Virginia Wine:

Opportunities within a Regional Food System

PLAC 570: Community Food Systems

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Executive Summary:

This report is intended to serve as a guide to help inform both local policymakers and winery operators of the tremendous potential for farm wineries to serve as important links in the regional food system. In order to properly acquaint food system stakeholders with the challenges and opportunities facing the Virginia farm winery industry, this guide will begin by describing the basic business model for farm wineries. It will then provide an overview of state and local policies, including a description and analysis of a number of new measures on the state level that will affect the industry. With a basic understanding of business and policy, this guide will continue with a description of how farm wineries currently fit into an emerging regional food system located around the Charlottesville/Albemarle area, where this study was completed. This guide will conclude with a number of recommendations of how the industry can help promote local foods and enhance the relationships necessary for a successfully operating regional food system. The intention is that any findings from Charlottesville area wineries can be broadly applied to other regional food systems worldwide.

Introduction:

The farm wine industry plays an important role in Virginia's local economies. Wineries and vineyards bring urban residents into direct contact with productive rural lands as well as provide an economically viable form of agriculture. According to the Virginia Wine Board, vineyards are the only growing agricultural sector in the Commonwealth and their continued success creates a significant opportunity for the expansion of the local food-shed. The cultivation of grapes on vineyards and the production of wine at wineries provide locally-owned farms and farm wineries with marketable crops and profitable value added products.

Additionally, tourism based on agriculture, or “agritourism”, is an essential component to a winery’s business model and increases local tax revenues from on-site sales, additional agricultural jobs related to wine production, increased tourism revenue for communities, and brand recognition for regional agricultural products. A recent Virginia Tourism Corporation study found that for every dollar spent at a winery, seven additional dollars are spent elsewhere in the local economy. It is clear that agritourism is an important economic activity for both public and private stakeholders.

State and local level policies relating to the farm winery industry are in a period of dramatic change, and it is essential that local authorities understand how best to address the rapid growth of the farm winery industry. In the past fifteen years, the industry has been characterized by unprecedented growth. The total number of planted acres has doubled as has the number of wineries. This has led to uncertainty by local officials on how to preserve the local rural character and not hinder farm winery businesses. Being that this is a recently expanded form of agriculture, both sides are in the process of developing a dialogue in which to communicate. An example of a state that has dealt with similar growth is Oregon. Virginia is currently at the same level as Oregon fifteen years ago in terms of total production and acreage. Oregon has dealt with many of the same issues the industry in Virginia is grappling with, and has produced some innovative solutions. For example, Oregon takes into account the vineyard size in its restrictions of ancillary activities. In terms of policy, Oregon is a good place for Virginia’s policy makers and industry leaders to look towards for structured examples.

The Business of Wine:

Wine production is a difficult industry to enter because high start-up costs are coupled with initially low rates of return. To enter into business, a winery needs significant capital to invest at least ten to fifteen acres of often expensive land, machinery to process grapes into wine, the grape vines themselves, and physical infrastructure such as production and sales buildings, all necessary to support the business. Vines often take up to four years from their initial planting to produce a crop, which won't be ready for market for another year as they are processed, aged, and bottled. It can take a small farm winery up to six or seven years before it starts to make a positive cash inflow, and thus six or seven years before debt payments on the equity or debt investment can be made. It can take up to ten years of positive return to pay off the initial investment, after which the vineyard has the potential to make significant returns. It is also difficult for new wineries to find a distributor for their product. Distributors focus on quantity and established products, so until brand recognition causes demand, it is difficult for wineries to break into off site markets.

In Virginia, wineries have approached this lag period between initial investment and first cash flow in a number of ways. At Cardinal Point in Nelson County, unplanted land was grazed by cattle sold on market in an incremental solution that slowly replaced pasture with vines as the winery could afford to plant more. Veritas, also in Nelson County, used growth enhancement techniques to speed up the process so it only took two years for the vines to produce wine-quality grapes. Agritourism, or on-site wine sales through tasting rooms, is an important source of ancillary revenue for wineries early in their investment lifespan as it brings much needed cash at a point when off-site distribution is limited. This is also the approach the industry is taking on a global level, and in wine producing regions worldwide, vineyards are becoming tourist destinations soon after their founding to cover initial cash flow deficits.

Planting a vineyard is a significant investment in both the land and place. High overhead costs, delayed vine production, and the longevity of grape plants ensure that vineyards stay in agricultural production for decades. If current industry growth continues, total acreage placed under vine or under conservation easement will increase as well, and synergies between wine production and subsidiary agricultural activities will be amplified.

<u>The Viability of Wine in Virginia</u>:

Wine in Virginia is both ecologically and economically feasible, and there is a great potential for the industry to compete on a regional and global scale. The Virginia Wine Board has commissioned detailed county-by-county studies of the best growing regions for wine. These studies identify the best locations down to specific parcels based on climate, topography, and soil and are a potential resource for counties to use in their rural comprehensive planning.

Economically, Virginia can be competitive because great vineyard land is relatively cheap compared to other growing locations, with prime agricultural tracts selling from $10,000 to $20,000 per acre, compared to $100,000 to $1,000,000 an acre in California. As quality increases, this low land cost will help balance other higher expenses to develop a competitive price point. But, while the Virginia wine industry grew from six to approximately forty wineries from 1979 to 1995, this growth rate was slow compared to that found in west coast regions, which absorbed most of the growth in consumer demand. These first forty wineries were small, hobby businesses with limited access to larger distribution systems. In order to make up for low off-site sales they primarily focused on agritourism, or the sale of wine to tourists on-site through tasting rooms, which allowed them to capture the whole profit of wine production which could be as high as sixty percent gross profit. A common practice of these older wineries was to grow a large number of varietals to accommodate every visitors taste, but this meant that they had to diversify and didn't focus on developing a wine to its fullest potential. For example, Afton Vineyards, one of the state's oldest grows fifteen varietals on fifteen acres. However between 1995 and 2005, Virginia's wine industry entered a second stage of wine growth, and total planted acres doubled. The new wineries planted a more limited number of varietals to maximize the quality of each.

For Virginia to capitalize on the continued rising local and national demand for wine, it will have to increase the quality of the best wines that it can grow, namely those wines produced from merlot, cabernet franc, and viognier all of which are European varietals. One native North American grape, Norton, is also grown on a limited scale in Virginia, but there is not a high consumer demand for the more bitter wine. It has achieved the greatest success as a component of blended wines, as it has a deep red hue. Before the advent of modern American wine production, blended Bordeaux in a French style were once the great wines. But, red wines like the Bordeauxs don't grow well in the west because of a hot climate, so California marketers convinced Americans to drink single varietals instead, those wines like Chardonnay that grew extremely well in western valleys. A real opportunity for Virginia wine is to reintroduce and encourage those blended wines, which grow better and healthier here because of more temperate weather.

Brand development and management is very important for wineries as it creates a loyal customer base largely within the region. The industry has taken several approaches to developing brand loyalty and awareness, from cooperative advertising that focuses on the region as a whole and is aimed at the regional wine consuming public and finding outlets in wine trade magazines and newspapers, to advertising a specific winery through word of mouth and repeat customers. As such, it is important for wineries to not just sell their wine, but to sell the whole experience of being out in the countryside tasting a product that came from that land, "it's more than a bottle of wine, it's a story, it's a little peace of the earth that you are connected with." (Sarah Gorman, Cardinal Point) Finally, wineries increase brand quality by hiring renounced vintners to come and improve their wines. Kluge Estates hired Michel Rolland, a worldwide consultant, and King Family brought in Michael Shaps.

State Policies:

In 1980 the Virginia Farm Winery Act was passed allowing Virginia Wineries to by pass the traditional three tiered distribution system and distribute their product directly to retailers. In 2006 the Act was ruled as a violation of the Constitutions Commerce Clause by the Federal District Court in Richmond. Republican Delegate Chris Saxman of Augusta County, VA pushed for House Bill 1288, which was rejected in the 2006 General Assembly, to allow small wineries to by pass the three tier system. Losing the right to distribute their own product will harm smaller wineries that have trouble finding distributors to handle their wines.

HB1435 was passed in 2006 requiring the Virginia Secretary of Agriculture and Forestry to research the Virginia farm winery industries economic viability. The study included an assessment of trends in the business, marketing, profits, possibilities, and governance. The Secretary was required to include in his research findings from past studies, and make suggestions about legislation so the state can support the industry's growth and aid in the industry's success. The study also addressed agritourism in Virginia and the relationship between farm wineries, their local authorities, and the communities in which they reside. There was to be specific focus regarding practices of tastings and "special events." The study researched prevalent issues and made policy recommendations for how to avoid tension between wineries and communities, and was to include recommendations on how to "streamline" the permit process for wineries. The assessment of agritourism did not just address the increased profit margins for wineries, but how it affects, both positively and negatively, the communities and businesses within the communities.

HB1435 states that farm wineries can produce and manufacture their product without a special use permit. All ordinances, special use permits, exception requirements that were in place January, 1 2006 must stay in place until July, 1 2007 unless they are lessened by local authorities. The locals may not create new special use or exceptions permits until the Secretary of Agriculture and Forestry's feasibility study is presented. No local may require the need for *"special exceptions or special use permits"* that restricts amplified music that does not extend beyond the property of the farm winery, prohibits private gatherings held by the owner of the farm winery that does not include the sale of wine, nor restricts construction or the addition of any facility that is used in the process of wine production. HB1435 allows for the wineries to conduct tastings, serve meals, and hold musical performances to promote their product. The winery however must comply with all local ordinances and setback requirements that are in place.

As result of the Secretary's findings Senate Bill 1205 was passed in the 2007 General Assembly and expressed that the state of Virginia supports the farm winery industry and will do what it can to support the growth of the industry. The bill upheld the previous ruling in HB1435 that no local may restrict owners of farm wineries from holding private gatherings or parties where the sale, promotion, or marketing of wine does not take place. According to SB1205 Local authorities may not restrict licensed farm wineries from, *"…on premises sale, tastings, or* *consumption of wine…the direct sale and shipment of wine by common carrier… sale and shipment of wine to the Alcoholic Beverage Control Board, licensed wholesalers, and out-of-state purchasers…the storage, warehousing, and wholesaling of wine in accordance of Title 4."*

Just in 2007 House Bill 3120 was passed addressing the taxing of wine sales. HB 3120 states that no local may enact any ordinance that restricts any business related conducted by farm wineries or businesses affiliated in the distribution or marketing of farm winery products. No local may place tax on wine or alcoholic beverage sales that is not already in place and approved by the Alcoholic Beverage Control Board.

<u>Local Policies:</u>

Zoning & Planning

Farm Wineries in Virginia operate under the farm wineries act of 1980. The act set out restriction and policy surrounding the farm winery industry. The act also stipulated that wineries were farms and thus could operate under all leeway's given to normal agricultural activity. This policy was all well and fine when there were only a handful of producers with relatively small operations. Today however, things have changed considerably. There are over 119 farm wineries operating throughout the Commonwealth (VA Wine Board). These wineries are not only growing and producing wine but are destinations for agricultural tourism.

The growth of the industry has put a strain on state and county officials as they grapple with the best way to deal with the growing industry. The original state laws were aimed at a small cottage industry and not the burgeoning agricultural sector it is becoming today. Farm winery activity has grown from simply growing, producing, tasting, and selling, to hosting events like weddings and functions, the serving of light food and the hosting of significant numbers of tourists. This increase in activity above and beyond simply growing and selling has prompted counties place regulations on what is seen as accessory activities to that which is laid out in Farm Wineries act of 1980. What has resulted is that the vineyards and local policy makers have begun to interpret the activities in different ways. The government looks to protect health, safety, and welfare. The farm wineries who feel that they are acting within there rights as farm wineries and are only trying to conduct orderly business. For example counties have begun to limit the number of events that wineries can host (events being such things as weddings, receptions, meetings, or other such gatherings). Albemarle County limits event activity on wineries through a special use permit (SUP). A winery is not permitted to have more than 12 events in a given year. Being that wineries have become tourist attractions they bring increased traffic to rural area, which often causes concern for the people residing in the rural areas who feel that the excess traffic and noise harms the rural character. The counties are also concerned by the safety issues of having increased numbers on windy rural roads. The regulations are the result of the fact that events are seen as something that in not a conforming use in areas that are zone agricultural (A-1) and thus to do this sort of activity requires special permitting.

Restrictions are necessary to preserve and protect rural character. However, the restrictions need to be just and should be designed to take into account the uniqueness of the wine industry. Good examples of policy can be found in Oregon where they have addressed the growing industry and tourism through permitting that takes into considerations factors such as the size of the property, the number of acres in production, and vineyard location.

We have come to understand that with a shift in local policy and a more active role in the community from farm wineries, the industry can continue to grow in a positive manner. It well worth noting that vineyards despite there events and increased traffic do a lot to preserve farming and rural landscapes and provide economic opportunity for rural farmers. Many wineries have there properties under conservation easement, and those that don't have chosen to make a long term investment in the land by planting a crop that takes at least 4 years to produce any useable fruit. With an encouraging political climate wine production can provide a valuable farming alternative that preserves a way of life and a coveted landscape.

Hurdles and Barriers

Wine production is unique among agricultural products, it's a highly value added luxury product that is unique in its production, sale and marketing. It does not lend its self well to large intensive cropping techniques. The school of though on wine is the fewer bunches of grapes produced by one plant the better the wine. Wineries feel that the root of there problems is that there is no constant set of policies to turn to, nor is there a history of one. Wineries feel that there activities are not well understood by policy makers and thus are dealing with a difficult regulatory climate. Wineries have opted to lobby the state legislature for an overriding policy measure that gives them and local policy maker's clear guidance.

Since wine is an alcoholic beverage and thus is subjected to a laundry list of special State and Federal regulations. Sale distribution and production are controlled in Virginia under a 3 tier system. In this system no operation may occupy more than one tier. This makes it very difficult for farm wineries to distributor there product them selves or directly to local stores, events, and restraints. On July 1 2006 Virginia farm wineries lost there self distribution loophole when the federal court in Richmond ruled that Virginias policy to allow only its wines to self distribute was unconstitutional under the interstate commerce clause.

Recent legislation has attempted to provide alternatives to the industry as it deals with the loss of the ability to self distribute. Recently legislation was passed that provided wineries with production under 3000 cases with a loophole to self distribute again (VA Wine Board). The state is also trying to set up a sort of cooperative distribution origination through the Department of Agriculture. This new distribution system will may end up being cost prohibitive and to complex for smaller wineries.

These policies make it hard for wineries to distribute locally off there premises and thus making it easer for consumers to get a wine from 12 thousand miles away than one from 12 miles up the road. Wineries are also restricted to where they can sell there product, with out special ABC permits they can't sell wine at farmers markets or in a store they operate off site from there vineyard.

Policy Suggestions

Base special events parking and activity based on acreage in production. Set a base as 12 events a year, then for every acre over 10 allow for 5 more parking spaces & 1 more special event. This idea is similar to policy used by Oregon (http://www.oregonwine.org/).

The serving of food in tasting rooms could be dealt with through the issuing of a variances to wineries if they commit to use locally produced food stuffs and agricultural products. For example a stipulation could be set that a tasting room could prepare light snacks as long as a 30% of the product was sourced locally. Arrangements could event be established between vineyards and local bakers and cheese makers so that they could produce there products off site and then sell them in the tasting rooms and wine shops.

The state should also consider increasing its investment in the wine industry. Wine should receive a larger share of the State department of agriculture's research funding. The Department of Agriculture should also provide qualified farmers low interest start up loans and finical assistance during the early years. Provide support services to farmers looking to switch to grape production. It is not necessary for farmers to become a full farm winery; they can just be a vineyard growing grapes.

Further suggestions would be to adopt some of the best grape producing lands as identified by industry report into the counties comprehensive rural plans. These areas have been identified much in the same ways as prime agricultural and forestry lands. By including this in the comprehensive plan counties can target areas in which to promote vineyard growth.

Current Synergies with the Local Food System

Farm wineries and vineyards are important components of the local agricultural economy and as the only growing agricultural sector in Virginia, they provide essential public exposure to agricultural uses of rural lands. This capacity to promote a fledgling regional food system can be carried out in either passive or active manner, although currently the industry is mostly acting in a passive way with a few notable exceptions. This section will describe what is already being done by Virginia's farm wineries, while the next will offer some recommendations on how wineries can become more active participants in a regional food system.

The most important of the current synergies between the wine industry and the food economy is the encouragement of agritourism, or the visitation of rural value-added businesses by local, regional, or national tourists. Agritourism has already been described above as an essential part of a winery's business plan and direct on-site sales through tasting rooms bring visitors out into rural food production areas. By visiting the actual farm where the wine they consume is grown and produced, visitors begin to develop a romantic connection with a physical place, including the soil, vistas, and sensual experience associated with place, what has been referred to as "terroir". There are several potential results of this connection ranging from the benefits of co-locational marketing to an increased demand by tourist-consumers for local foods. By bringing tourists into the agricultural hinterland, wineries increase exposure to food opportunities such as roadside farmers' stands, rural markets, and other agricultural on-site sales locations that encourage consumer self-distribution. In particular, the direct interaction between producer and consumer inherent to on-site sales introduces local consumers visiting wineries to supply nodes in the local food system. While a majority of tourists to wineries are from outside the region, an increasing number of local visitors are attending special events at the wineries and as this activity increases so does co-locational exposure. There is an opportunity for further study into the magnitude of this effect, but experiential evidence suggests there are positive benefits to co-location where it exists.[1] Increased producer – consumer interaction is a necessary link in a local food economy that seeks to remove nationally controlled distribution systems.

Wineries purchase a small but significant percentage of their wine grapes from local farmers to supplement their own agricultural production. This provides an important ancillary income for local farmers struggling to maintain a profit with conventional food crops. This creates another layer of relationships between farmers and vintners. Mountain Cove vineyard in particular was effective at creating working relationships with other farmers, and it sources not only a large percentage of grapes from local growers, but also makes a number of fruit wines from apples and other crops grown on a neighboring farm, Mountain Cove Orchards. Sales to

[1] Traveling Route 250 on the way out to a number of the wineries we visited, we passed a farmers market, a number of local groceries, and a commercial farm-nursery, each of which we would not have known existed

wineries are indeed an important activity for local farmers. Many grow grapes as an ancillary crop that helps supplement their often limited income, and the market for grapes is strong and growing. This grape market helps keep farmers farming and rural lands in local food production. It is this creation of established relationships among the key stakeholders in the food system. The industry facilitates direct consumer – producer and producer – supplier connections, both of which exclude the distributor as another layer to the network. These connections simplify the food system decreasing food-to-market miles and increasing personal relationships among members of the system. In addition, wineries create new agriculturally related markets, such as the market for grapes and other fruits.

Future Opportunities

There is a big potential for wineries to be a key contributor to a regional food system. We suggest two areas where policies may be improved, through both the locality and the wineries. There are a number of policy suggestions that we hope to develop to better assist both wine businesses and local governments in regulating the industry. What we have found is that many of the problems lie in miscommunication between local businesses and local authorities and also in a lack of knowledge by government officials of how the wine industry works. This amounts to a deficiency in trust between the two sides. A comprehensive guide on the wine industry would be helpful for regulators to understand the particular challenges facing the industry. We have produced a guide entitled, “Virginia Wine: Opportunities within a Regional Food System” that includes several ideas of policies.

We also believe that the industry can be a great promoter of the local food system, and a number of policy suggestions that focus on encouraging wineries to work with, enhance their connection to, and possibly produce even more food for the regional system. Examples of such a policy would be to allow wineries to sell or prepare food for sale if it is largely sourced locally. Wineries want the ability to serve food prepared on site, but they are currently limited because of restaurant and farm use laws. Some mutually beneficial compromise could be reached between counties and the wineries. In addition, public programs could encourage the co-locating of farmers market sales with winery tasting rooms, or encouraging farmers to meet with locals at events hosted by wineries. Both the food system and the wineries would benefit from such interactions.