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Who profits at the tap? The liquor licensing authorities want to know

January 30, 2014 - Spotlights

Bar and restaurant owners recently seeking approval for the direct issuance or transfer of a liquor license have learned that the local licensing authority and the state Alcoholic Beverages Control Commission ("ABCC") have expanded their due diligence. Several landlords have been surprised that the increased scrutiny not only requires background checks on and disclosure of information from tenants, but may also require such information from landlords. As a result, tenants and landlords need to understand these requirements at the earliest stages of negotiating a lease. A key to understanding the process of the ABCC is recognizing that the grant of a liquor license is a privilege and not a right.

The ABCC in particular is most concerned that there be full disclosure by all parties who have a "direct or indirect, beneficial or financial interest" in the proceeds from liquor sales. The ABCC wants to ensure that applicants meet certain statutory requirements, including being of good character and not having been convicted of violating drug laws. For applicants who lease the premises for which the license is desired, the ABCC specifically requires that the applicant submit a copy of the final lease, as well as a list of all parties that may hold interests in the license, specifically including a "landlord with a percentage rent based on alcohol sales." For each party listed, a personal information form needs to be provided together with a completed Criminal Offender Record Information ("CORI") Request Form. While the preparation of materials is often daunting and the review by the ABCC is extensive and time consuming, the ABCC's concern is understandable and part of its broad policy favoring full disclosure of a transaction involving a liquor license. In relation to any financing or attempts to pledge the liquor license to the landlord, the ABCC will review the note, security agreement and any pledge documents, as well as lease provisions related to the right of the landlord (or its designee) to acquire the liquor license upon termination of the lease. The ABCC will not permit a pledge of the liquor license to secure lease obligations. Also, while the ABCC has not, in practice, permitted a lease provision that expressly restricts tenant's transfer of a liquor license to only a party leasing space at landlord's premises, the ABCC has permitted a landlord (or its designee) to have a commercially reasonable right of first refusal to purchase a liquor license, subject to the landlord or a new tenant meeting the ABCC's requirements.

Accordingly, it is critical that as part of the negotiations surrounding a letter of intent and subsequently a lease, both landlord and tenant need to know whether the liquor license and the other provisions of the lease and related documents will be in compliance with the requirements of the ABCC and which parties will be required to disclose information to the ABCC. Otherwise, financial and other provisions of a final and executed lease submitted to the licensing authorities may need to be amended for the liquor license to be approved, often to the disadvantage of a landlord. By way of example, if the lease is to provide for percentage rent and individuals that are

part of the landlord entity do not want to complete the disclosure forms required by the ABCC, then some landlords may decide to forego collecting percentage rent for liquor sales. In that event, a landlord may be losing significant income from percentage rent because liquor sales generate substantial profits at many restaurants. However, in the event that a single interest holder in a landlord entity does not wish to provide the required information, the ABCC has been amenable to permitting that individual party to waive any interest in the liquor license and its right to receive remuneration in the form of proceeds from the sale of alcohol. With that waiver, the ABCC has permitted the remaining interest holders in the landlord entity to receive income based on percentage rent that includes liquor sales.

The ABCC desires to be transparent and beyond reproach by implementing comprehensive disclosure requirements. On the other hand, the ABCC and local licensing boards have been receptive to a dialogue with prospective applicants to clarify issues in advance of an application to avoid problems and requests for additional information that often delay the process. In order to minimize delays and unnecessary expenses in connection with the transfer or issuance of a liquor license, tenants and landlords should see counsel at the earliest stage of lease negotiations.

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