Issue Number 22.

2. On December 15, 2016, a public hearing was held to consider the proposed amendment. Dax Cetraro, Montana Tavern Association; Jim Harris, Montana Distillers Guild; Sam Hoffman, Red Lodge Ales; John Iverson, Montana Tavern Association; Matt Leow, Montana Brewers Association; Neil Peterson, Gaming Industry Association of Montana; Melissa Shannon, Montana Beer and Wine Distributors Association; and Joel Silverman, Liquor Store Owners Association of Montana, appeared and testified at the hearing. Several of those who testified at the hearing also provided supplemental written comments. Other members of the public attended the hearing, but did not testify. Kristi Blazer, Montana Beer and Wine Distributors Association; Michael Lawlor, Goodrich and Reely, PLLC; and Brian Smith, Blackfoot River Brewing Co., provided written comments.

3. The department amends ARM 42.13.210 and 42.13.1003 as proposed.

4. After consideration of the comments received, the department amends ARM 42.12.132 and 42.13.101 as proposed, but with the following changes from the original proposal, new matter underlined, deleted matter interlined:

42.12.132 LOCATION MANAGER (1) and (2) remain as proposed.

(3) A location manager is an employee who provides general oversight of the alcoholic beverage operations and ensures compliance with alcoholic beverage laws and regulations. The location manager designation is based upon the duties performed rather than the job title assigned. ~~Location manager duties may include, but are not limited to, the following services related to the alcoholic beverage business operations:~~

- ~~(a) hiring, firing, training, or supervising employees;~~
- ~~(b) signing applications or agreements on behalf of the licensee;~~
- ~~(c) determining the hours of operation and employee work schedules;~~

(d) ~~managing inventory;~~
(e) ~~signing checks or overseeing bank deposits or financial reconciliations;~~
and

(f) ~~ensuring payment of taxes or filing tax reports.~~

(4) and (5) remain as proposed.

(6) The licensee shall:

(a) and (b) remain as proposed.

(c) except for an owner acting as a location manager, provide the location manager compensation as a fixed amount that is commensurate with the duties performed. Compensation shall not be based on a percentage of gross sales or net profits.

(7) remains as proposed.

42.13.101 COMPLIANCE WITH LAWS AND RULES (1) through (10) remain as proposed.

(11) Aggravating circumstances include, but are not limited to:

(a) through (e) remain as proposed.

(f) lack of cooperation by the licensee, ~~licensee's employees, or licensee's agent~~ in an investigation; and

(g) ~~conducting business operations that have the potential to negatively impact or has negatively impacted~~ a violation's significant negative effect on the health and welfare of the community in which the licensee operates.

(12) remains as proposed.

5. The department has thoroughly considered the comments and testimony received. A summary of the comments received and the department's responses are as follows:

COMMENT 1: Mr. Smith requested further amendment of ARM 42.12.132, to include a prohibition against retail licensees having location managers with any affiliation to a manufacturer, importer, bottler, or distributor. He stated that such an amendment is consistent with 16-4-401(2)(a)(iii), MCA, which specifies that "the applicant or any member of the applicant's immediate family is without financing from or any affiliation to a manufacturer, importer, bottler, or distributor of alcoholic beverages."

RESPONSE 1: Although the department will consider the inclusion of such a prohibition in future rulemaking, such an amendment cannot occur at this stage of this current rulemaking process, as it would be implementing new content that the public did not have an opportunity to comment on.

COMMENT 2: Mr. Silverman requested clarification whether agency liquor stores are subject to ARM 42.12.132, and whether agency liquor stores must verify if a person placing an order is an approved location manager.

RESPONSE 2: Agency liquor stores are not subject to the location manager provisions and the rule does not impose any duties on an agency liquor store.

ARM 42.12.132 is located in ARM Title 42, chapter 12, which contains rules related to liquor licenses and permits. Administrative rules relating to agency liquor stores are located in ARM Title 42, chapter 11.

COMMENT 3: Mr. Cetraro, Mr. Hoffman, Mr. Iverson, Mr. Peterson, and Mr. Silverman all commented in opposition to the proposed requirement for a licensee to seek the department's approval for each location manager performing location manager duties. The parties requested that the licensees be required to designate only one location manager per location.

RESPONSE 3: The department must be able to screen all persons who are performing location manager duties to ensure the person is likely to operate the business in compliance with all federal and state alcoholic beverage regulations. As proposed, the rule allows a licensee flexibility in establishing the management structure that works for its business. This may mean having a single location manager or multiple location managers. The department declines to amend this rule to require a licensee to vest all location manager duties in one person.

COMMENT 4: Mr. Hoffman, Mr. Iverson, Mr. Peterson, and Mr. Silverman requested removal of the proposed language in ARM 42.12.132(3)(a) through (f), which lists examples of location manager duties. The parties stated that confusion would be reduced by having only the language at the beginning of proposed (3), which refers to providing general oversight of the alcoholic beverage operation and ensuring compliance with alcohol beverage laws and regulations.

RESPONSE 4: The department has further amended ARM 42.12.132 to remove the proposed language in (3)(a) through (f), which lists examples of location manager duties.

COMMENT 5: Mr. Lawlor, Mr. Peterson, and Mr. Silverman commented that it was redundant for ARM 42.12.132 to require an owner to seek approval as a manager when the owner has already been screened and approved under 16-4-401, MCA. Mr. Lawlor stated that when such an owner performs location manager duties, the department should only require a written statement, such as resolutions or minutes, designating the owner who will exercise management duties.

RESPONSE 5: The department agrees that an owner screened and approved under 16-4-401, MCA, does not need to resubmit a personal history statement and fingerprint cards. This is reflected in proposed ARM 42.13.132(1), which requires only persons who were not previously screened and approved as owners under 16-4-401, MCA, to submit a personal history statement and fingerprint cards. While such owners performing location manager duties do not need to be screened again, the department does need to know who will be performing location manager duties, whether that be a previously screened owner or another person. Also, disclosing who will perform these services to the department is different than who has the authority to perform these services for the business entity and, therefore, the department will require completion of a location manager form rather

than submission of resolutions or minutes. Furthermore, submission of this information on a department form will enable the department to ensure consistent processing.

COMMENT 6: Mr. Lawlor stated that the requirement in ARM 42.12.132(1) for off-premises retail licensees to be subjected to background checks and fingerprinting requirements is contrary to 16-4-414(3), MCA, which expressly states that managers for off-premises licensees are not subject to this screening.

RESPONSE 6: Section 16-4-414(2)(ii), MCA, states that a person designated by the off-premises applicant as being responsible for operating the licensed establishment on behalf of the applicant is subject to fingerprint and background checks. ARM 42.12.132 is consistent with this requirement, as it requires background checks and fingerprinting of only those individuals who provide general oversight of the alcoholic beverage operations and ensure compliance with alcoholic beverage laws and regulations. Because the department is seeking by rule to screen the same parties authorized under statute, the department amends the language in ARM 42.12.132(1) as initially proposed.

COMMENT 7: Mr. Lawlor stated that the department's small business impact statement understates the additional compliance costs of requiring manager application forms in situations where a management agreement is not currently required.

RESPONSE 7: The proposed amendment to ARM 42.12.132 requires applicants and licensees to submit a location manager application when there is a change in location manager. Under the previous administrative rule, the applicants and licensees were required to submit management agreements. The small business impact statement accurately reflects that this change should be small and administratively feasible as the department's proposal is less burdensome on applicants and licensees.

COMMENT 8: Mr. Silverman requested that the department define "control," which is used in ARM 42.12.132(6)(a), and "active participation," which is used in ARM 42.12.132(6)(b). Mr. Silverman did not provide any proposed definitions.

RESPONSE 8: ARM 42.12.132(6) sets out requirements for the licensee, including that the licensee must retain ultimate control over the license and premises, and maintain an active participation in the alcoholic beverage operation sufficient to ensure the proper and lawful conduct of the business. The subparagraphs in which these terms are used provide sufficient context for determining their meaning. Accordingly, the department declines to further define these terms.

COMMENT 9: Mr. Hoffman, Mr. Iverson, and Mr. Peterson requested that the department remove the proposed requirement in ARM 42.12.132(6)(c), that location manager compensation be a fixed amount. The parties generally stated that this

provision would eliminate the payment of bonuses to location managers, which are used in the industry to incentivize managers.

RESPONSE 9: The department was not seeking to eliminate bonuses provided to location managers that are not based upon gross or net sales. Accordingly, it has further amended ARM 42.12.132(6)(c) by striking the language requiring that location manager compensation be a fixed amount.

COMMENT 10: Mr. Lawlor and Mr. Silverman requested that the department remove the proposed prohibition in ARM 42.12.132(6)(c) stating that location managers' compensation cannot be based on a percentage of gross sales. Mr. Lawlor further commented that if the department would not remove the prohibition in its entirety, that it should amend the restriction to allow compensation based on the gross sales from non-alcoholic and non-gaming revenue. Mr. Silverman further commented that this change would require the amendment of many current management agreements where compensation is based upon gross sales. Mr. Leow requested clarification on how the proposed changes to ARM 42.12.132(6)(c) would impact the compensation allowed for current location managers.

RESPONSE 10: The existing language in ARM 42.12.132(3)(g) requires manager compensation to be "a fixed amount, percentage of gross sales, or a combination of a fixed amount and percentage of gross sales." The proposed amendment to prohibit licensees from tying location manager compensation to sales is needed to prevent the creation of undisclosed ownership interests by location managers. Such interests are created when a non-owner shares in any portion of the business profits, whether it be from the sale of alcoholic beverages or otherwise. Accordingly, the department declines to remove the proposed prohibition. Due to this change, existing manager agreements basing compensation on gross sales would require amendment or termination. Because the proposed rule no longer requires department approval of these contracts, however, the amended contracts do not need to be submitted to the department.

COMMENT 11: Mr. Lawlor requested clarification with regard to undisclosed ownership violations. He questioned whether the department has concluded that undisclosed ownership violations cannot occur with respect to an individual who is already an approved owner of a licensee entity based upon the department's stated reasons for the proposed changes to ARM 42.12.132(6)(c). Mr. Lawlor further requested that the department not consider situations where licensees transfer funds from one business they own to another business they own as undisclosed ownership violations.

RESPONSE 11: The department's proposal in ARM 42.12.132(6)(c) allows an owner who is also acting as a location manager to receive compensation beyond what is commensurate with location manager duties because owners are entitled to share in the profits of the business. Without the exception in ARM 42.12.132(6)(c), the restriction would have created an unnecessary prohibition on an owner's ability to share in the profits of the business.

COMMENT 12: Mr. Lawlor stated that 16-4-406(3), MCA, requires the department to consider mitigating circumstances in determining the proposed penalty and, therefore, the department cannot strike the language from ARM 42.13.101(3) stating that the department will do so.

RESPONSE 12: The department is proposing to strike that language from ARM 42.13.101(3) specifically because it is already set forth in 16-4-406(3), MCA, and it is unnecessary to reiterate statutory language in rule. The department amends this section as initially proposed.

COMMENT 13: Mr. Lawlor asked the department to reconsider the proposed amendment to ARM 42.13.101 changing the proposed penalty for undisclosed ownership interests from "Monetary Penalty, Suspension, or Revocation" to "\$1,500/Revocation." Mr. Silverman echoed this comment and also raised the same request for the proposed penalty for denial of a premises inspection, which had the same proposed amendment from "Monetary Penalty, Suspension, or Revocation" to "\$1,500/Revocation."

RESPONSE 13: Undisclosed ownership interests and premises inspection denials are some of the most serious violations committed by a licensee. Such violations go to the very core of a licensee's suitability. When a licensee allows an individual to obtain an undisclosed ownership interest, the department has not screened the individual to determine suitability, including whether the individual is likely to operate the establishment in compliance with the law. Furthermore, a licensee's prohibition of a premises inspection could allow the licensee to conceal the occurrence of other violations on the premises. Heavier penalties are needed to deter and punish those who engage in such actions. Accordingly, the department adopts these amendments to ARM 42.13.101 as proposed.

COMMENT 14: Mr. Lawlor requested that the department reinstate its prior policy, not expressly stated in rule, whereby "self-disclosed" undisclosed ownership violations would result in a lesser penalty of \$250.

RESPONSE 14: Section 16-4-406(3), MCA, requires the department to consider mitigating circumstances. For undisclosed ownership violations, the department may adjust penalties after evaluating any mitigating circumstances presented by the licensee. Accordingly, the department adopts the proposed amendment to ARM 42.13.101 as proposed.

COMMENT 15: Mr. Lawlor and Mr. Silverman requested amendments to ARM 42.13.101(3), which proposed to set the violation date for violations occurring over time as the date the department issues its notice of proposed department action. Mr. Lawlor asked that for "self-disclosed ownership interest violations," the violation date be set as the date a licensee contacts the department to inform it that the licensee has allowed someone to obtain an undisclosed ownership interest. Mr.

Silverman asked that the violation date be set as the date the undisclosed ownership interest violation occurs.

RESPONSE 15: There are violations that occur on a certain date, such as selling after hours or to an underage person, and those that occur over time, such as an undisclosed ownership interest. For violations that occur over time, the violation date is set at the date the department issues its notice. Setting the violation date at the first possible date the interest was transferred would incentivize licensees to hide undisclosed ownerships until at least three years have passed. Setting the violation date as the date the licensee notifies the department that a violation has occurred is similarly unacceptable. It is the screening and approval of the undisclosed owner, not notice of the violation, which cures such undisclosed ownership interests. Accordingly, the department amends the language in ARM 42.13.101(3) as proposed.

COMMENT 16: Mr. Lawlor requested clarification regarding the import of the proposed amendment to the progressive penalty schedule in ARM 42.13.101 changing the violation previously titled "Sale after Hours" to "Sales or Consumption after Hours."

RESPONSE 16: Section 16-3-304, MCA, generally prohibits a retail licensee from being open to the public between 2 a.m. and 8 a.m. The proposed penalty for being open after hours was addressed as a specific violation type in the previous version of ARM 42.13.101. Section 16-3-305, MCA, prohibits a retail licensee from selling, offering for sale, or giving away alcohol between 2 a.m. and 8 a.m. The proposed amendment to the progressive penalty in ARM 42.13.101 clarifies the proposed penalties for this violation.

COMMENT 17: Mr. Harris requested clarification whether the proposed amendment to ARM 42.13.101(3), which changed the violation title from "Re-pouring" to "Refilling of Bottles," had any impact on a manufacturer's ability to reuse bottles as allowed by the Alcohol and Tobacco Tax and Trade Bureau.

RESPONSE 17: The refilling of liquor bottles is prohibited by 16-3-308, MCA. However, this statute specifically allows liquor bottles to be reused as permitted under federal laws or regulations. The department's proposed change to the violation's name is to more accurately reflect the statutory title and does not supersede the statutory provisions. Accordingly, the department adopts this amendment to ARM 42.13.101(3) as initially proposed.

COMMENT 18: Mr. Lawlor requested clarification whether the proposed insertion of "lapsed" in ARM 42.13.101(4) referred only to the situation where the department lapses a license due to nonuse under 16-3-310, MCA.

RESPONSE 18: The department confirms that "lapsed" in ARM 42.13.101(4) refers to the lapse of a license due to nonuse under 16-3-310, MCA. The department amends this section as initially proposed.

COMMENT 19: Mr. Harris requested that the department leave ARM 42.13.101(11) as written and not adopt its proposed amendments. Mr. Iverson and Mr. Peterson requested that the department repeal the aggravating circumstances listed in ARM 42.13.101(11). Absent repeal, they requested the following four changes to this section: 1) leave (11)(c) as currently written to account for situations where a licensee inadvertently commits a violation; 2) remove the proposed insertion of (11)(e) because the statute for an underage sale does not differentiate between selling to someone who is under 18 years of age and someone who is under 21 years of age; 3) leave (11)(f) as currently written because employers should not be held responsible for the lack of cooperation of employees or agents, especially those who may be exercising constitutional rights in a criminal action stemming from the underlying violation; and 4) remove (11)(g) entirely, as it is unclear what it means.

RESPONSE 19: The department declines to repeal the aggravating circumstances set forth in ARM 42.13.101(11). Section 16-4-406(4), MCA, requires the department to consider aggravating circumstances and further states that the department may adjust penalties based upon these considerations. The statute sets out a non-exhaustive list of aggravating circumstances. The department lists additional aggravating circumstances considered for penalty determination in administrative rule to increase transparency. With regard to the additional comments above, the department responds as follows: 1) the department is amending (11)(c) as proposed because the prior wording is already set forth in 16-4-406(4), MCA, and the proposed amendment is necessary to address situations where the licensee is involved in the violation; 2) the department is amending (11)(e) as proposed because selling to a person under 18 years of age is considered a more egregious violation than selling to a person over 18 years of age; 3) the department is further amending (11)(f) to remove the wording that would hold an employer responsible for the lack of cooperation of employees or agents; and 4) the department is reverting to the previous wording in (11)(g) based upon the comments received.

COMMENT 20: Ms. Blazer and Ms. Shannon requested that the department not adopt its proposed removal of ARM 42.13.210(4)(e). They contend that without prior department approval, there is no procedure for harmed industry members to object to consumer promotions.

RESPONSE 20: ARM 42.13.210(4)(e) requires approval from the department prior to a consumer promotion being undertaken. Under the existing rule, there is no mechanism for another industry member to contest the department's approval of a third party's consumer promotion. Additionally, violation of consumer promotion regulations in ARM 42.13.210 and section 6.96 of Title 27 of the Code of Federal Regulations, such as not offering the promotion to all retailers within the market or reimbursement in excess of the coupon plus handling fee, would not occur until after the promotion is implemented. An industry member concerned that a consumer promotion violates state or federal regulations can submit a written, verified

complaint to the department. Once the department has sufficient information, the complaint will be forwarded to the Montana Department of Justice (DOJ) for investigation. If, based on the DOJ's investigation, the department has reasonable cause to believe the promoter violated the law, the department can initiate administrative action against the promoter. Accordingly, the department amends this rule as proposed.

/s/ Laurie Logan
Laurie Logan
Rule Reviewer

/s/ Mike Kadas
Mike Kadas
Director of Revenue

Certified to the Secretary of State March 13, 2017.