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A Time of Testing for Wineries

Climate change and wildfires add to risks, while making insurance costly and hard to get

What's your dream job? Playing in the PGA tour? Having your own cooking show?

How about owning a winery? That option has become quite popular in recent years.

According to the U.S. Bureau of Labor Statistics (BLS), the number of wineries in the U.S. has grown nearly fivefold from about 1,000 in 2001 to more than 5,000 in 2020. That count represents the number of physical locations with wine-producing operations.[1]

Since many wine producers share facilities with others, the number of wine production enterprises is actually much greater than the number of physical wineries, according to Wines Vines Analytics (WVA), a firm that provides extensive market data on the wine industry. **According to WVA's methodology, the number of wineries in the U.S. increased by nearly three-quarters from 2009 through 2021, from a total of 6,357 to 11,053.[2]**

So, however you count them, wineries have been among the fastest growing-industries in the U.S. in the 21st century. Many wineries don't even seek to turn a profit. Rather, they are a labor of love for amateur vintners who have made their living in another field.

Is the growth in wineries sustainable? It depends in large part on whether a declining number of distributors can continue to support them.

Around the year 2000, there were roughly 3,000 distributors for 2,500 wineries. As of 2019, only about 700 distribution companies remained for 9,000+ wineries, with five or six major national beverage wholesalers controlling 65% of all wines available in the US.[3]

"I believe we are living in a wine bubble that is destined to pop for economic, political, or other unforeseen reasons," writes Carl Giavanti, a marketing consultant for wineries.[4]

Climate Conditions

If anything is poised to "pop the bubble" in the domestic wine industry, it is the warming climate, which effects wineries in two ways.

Sheila E. Salvatore, Editor | Editor@AdjustersInternational.com

800.248.2888 | greenspanai.com
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First, extreme heat in traditionally wine-producing regions disrupts traditional growing seasons by drought and by reducing the time grapes need to ripen, which affects their body and flavor. Since the onset of high temperatures has happened rather quickly, winemakers are forced to catch up in their cultivation of modified strains of grapes and development of new wines.

Climate change cuts both ways for wine producers, however. While hot temperatures complicate viticulture in previously temperate regions, a warming climate also appears to be creating opportunities for wine production in areas previously considered to be too cold for doing so.

Of greater and more immediate impact, however, are the drought-induced wildfires in recent years that have ravaged California and the Pacific Northwest, still the center of wine production in the United States.

By the BLS count, nearly 2,000 of the nation's 5,000 wineries in 2020 were in California; roughly 800 more were in Oregon and Washington. According to WVA's methodology, California accounted for more than 4,000 wineries, 43% of the U.S. total, in 2021; 16% were in Oregon and Washington.

Wildfires have three principal effects on West Coast winery operators:

- The physical damage caused by flames to buildings, equipment, and vineyards;
- The effect of "smoke taint" on grapes, which often makes them unsuitable for winemaking; and
- The immediate and long-term effects of closing off wildfire-stricken areas from tourists.

In 2017, wildfires affecting Napa and Sonoma counties in California damaged 27 wineries, contributing to an estimated $2.6 billion overall insurance loss for Lloyd's of London. At the time, Lloyd's had come to be a leading provider of coverage for the California wine sector. In response to the losses, Lloyd's abruptly pulled out of the market in mid-2019, leaving wineries scrambling for coverage.

FAIR Plan Opened Up

In the three years since Lloyd's pulled out, neither wildfires nor insurance troubles have abated for winery owners on the West Coast. Anecdotes abound of winery owners who are paying 3-5 times as much for less coverage than they had before 2017; many can't find coverage at any price.

Responding to the crisis, in July 2021 California acted to allow certain types of farm property to be eligible for insurance coverage under the state's Fair Access to Insurance Requirements (FAIR) plan, a market of last resort for property owners unable to acquire coverage in the private market.

Under the FAIR plan extension, California wineries and other agricultural enterprises will be able to cover residences, barns, crop storage units, and other buildings

Sheila E. Salvatore, Editor | Editor@AdjustersInternational.com

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against fire and other perils, but agricultural commodities themselves, as well as equipment to process and transport those commodities, will still be excluded from coverage.[5]

Agricultural Hazards
Technically speaking, a winery includes facilities for fermenting grapes and other fruits into wine with some alcoholic content. A winery doesn't necessarily need to have its own vineyard or orchard, although many do.

Vineyards and orchards represent costly components of an investment in a winery, as they require sizeable amounts of land in prime locations for growing. Vineyards and orchards also account for a large share of the risks to a winery, particularly natural hazards.

Like other agricultural commodities, grapes are subject to damage by extreme weather events, such as droughts, inundations, and unexpected freezes, as well as plant diseases and infestations of damaging insects and other pests.

Any one of these occurrences can ruin a crop for purposes of producing wine, especially if the terrain and grapes are selected and prepared for a particular vintage. Federal crop insurance is available and essential for addressing certain perils to growing crops, but it will not address losses in value due to subtle changes to growing conditions.

Controlling these natural conditions and their effects accounts for one of the biggest liability exposures of wineries: Chemical drift liability, the responsibility of an agricultural operation for bodily injury or property damage caused when pesticides, herbicides, and other chemicals sprayed on one's fields drift onto another's property.

Poor growing conditions can be one cause among many for a batch of wine to be tainted, potentially leading to products liability exposure for any disease arising from drinking tainted wine.

Buildings and Equipment
Once grapes are harvested or brought in from elsewhere, they must be put through the process of fermentation to create the wine. With this process, a winery adds the risks of light industrial operations to its agricultural operation.

Through the fermentation and production process, a winery runs the risk of its equipment breaking down, ruining a batch of wine in the process, or suspending the wine-making operation during a critical time for both the life of the grapes and the demand from markets.

In addition, wineries often lose valuable stock due to leaks in their equipment and associated spoilage, plus malicious tampering by disgruntled employees or zealous competitors.

For these reasons and more, equipment breakdown coverage, including business income and extra expense coverage to address losses when operations must be suspended due to breakdowns, is an important component to a winery insurance program.

Once produced and bottled, wine must be transported to market, creating a transit exposure with sensitive concerns for timing, temperature control, and handling.

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Lloyd's became a leading insurance of U.S. wineries largely because of its expertise in writing "stock throughput" policies, which cover goods for damage from the point where they are produced to their final destination.

Winemakers like to consider their craft as an art form. Indeed, the process of creating wine to particular specifications takes more care and consideration than many other commercial undertakings. It is not like cooking, where one can readily create another meal, or fabric work, where one can unravel a piece and start over. There's much greater risk that an entire batch will be ruined.

Serving the Public

Today's wineries are no longer merely producing a product, they're providing an experience. To that end, growing numbers of owners of wineries and vineyards are opening them up to the public for tours, tastings, meal services, and catered events.

Initiatives such as these open up a winery to a range of liability exposures linked connected to hospitality, ranging from simple "slip and fall" injuries to touring guests to illnesses from tainted wine to, most seriously, host liquor liability for injury or damage caused by a patron who became inebriated during a tasting.

The stakes in this line of business have become huge.

According to Forbes ,"what harmed regions like Napa and Sonoma the most in the months following the [2017] fires . . . was the perception that wine country was severely damaged and not open for business. Low hotel and restaurant occupancy in late October and November cost many wine regions financially more than fire damage."

The presence of liability risks amid a crisis in property insurance is a vivid indication that the owner-operators of a winery are not engaged in a hobby, no matter how passionately they engage in the enterprise.

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[1] Erin Delaney, "Industry on Tap: Wineries," U.S. Bureau of Labor Statistics, Spotlight on Statistics," August 2021; accessed at https://www.bls.gov/spotlight/2021/industry-on-tap-wineries/

[2] Wines Vines Analytics, "U.S. Wineries by State, January 2022;" accessed at https://winesvinesanalytics.com/statistics/winery/. For WVA totals since 2009, see Statista, "Total number of wineries in the United States from 2009 to 2021;" accessed at https://www.statista.com/statistics/259353/number-of-wineries-in-the-us/ WVA describes its methodology for counting wineries as follows:

> "The Wines Vines Analytics winery database includes all unique virtual and bonded wineries. Bonded wineries are licensed by the [federal Alcohol and Tobacco Trade Bureau]; additional bonded production or storage locations under the same management are not considered as unique wineries and are not included in the counts. A virtual winery has a physical location (that may be another entity's winery), produces at least one brand (may have multiple brands and/or produce for others) and has its own winemaker and management (may share either of these with another entity). The winery count excludes wineries that are no longer viable. The count excludes bonded facilities which produce non-wine product such as beer, spirits, hard cider, sake and blended cocktails."

[3] Carl Giavanti ,"Three Biggest Challenges Facing Small Wineries Today,"The Grapevine Magazine, April 8, 2019; accessed at https://thegrapevinemagazine.net/2019/04/three-biggest-challenges-facing-small-wineries-today/

[4] Ibid.

[5] California Department of Insurance, "Statement of Commissioner Lara on Governor signature on SB 11," July 23, 2021; accessed at http://www.insurance.ca.gov/0400-news/0100-press-releases/2021/statement077-2021.cfm