Competition in the Markets for Beer, Wine, and Spirits

February 2022
Executive Order 14036, “Promoting Competition in the American Economy.”

On July 9, 2021, President Biden issued Executive Order 14036, “Promoting Competition in the American Economy.” The goal of the Executive Order is to reduce the trend of corporate consolidation, increase competition, and deliver concrete benefits to America’s consumers, workers, and small businesses. Those benefits include more choices, better service, and lower prices for consumers through a competitive market, as well as fairer opportunities for small businesses and entrepreneurs to compete.

In particular, “[t]o protect the vibrancy of the American markets for beer, wine, and spirits, and to improve market access for smaller, independent, and new operations,” the Order required the Secretary of the Treasury, in consultation with the Attorney General and the Chair of the FTC, to “submit a report...assess[ing] the current market structure and conditions of competition, including an assessment of any threats to competition and barriers to new entrants, including:

(i) any unlawful trade practices in the beer, wine, and spirits markets, such as certain exclusionary, discriminatory, or anticompetitive distribution practices, that hinder smaller and independent businesses or new entrants from distributing their products;

(ii) patterns of consolidation in production, distribution, or retail beer, wine, and spirits markets; and

(iii) any unnecessary trade practice regulations of matters such as bottle sizes, permitting, or labeling that may unnecessarily inhibit competition by increasing costs without serving any public health, informational, or tax purpose.”

Accordingly, the Treasury Department has produced the following report. It is based on input from government agencies, industry participants, trade associations, public interest groups, and concerned citizens, including responses to a Treasury Department request for information.

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1 86 Fed. Reg. 36987.
2 Id. at 36994.
Executive Summary

The Treasury Department’s Alcohol and Tobacco Tax and Trade Bureau (TTB) and the Food and Drug Administration (FDA) are federal regulators of the beverage alcohol industry. The Federal Trade Commission (FTC) and the Department of Justice (DOJ) oversee mergers and also police anticompetitive conduct. The Treasury Department regulates sales activity, labeling, and advertising under the Federal Alcohol Administration (FAA) Act’s trade practices provisions, in addition to administering the federal excise tax on alcohol.

The markets for beer, wine, and spirits are unusual. The public health and social concerns inherent in alcohol consumption have led to special forms of regulation, including Prohibition. The 21st Amendment, which ended Prohibition in 1933, incorporates special deference to state laws regarding intoxicating liquors. Consequently, state regulation has a different role in alcohol markets than in other markets. And the FAA Act of 1935 demonstrated a particularized concern with vertical integration, exclusionary conduct, and monopolization more generally.4

Two major industry trends mark the last several decades. The first is significant growth in the number of small and “craft” producers of beer, wine, and spirits. There are now over 6,400 operating breweries in the United States, up from a low of 89 in the late 1970s,5 and more than 6,600 operating wineries. There also more than 1,900 operating distilleries. These businesses are dispersed throughout the country, and they have helped build a strong global reputation for quality and craftsmanship. In addition, over the last several decades the United States has become an innovator in bringing new types of beers, wine, and spirits to the world.

However, the second trend is one of consolidation, particularly at the distribution and/or retail levels for beer, wine, and spirits and at the production level for beer. In many states, there has been significant consolidation in distribution. Additionally, two brewers have dominated the U.S. markets since 2008 and today account for an estimated 65 percent of the beer market nationwide, as measured by revenue.6

It was the evident goal of the FAA Act to combat monopolies in the alcohol beverage industry. By this metric the goals of the statute and the Executive Order are being met in some ways, but not in others. The innovation in American wine, beer, and spirits in the last few decades has resulted in a flourishing of small and craft producers in local markets that is unusual in a contemporary U.S. economy where many markets are dominated by a few, national brands. This may be, at least in part, a byproduct of tax policy and some state and federal laws and their limits on vertical conduct. For example, the regulatory restrictions on slotting allowances for access to shelf space—sometimes called “pay to play” schemes—are distinctive in American retail.

Despite the positive development of significant growth in the number of small and craft producers of beer, wine, and spirits, we find the following matters of concern:

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4 These concerns are codified at 27 U.S.C. § 205(a)-(d).
- Beer production is concentrated heavily with two major brewers, and several distributors have expanded their geographic reach, giving rise to concerns from craft brewers. Studies have shown direct links between major brewery mergers and an ability to raise prices in the markets in which they compete.

- Despite TTB’s active enforcement of the FAA Act’s competition provisions, complaints about exclusionary behavior by large producers, distributors, and retailers are common. Some of the major complaints include those about (1) discriminatory conduct by distributors, and (2) slotting, shelving, and other preferential practices, despite a ban on such practices.

- The complaints suggest that the FAA Act’s competition provisions, originally intended to address overconsumption of alcohol and problems with organized crime may, in a much-changed marketplace, not fully address the exclusionary impact of some business practices. They may, at the same time, unnecessarily burden small firms and new entrants.

- Some of the laws and regulations, both state and federal, may impose a disproportionate burden on small and medium-sized producers without corresponding justifications based in public health or the prevention of anticompetitive behavior. Some of the rules in question include labeling preapproval requirements, bottle size restrictions, mandatory classification of beverages, and complex application requirements to qualify for a permit to produce alcohol.

- While originally designed to prevent anticompetitive vertical integration where distribution is dominated by a few players, some state and federal laws may actually inhibit the growth and competitiveness of small producers. Other laws may unnecessarily inhibit forms of marketing that could otherwise help competition. Restrictive laws also can have financial consequences for consumers. Some state laws require distributors to set publicly and adhere to prices, stifling competition and likely increasing prices to consumers. One study estimated that “post and hold” laws restricting price competition could lead beer consumers to “spend $147-478 million more than they did previously.”

- Regulatory proposals that could serve public health and foster competition by providing information to consumers, such as mandatory allergen, nutrition, and ingredient labeling proposals, have not been implemented.

- Federal tax rates differ between beer, wine, and spirits and affect competition between each of those sectors. Rates that differ between domestic and foreign producers, and between large and small producers also affect competition.

- The direct-to-consumer model, common in wine, has been spreading to beer and spirits and offers distribution opportunities for small producers. Some, however, argue that direct shipment risks making alcohol available to under-age drinkers. An FTC study of

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direct wine shipments found no evidence of such abuse, but there is a lack of evidence specific to beer and spirits.

In light of these considerations, this report makes the following recommendations:

- We encourage the DOJ and the FTC, which have contributed to this report, to continue to vigorously enforce the antitrust laws, while continuing to examine their approach to horizontal consolidation and to evaluate the effectiveness of their remedies in the alcohol markets. In addition, we encourage:
  - the DOJ to consider the effects on distribution stemming from the acquisition of craft brewers by major brewers.
  - the DOJ and the FTC to apply particular skepticism to claims of efficiencies, and particular attention to concerns relating to coordination, in assessing mergers and in considering revisions to merger guidelines.
  - the DOJ and the FTC to engage with state actors on state laws impacting competition in the alcohol markets by submitting letters in response to state legislative requests for technical assistance.
  - the DOJ, contingent on resources and working with the FTC as appropriate, to consider conducting a retrospective on the pricing, innovation, and distribution impacts from craft acquisitions by major brewers.
  - the DOJ and the FTC, in assessing revisions to merger guidelines, to consider guidance as to markets that are already highly concentrated.

- We also encourage the DOJ and the FTC, in consultation with TTB, to consider taking a closer look at vertical mergers or arrangements that may lead to monopolization or exclusion in the alcohol markets, particularly exclusion of small firms or new entrants.

- TTB should reexamine its labeling and other practices to prioritize labeling rules that protect consumers and public health, while reducing or eliminating any regulatory requirements that create compliance costs and can be barriers to new entrants or burdens to small businesses.

- TTB should consider rulemaking to update certain of its trade practice regulations under the FAA Act with several ideas in mind:
  - Responding to the many requests for greater clarity, to sharpen and modernize the categories of conduct that are considered intrinsically harmful, and any exceptions. In such course, TTB should solicit feedback on newer and less-well-understood forms of exclusionary conduct;
  - Strengthen the existing rule on category management—i.e., the design of shelving schemes and the offering of related services for “free”—to improve deterrence.

- TTB should evaluate its trade practice enforcement policies, particularly to:
  - Address complaints of underenforcement, particularly as pertains to conduct by the larger members of the industry;
- Focus additional enforcement efforts, wherever possible, on category management schemes and tying arrangements;

- Continue to exercise enforcement discretion to temper enforcement against entities lacking market power, in the absence of obvious anticompetitive effect;

- Seek collaboration with the DOJ or the FTC with respect to large and complex cases.

- We encourage the states to examine the effects of their regulations on small producers and their ability to compete, including their access to distribution.
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1. Introduction

The U.S. markets for beer, wine, and spirits—production, distribution, and retail—are heavily regulated. In this regulatory environment, there has been consolidation in these industries at various levels. While larger firms account for significant market share, the number of smaller brewers, vintners, and distillers, often called the craft sector, has grown dramatically but still occupies only a small share of the market. Small firms face challenges distributing their products due to increased concentration in many state distribution markets and because of state regulations governing distribution. Comments provided in response to the request for information for this report⁸ argue that marketing arrangements among large producers, large retailers, and distributors also hinder the growth of small firms.

Alcohol is regulated at the federal, state, and sometimes local level. Because the 21st Amendment, which ended Prohibition in 1933, incorporates special deference to state laws regarding intoxicating liquors, federal regulation does not necessarily pre-empt state regulation in the same way as it does for other commodities.⁹

Agencies with federal jurisdiction over the conduct of firms in these markets include Treasury’s Alcohol and Tobacco Tax and Trade Bureau (TTB), the Department of Justice (DOJ), the Federal Trade Commission (FTC), and the Food and Drug Administration (FDA). Both the FTC and the DOJ’s Antitrust Division enforce U.S. antitrust laws. In the alcohol sector, the two agencies have developed expertise in particular industries or products. DOJ has historically enforced the antitrust laws in the beer industry, while the FTC has done so in markets for wine and spirits. While the antitrust laws apply broadly to prevent anticompetitive conduct and mergers, several of the Federal Alcohol Administration (FAA) Act’s prohibitions, which TTB administers, aim to further limit vertical integration and exclusionary practices in the alcohol industry.¹⁰ The TTB-administered FAA Act provisions on labeling and advertising¹¹ also affect competition, as do the federal alcohol tax laws that TTB and Customs and Border Protection (CBP) administer.¹² The FDA’s responsibility includes enforcing laws prohibiting adulteration and misbranding of food, including alcohol beverages.

1.1. U.S. Department of the Treasury

The Treasury Department’s TTB collects federal excise taxes on alcohol, tobacco, firearms, and ammunition and enforces federal tobacco permitting and alcohol permitting, labeling, and marketing requirements to protect consumers. Treasury’s role regulating competition in alcohol markets lies largely in its administration of the FAA Act’s exclusive outlet, tied house, consignment sale, and commercial bribery provisions. These were designed chiefly to restrict vertical integration and exclusionary practices in the alcohol industry. FAA

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⁹ U.S. Const. amend. XXI, § 2 (“The transportation or importation into any State, Territory, or possession of the United States for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited.”).
¹² CBP administers taxes on imported alcohol under a delegation from the Secretary of the Treasury to the Department of Homeland Security. Treasury Order 100-16.
Act provisions on labeling and advertising also affect competition, as do the tax laws that Treasury administers.

TTB investigations in the exclusive outlet, tied house, consignment sale, and commercial bribery areas generally are complex and require extensive field work, often taking a year or more to resolve. Since 2017, TTB has initiated approximately 80 of these investigations and has resolved 44, resulting in 34 permit suspensions and 11 Offers in Compromise (OICs). Settlement agreements have ranged from $325,000 to $5,000,000. TTB determines the length of permit suspension and the amount of an OIC based on the egregiousness and scope of the conduct at issue.

1.2. U.S. Department of Justice

The DOJ’s Antitrust Division enforces the Sherman Antitrust Act and the Clayton Act. The Sherman Act outlaws all contracts, combinations, and conspiracies that unreasonably restrain interstate and foreign trade. This includes agreements among competitors to fix prices, rig bids, and allocate customers, which are punishable as criminal felonies. The Sherman Act also makes it a crime to monopolize any part of interstate commerce. The Antitrust Division enforces the Sherman Act through both criminal and civil enforcement actions.

The Clayton Act is a civil statute (carrying no criminal penalties) that prohibits mergers and acquisitions where the effect “may be substantially to lessen competition, or to tend to create a monopoly.” As amended by the Robinson-Patman Act of 1936, the Clayton Act also bans certain discriminatory prices, services, and allowances in dealings between merchants.

The DOJ has been active in investigating the beer market. Among other things, over the past decade, the Antitrust Division has investigated several significant acquisitions of competing brewers by Anheuser-Busch InBev SA/NV (“ABI”), the largest brewer in the United States, which engaged in a significant effort to monopolize the industry, as described below. The Division obtained remedies to effectively address the potential anticompetitive effects of those acquisitions, including prohibiting certain distribution practices by ABI.

1.3. Federal Trade Commission

The FTC enforces the Clayton Act and the Federal Trade Commission Act. The FTC Act gives the Commission the authority to prevent unfair methods of competition, including those that violate the Sherman Act, as well as unfair and deceptive practices. The FTC Act also reaches other practices that harm competition, but that may not fit neatly into categories of conduct formally prohibited by the Sherman Act. Only the FTC brings cases under the FTC Act.

The FTC can take action to prevent consumer deception arising from the marketing of alcohol products. Deceptive marketing can undermine fair competition, and also have public

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13 One case involved both a suspension and an OIC.
16 The Supreme Court has said that all violations of the Sherman Act also violate the FTC Act. See FTC v. Actavis, 570 U.S. 136, 145 (2013); Cal. Dental Ass’n v. FTC, 526 U.S. 756, 762 & n.3 (1999). Thus, although the FTC does not technically enforce the Sherman Act, it can bring cases under the FTC Act against the same kinds of activities that violate the Sherman Act.
health implications, especially when related to the amount of alcohol or its effects. For example, companies marketing alcohol products may not, in connection with the advertising, sale, or distribution of any product, make false representations about alcohol content, or, for example, suggest that consumers who drink a product with certain ingredients will remain alert when consuming alcohol unless the company possesses and relies upon competent and reliable scientific evidence that substantiates the representation.

1.4. U.S. Food and Drug Administration

Alcohol beverages are subject to the Food, Drug, and Cosmetic Act’s adulteration and misbranding provisions, and the FDA’s implementing regulations, related to food. There are also certain requirements for nutrition labeling on menus, menu boards, and other written materials for alcohol beverages served in restaurants or similar establishments. However, most labels on alcohol beverages themselves are regulated by TTB alone.

2. State Regulation of Competition for Alcohol Sales

2.1. Overview and the Three-Tier System

The 21st Amendment, which ended Prohibition in 1933, incorporates special deference to state laws regarding intoxicating liquors. Consequently, state regulation has a particularly significant role in the markets for alcohol. Many states require beverage alcohol to be sold through a “three-tier” supply chain in which beverages pass from a producer/supplier, to a distributor/wholesaler, to a retailer—and in which no business operating in one tier may hold a significant ownership interest in another tier. Some states, such as California, allow suppliers to own their in-state distributor or to self-distribute. In some states, laws allow suppliers to

17 See, e.g., In re Phusion Projects, LLC et al., Dkt. C-4382 (complaint Oct. 3, 2011), available at https://www.ftc.gov/enforcement/cases-proceedings/112-3084/phusion-projects-llc-jaisen-freeman-christopher-hunter. The FTC charged that Phusion Project LLC’s packaging and marketing for its Four Loko products violated the FTC Act by making false and misleading claims. According to the FTC complaint, the respondents represented in its marketing materials that a 23.5 oz can of 11 percent or 12 percent ABV Four Loko: (a) contains the alcohol equivalent to one or two regular, 12 oz beers, and (b) could safely be consumed in its entirety on a single occasion. The complaint alleged that both claims were false or misleading because a 23.5 oz can of 11 percent ABV Four Loko contained alcohol equivalent to 4.3 regular beers and a 23.5 oz can of 12 percent ABV Four Loko contained alcohol equivalent to 4.7 regular beers. The consent order requires Phusion to disclose, on its product labels, the number of alcohol servings contained in a can of the product.

18 See In re Constellation Brands, Inc., Dkt. C-4266 (claims that consumer will remain alert after drinking product containing 30 percent alcohol by volume plus caffeine were false and misleading because they lacked reasonable basis that substantiated the claims at the time they were made), https://www.ftc.gov/enforcement/cases-proceedings/092-3035/constellation-brands-inc-corporation-matter. The settlement order requires Constellation to not represent that (1) Wide Eye or any other alcohol product containing caffeine, ginseng, guarana, or any stimulant would keep consumers alert, or (2) that any product ingredient would counteract the intoxicating effects of alcohol, unless such claims were true, nonmisleading, and substantiated.

19 The definition of “food” under the Food, Drug & Cosmetic Act of 1938 includes “articles used for food or drink” and thus includes alcohol beverages. 21 U.S.C. § 321(f). For example, manufacturers of alcohol beverages are responsible for adhering to the registration of food facilities requirements in 21 CFR part 1 and to the good manufacturing practices in 21 CFR part 110. FDA regulates labeling of some alcohol beverages that are not subject to the FAA Act (such as wines below seven percent alcohol by volume and certain beverages taxable as beer that are not made from both malted barley and hops (e.g., hard seltzer drinks brewed from sugar, with added flavors)).

20 In a wine industry group’s analysis, only 13 states “allow for very limited interstate self-distribution.” Wine Institute, Comment #258. All comments are available at https://www.regulations.gov/document/TTB-2021-0007-0001/comment.
engage in limited “direct to customer” shipping, and wineries have been the major users of this channel. Nonetheless, these channels remain restricted for most suppliers, and relatively little commerce flows through them.

While one of the goals of a three-tier system is to prevent foreclosure by a vertically integrated dominant producer, some commenters, especially new and small suppliers, have expressed concerns that the required distributor tier presents a barrier to their ability to access retailers and consumers. Suppliers complain that major distributors with large portfolios either refuse to distribute their brands or sign them to exclusive contracts only to fail to promote their brands. Many have objected that distributors often focus on their largest suppliers at the expense of smaller producers. For many suppliers, the trend toward distributor consolidation has exacerbated this problem. Although distributor consolidation can benefit a new entrant with the backing of a major multistate distributor, many smaller and new suppliers have cited challenges in getting their products attention from the major distributors, who have increasingly large portfolios.

For states that have adopted some variety of a three-tier system, the reasons for adopting that system vary. Often states hoped to collect taxes more efficiently, limit alcohol sales to minors, prevent organized crime from gaining control of alcohol distribution, and, in some cases, may have sought to reduce consumption through artificially high prices. Preventing vertical integration can also be understood to have pro-competitive, anti-exclusionary intentions similar to the FAA Act.

A number of commentators stressed the public health benefits of the three-tier system in terms of maintaining artificially high prices to reduce consumption. To the extent this is the goal, however, States may be able to achieve these aims through higher taxes and thus benefit the public treasury rather than private intermediaries deriving economic rents.

2.2. Open, Franchise, and Control States

The distributor tier is subject to extensive and varying regulation by state governments. There are three primary regulatory schemes: “open,” “franchise,” and “control.” In open states, distributors buy and sell alcohol and provide marketing and promotional services. Suppliers are free to terminate their relationships with existing distributors and switch to another distributor (subject to contractual obligations). In franchise states, however, a supplier typically must show

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21 See, e.g., Mass Comment #4 (“Antiquated Three-Tiered System forces breweries into costly, one-sided partnerships that unduly benefit established distributors while providing minimal or negligent service to small breweries, creating the largest roadblock to growth.”); Mass Comment #5 (“Regulators should allow small and medium-sized producers, farmers, and small businesses more opportunity to compete in a modern marketplace where we can sell directly to consumers and trade accounts. [] The ability of small producers to self distribute across all states would benefit consumers, small distributors, and producers alike. This is the biggest barrier to entry, as producers could build up their accounts until it was necessary for logistics reasons to partner with a local distributor.”); W. Blake Gray, Comment #40 (“Large distributors are uninterested in the smallest producers in their portfolio. Small wine and spirits producers have two choices in the three-tier system: place their products with small distributors, who might be more interested in them but have little clout with retailers and restaurants; or see their products buried among 100 similar products on a large distributor’s list.”).

22 Federal Trade Commission, Possible Anticompetitive Barriers to E-Commerce: Wine (July 2003), at 6, available at https://www.ftc.gov/sites/default/files/documents/reports/possible-anticompetitive-barriers-e-commerce-wine/winereport2_0.pdf (As of July 2002, 23 states allowed interstate direct shipments of wine under certain conditions, whereas 27 prohibited it.).
cause in a legal proceeding before terminating its relationship with a distributor, and, in practice, suppliers rarely switch distributors. As a result, the distributor landscape is much more fragmented in franchise states than open states. In control states, a state-run monopoly carries out distribution; the state may also carry out the off-premise retail sale of alcohol. In such states, suppliers sell directly to the state, and use distributors solely for “brokerage” (i.e., marketing services). Control states often have a more limited selection of products in off-premise retailers than non-control states.

In general, states use different regulatory schemes for beer, wine, and spirits. Virginia, for example, is a franchise state for beer and wine, but a control state for spirits.

2.3. State Franchise Laws

Distributors play a significant role in a producer’s success and growth. They establish relationships with retailers to sell the alcohol brands that they carry, competing for retail business by offering a wide selection of brands. And while producers typically are responsible for providing national and regional advertising, distributors often provide point-of-sale promotions like enhanced product placement, setting up displays, conducting in-store events, and supplying retailers with information on the brands they represent.23

In a competitive market, distributors would vie with each other to secure and maintain producers’ business, competing on price, the range of services they offer, and the quality and consistency of their services. If a distributor’s bid or performance was unsatisfactory, a producer could choose a competing offer. But state franchise laws often restrict this competition.24 Almost all states have franchise laws for beer,25 and many have them for wine and spirits as well.26 The laws were written with the assumption that distributors would need protection from powerful producers. However, commentators complain that franchise laws often restrain competition by imposing restrictions on the ability of a producer to switch distributors, by, for example, barring a producer from terminating or declining to renew a contract with a distributor without “good cause” or “for cause.” Separating from a distributor or declining to renew a contract often requires a producer to undertake numerous, time-consuming, and costly steps.

23 FTC Staff/DOJ Comment to the Hon. Jim Wood, California State Assembly, Concerning the Proposed California Assembly Bill 1541, at 4 (March 2020) (“FTC Staff/DOJ Comment CA 1541”), available at https://www.ftc.gov/system/files/documents/advocacy_documents/joint-comment-ftc-staff-doj-antitrust-division-staff-california-state-assembly-concerning-california/v200008_california_beer_distribution_advocacy_2020.pdf. The agencies provided comments on a proposed bill that would have significantly restricted brewers in contracting with distributors. Provisions of the proposed bill were very similar to restrictive state franchise laws elsewhere. Ultimately, the bill died.

24 See FTC Staff/DOJ Comment CA 1541, at 10.


One commenter described these franchise laws as “[t]he most anticompetitive state laws . . . that make it all-but-impossible for a brewer[] to terminate a wholesaler . . . Once a brewer appoints a wholesaler in a given territory, it effectively cannot move away from that wholesaler regardless of the performance or focus of the wholesaler on its brands.”

The “good cause” or “for cause” requirement is often paired with notice requirements to the distributor and an opportunity to cure, with the burden falling squarely on the producer to show cause and satisfy the statutory requirements. For example, Virginia’s Beer Franchise Act provides:

Notwithstanding the terms, provisions or conditions of any agreement, no brewery shall unilaterally amend, cancel, terminate or refuse to continue to renew any agreement, or unilaterally cause a wholesaler to resign from an agreement, unless the brewery has first complied with § 4.1-506 and good cause exists for amendment, termination, cancellation, nonrenewal, noncontinuation or causing a resignation.

In considering the spirits industry, the FTC argues that the effect of such laws is to shield liquor distribution from market forces. Without such limitations, distributors know that if they attempt to charge more than the competitive price, suppliers could move their business to new distributors that are willing to charge lower wholesale prices. Requiring proof of “good cause” reduces this competitive pressure by making it very challenging for suppliers to leave their current distributors. Those constraints reduce competitive dynamism, leading to higher consumer prices.

In addition, many states’ laws require producers to assign exclusive distributor territories, which prohibit producers from using multiple distributors within any given territory. One commenter characterized these laws as “mandated exclusivity” resulting in “[w]holesalers receiv[ing] absolute protection against competition from any other business selling a brand carried by that wholesaler. As a result, retailers seeking a popular brand have no choice but to deal with the wholesaler granted the exclusive right to that brand in the retailer’s territory.”

State franchise laws may lead to less investment by distributors in promoting producers’ brands due to an imperfect alignment of incentives. Although producers and distributors both care about sales, distributors typically care less about stimulating sales of particular products than the individual producers with whom they contract. Because some of the returns from a distributor’s efforts accrue to an individual producer’s benefit, not to the distributor’s (e.g., a free riding situation where distributor marketing leads to a craft producer gaining a new customer that

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27 Brewers Association, Comment #477.
28 With few exceptions for immediate termination, Virginia Code § 4.1-506 requires a brewer to provide 90 days’ written notice to the distributor of any intent to amend, terminate, cancel, or not renew the agreement, as well as to the Board of Directors of the Virginia Alcoholic Beverage Control Authority (“Board”). In its notice, the brewer must state “all the reasons for the intended amendment, termination, cancellation or nonrenewal.” The distributor then typically has 60 days to rectify the condition(s) prompting the brewer’s notice. If the brewer disputes that the distributor has rectified the condition, the brewer must request a hearing before the Board and the Board determines if the distributor rectified the condition. The Board must find “good cause” to amend or terminate the agreement, and the brewer bears the burden of proving good cause.
29 VA. CODE § 4.1-505.
30 See Beer Franchise Law Summary, supra note 25.
31 Brewers Association, Comment #477.
is not tied to a particular distributor), the distributor’s incentives may be to supply fewer of the demand-enhancing services than a producer would seek. While the contract between producer and distributor can help align their incentives to increase the sales of the producer’s brands by, for example, including quality standards and maximum resale prices or sales quotas, the franchise laws impose costly burdens for producers to enforce their contracts and make threat of termination less credible.\textsuperscript{32}

These types of state franchise laws may particularly burden craft producers, especially smaller, developing producers. Smaller producers may be less able than larger, established producers to bear the legal and regulatory costs of distributor termination and may be ill-equipped to enforce, alter, or decline to renew distribution agreements, especially in dealing with large distributors, or with distributors owned by large producers.\textsuperscript{33} Additionally, smaller producers’ ability to succeed may rely more heavily on the distributors’ marketing efforts than larger producers that may handle more of their own marketing and advertising. The inability to enforce or terminate an agreement with a poorly performing distributor may create a barrier to growth and to a producer’s willingness to introduce new products that might otherwise be a competitive constraint on the market power of the large producers. In addition, these laws may stifle innovation as producers—both well-established and new—may be less willing to invest in brand extensions or product developments that their distributors may not promote.\textsuperscript{34} State franchise laws also create barriers to entry for distributors, because it is very difficult to recruit new producers from incumbent distributors, further diminishing competition among distributors.

In general, therefore, state franchise laws tend to increase the producers’ costs of obtaining distribution services from distributors, which, in turn, are likely to increase the costs of distribution. These laws have the effect of encouraging opportunism by distributors, thereby increasing the cost of producing and inhibiting the growth of craft producers.\textsuperscript{35} Such laws make it easier for the largest producers to defend their dominant positions, likely lead to higher prices for consumers, and reduce the variety of products available to consumers in those states.

2.4. Pricing and Post-and-Hold Regulations

In addition to various other regulations, numerous states impose “post-and-hold” restrictions. In general, these laws require alcohol distributors to “post” their prices with state authorities, and then to “hold” or maintain those prices for a period of time, during which distributors generally cannot engage in price competition. The posted prices are widely available to competitors, but the states do not control the prices, nor do they review them for reasonableness.\textsuperscript{36} Some of these laws also contain what are known as “meet-but-not-beat” provisions, which provide distributors a brief period to match, but not undercut, their competitors’ lowest price\textsuperscript{37}—thereby giving the distributor that sets the lowest price the power to set minimum prices for its competitors. Typically, these laws were enacted at the end of

\textsuperscript{32} See FTC Staff/DOJ Comment CA 1541 at 9-10.
\textsuperscript{33} See id. at 8.
\textsuperscript{34} See id. at 9.
\textsuperscript{37} See, e.g., CONN. GEN. STAT. § 30-63(c).
Prohibition to limit alcohol consumption by raising prices—or “fostering and promoting temperance.”\textsuperscript{38}

Post-and-hold regulations are widely recognized to weaken price competition. As studies of post-and-hold regulations indicate, requiring distributors to set and adhere to prices in advance “softens competition,” “restricts quantity,” and “facilitates non-competitive pricing in the [distributor] market,” which “leads to unambiguously higher prices” for consumers.\textsuperscript{39} Such laws also make price cuts “much more expensive” for distributors, and thus “much less likely,” as price cuts are “irreversible” during the hold period.\textsuperscript{40} Additionally, “meet-but-not-beat” provisions exacerbate these anticompetitive effects because the ability to match lower prices may incentivize distributors to inflate initial prices, thus pushing all prices to levels above what could be sustained in a competitive market.\textsuperscript{41}

Post-and-hold laws make coordinated pricing among distributors more likely by making it easier for competing firms to reach and enforce agreements on prices.\textsuperscript{42} These laws effectively mimic agreements between rivals to fix prices. For this reason, retailers in a number of states have challenged the post-and-hold statutes as preempted by the Sherman Act, with mixed results.\textsuperscript{43} Over a dozen states currently impose post-and-hold restraints, covering a substantial part of the national population.\textsuperscript{44}

<table>
<thead>
<tr>
<th>State</th>
<th>Wine</th>
<th>Beer</th>
<th>Spirits</th>
</tr>
</thead>
<tbody>
<tr>
<td>California</td>
<td>None</td>
<td>Post</td>
<td>None</td>
</tr>
<tr>
<td>Connecticut</td>
<td>Post &amp; Hold (30)</td>
<td>Post &amp; Hold (30)</td>
<td>Post &amp; Hold (30)</td>
</tr>
<tr>
<td>Delaware</td>
<td>Post</td>
<td>Post</td>
<td>Post</td>
</tr>
</tbody>
</table>

\textsuperscript{38} TFWS, 242 F.3d at 203.

\textsuperscript{39} Christopher T. Conlon & Nirupama Rao, The Price of Liquor is Too Damn High: Alcohol Taxation and Market Structure, at 3 (N.Y.U. Wagner Research Paper No. 2610118, 2015); see also James C. Cooper & Joshua D. Wright, Alcohol, Antitrust, and the 21st Amendment: An Empirical Examination of Post and Hold Laws, 32 INT’L REV. L. & ECON. 379, 390 (2012) (“[C]onsumers in states with PH laws consume between 2-8 percent less alcohol (measured in ethanol equivalent gallons), with the effects for wine and spirits relatively larger than those for beer. . . The results are consistent with the prior literature linking state regulation of the alcoholic beverage industry to consumer harm in the form of lower output and higher prices. These results are further consistent with the underlying economics of PH laws, which increase incentives to collude and decrease unilateral incentives to discount.”). But see Henry Saffer & Markus Gehrtsitz, The Effect of Post-and-Hold Laws on Alcohol Consumption, NBER Working Paper No. 21367 (July 2015), available at https://www.nber.org/papers/w21367 (not finding that post-and-hold laws reduce competition or raise prices, but concluding “Taxes are more effective in driving up alcohol prices and reducing consumption than the post-and-hold laws.”). \textsuperscript{40}

\textsuperscript{40} 1 Phillip E. Areeda & Herbert Hovenkamp, Antitrust Law ¶ 217b2, at 390 n.52 (4th ed. 2013); see also Cooper & Wright, supra, at 381 n.14.

\textsuperscript{41} See Conlon & Rao, supra, at 15, 50.

\textsuperscript{42} Brewers typically develop pricing strategies for their brands with an ultimate consumer price in mind and provide recommended retail pricing to their distributors.


\textsuperscript{44} See, e.g., CONN. GEN. STAT. § 30-63(c); 4 DEL. ADMIN CODE 904; GA. COMP. R. & REGS. 560-2-4-.07; IDAHO CODE §§ 23-1029, 23-1329; MICH. COMP. LAWS § 436.1609a; N.Y. ALCO. BEV. CONT. LAw § 101-b(4); OKLA. ADMIN. CODE 45:30-3-8; S.D. ADMIN. R. 64:75:03:02; TENN. CODE § 57-6-104.
<table>
<thead>
<tr>
<th>State</th>
<th>Post &amp; Hold (180)</th>
<th>Post &amp; Hold (14)</th>
<th>Post &amp; Hold (7)</th>
<th>Post &amp; Hold (30)</th>
<th>Post &amp; Hold (90)</th>
<th>Post &amp; Hold (60)</th>
</tr>
</thead>
<tbody>
<tr>
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<td>Post &amp; Hold (180)</td>
<td>None</td>
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</tr>
<tr>
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<td>Post &amp; Hold (30)</td>
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<td>None</td>
<td>None</td>
<td>None</td>
<td>Post &amp; Hold (7)</td>
</tr>
<tr>
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<td>Post</td>
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<td>None</td>
<td>None</td>
<td>Post</td>
</tr>
<tr>
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<td>None</td>
<td>None</td>
<td>None</td>
</tr>
<tr>
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<td>Post &amp; Hold (30)</td>
<td>Post &amp; Hold (30)</td>
<td>Post &amp; Hold (30)</td>
<td>Post &amp; Hold (30)</td>
<td>Post &amp; Hold (30)</td>
</tr>
<tr>
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<td>Post &amp; Hold (90)</td>
<td>Post &amp; Hold (30)</td>
<td>Post &amp; Hold (30)</td>
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<td>Post</td>
</tr>
<tr>
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<td>Post &amp; Hold (30)</td>
<td>Post &amp; Hold (30)</td>
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<td>None</td>
<td>Post</td>
</tr>
<tr>
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<td>Post &amp; Hold (30)</td>
<td>Post &amp; Hold (30)</td>
<td>Post &amp; Hold (30)</td>
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</tr>
<tr>
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<td>Post &amp; Hold (90)</td>
<td>Post &amp; Hold (90)</td>
<td>None</td>
<td>Post</td>
</tr>
<tr>
<td>Oklahoma</td>
<td>Post &amp; Hold (60)</td>
<td>Post &amp; Hold (14)</td>
<td>Post &amp; Hold (14)</td>
<td>Post &amp; Hold (14)</td>
<td>Post &amp; Hold (14)</td>
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<td>None</td>
<td>Post &amp; Hold (10)</td>
<td>None</td>
<td>None</td>
<td>Post</td>
</tr>
<tr>
<td>South Dakota</td>
<td>Post &amp; Hold (10)</td>
<td>Post &amp; Hold (10)</td>
<td>Post &amp; Hold (10)</td>
<td>Post &amp; Hold (10)</td>
<td>Post &amp; Hold (10)</td>
<td>Post &amp; Hold (10)</td>
</tr>
<tr>
<td>Tennessee</td>
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<td>None</td>
<td>Post &amp; Hold (360)</td>
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</tr>
<tr>
<td>Vermont</td>
<td>Post &amp; Hold (14)</td>
<td>None</td>
<td>None</td>
<td>None</td>
<td>Post</td>
<td>None</td>
</tr>
<tr>
<td>Washington</td>
<td>Post</td>
<td>None</td>
<td>None</td>
<td>Post &amp; Hold (90)</td>
<td>None</td>
<td>None</td>
</tr>
<tr>
<td>West Virginia</td>
<td>Post &amp; Hold (90)</td>
<td>None</td>
<td>None</td>
<td>Post &amp; Hold (90)</td>
<td>None</td>
<td>None</td>
</tr>
</tbody>
</table>


Given that more than $250 billion of alcohol was sold in the United States in 2018, for example, even modest price increases in these states as a result of post-and-hold laws can lead to a substantial transfer of wealth from consumers to distributors and/or producers. According to one estimate, post-and-hold restraints may increase the price of a “bottle of wine by $0.39-1.10 (6.4%-18%)”; the price of a “six-pack of beer by $0.93-2.24 (12.5%-30%)”; and the price of a “bottle of spirits by $2.03-6.87 (9.6-32.5%).” In the beer market alone, that price increase “would reduce consumer surplus by $242-581 million, of which $236-567 million would be transferred to producers,” while “consumers would spend $147-478 million more than they did previously.”

States also impose a range of pricing regulations on the distributor tier. Some states require distributors to offer uniform pricing for a given product: a single price to all retailers in the on-premise channel, and a single price to all retailers in the off-premise channel. These laws limit retailers’ ability to play one distributor off another on price (limiting the ability of

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45 See, e.g., Cooper & Wright, supra, at 387 (“It is clear that producers benefit from PH laws at the expense of consumers.”)
46 Cooper & Wright, supra note 39, at 387.
47 Id. at 388.
distributors to compete on price), and they limit distributors’ ability to target particular retailers for price increases or decreases.

2.5. Direct Shipment: An Alternative to the Three-Tier Distribution System

Both the “direct-to-consumer” business model and the rise of online marketplaces have transformed many sectors over the past 25 years. In alcohol markets, however, state laws have substantially limited direct-to-consumer sales. By its nature, direct-to-consumer offers distinct distribution opportunities for small producers, opportunities for innovation, and the possibility of serving small niches. For such reasons, numerous commenters argued in favor of allowing direct shipment as a way for small firms to bring their product to market as an alternative to restrictively regulated or concentrated distribution networks.

Direct-to-consumer models started with Oregon’s 1985 reciprocal shipping law for wine, which granted shipping rights to producers in other states that also allowed for direct shipping. As a result of these laws, wineries and other producers could bypass the mandatory three-tier distribution system, where they were often unable to obtain wholesaler representation in all the markets. The direct-to-consumer model has been spreading to beer and spirits in recent years.

In the alcohol industry, while some of the restrictions on direct shipment to consumers may have had legitimate consumer protection or public health rationales, they also had the effect of making it challenging for niche producers to reach consumers and also insulating local retailers and distributors from out-of-state competitors. In 2002, the FTC hosted a series of hearings to discuss the development of policies to promote competition in a variety of industries through emerging e-commerce. One of the industries the FTC studied was wine, resulting in a staff report entitled “Possible Anticompetitive Barriers to E-commerce: Wine,” published in July 2003.49 The report was based on a study of one local market: the wine products available to consumers living in McLean, Virginia. That study found that 15 percent of a sample of wines available online were not available from retail wine stores within ten miles of McLean. This led to the conclusion that, by banning interstate direct shipments, states seriously limit consumers’ access to thousands of labels from smaller wineries. Moreover, the study found that, depending on the wine’s price, the quantity purchased, and the method of delivery, consumers could save money by purchasing wine online. The McLean study suggested that, if consumers used the least expensive shipping method, they could save an average of 8 to 13 percent on wines costing more than $20 per bottle and an average of 20 to 21 percent on wines costing more than $40 per bottle.50 The report concluded that “[s]tate bans on interstate direct shipping represent the single largest regulatory barrier to expanded e-commerce in wine.”51

In 1997, after 13 states had introduced direct shipping laws, a Model Direct Shipping Law was developed that required licensure in the recipient state, payment of taxes to the recipient state, acceptance of the jurisdiction of the recipient states courts, and certain procedural components such as adult signature requirements and winery reporting to the state regulators. Federal Trade Commission staff, “[a]fter extensive review,” concluded in 2003 that “states could

50 Id. at 16-26.
51 Id. at 3.
significantly enhance consumer welfare by allowing the direct shipment of wine to consumers,” lowering prices and providing greater selection. 52 Another 13 states passed direct-to-consumer shipping laws by 2004. In some cases, some retailers and wholesalers opposed liberalizing shipment laws, and some states adopted laws that allowed only in-state wineries to sell directly to consumers. In Granholm v. Heald,53 the Supreme Court consolidated a number of lawsuits challenging Michigan and New York statutes that gave in-state wineries a competitive advantage over wineries located outside the state. The Court’s opinion, which repeatedly cited to findings from the FTC Wine Report, struck down both laws, holding that they discriminated against interstate commerce in violation of the Commerce Clause. The Court held that states can regulate direct-to-consumer shipping in their states regardless of a wine’s origin, but they cannot discriminate against out of state wineries in so doing. As a result of this ruling, although states may mandate a three-tier distribution system pursuant to their authority under the 21st Amendment, they cannot require that costly scheme solely for out-of-state wineries, while allowing in-state producers to obtain a less-costly or burdensome license for direct sales. According to the Court, such “differential treatment between in-state and out-of-state wineries constitutes explicit discrimination against interstate commerce.”54

Today, 47 states authorize the direct shipment of wine under a regulatory system that allows any winery to apply for a permit to make direct sales to consumers in that state.55 The FTC has repeatedly supported legislative proposals to expand opportunities for the direct shipment of wine under state law.56 Thirteen states also allow out-of-state wineries to obtain licenses to self-distribute in each of those states, although these licenses can be subject to a number of restrictions that limit sales opportunities for many wineries.

In contrast, “only nine states plus D.C. permit direct shipping of distilled spirits.”57 Wine & Spirits Wholesalers of America reports that “100% of the state legislatures that have faced new interstate spirits shipping bills [in 2021] have chosen NOT to enact [direct-to consumer]

52 Id.
54 Id. at 467.
55 According to the Wine Institute, only Delaware, Mississippi, and Utah have yet to allow consumers to have wine delivered to their door via common carrier from a winery. Wine Institute, Comment #258, Dkt. TTB-2021-0007, Notice No. 204.
57 Tom Potter, Let distillers sell directly to consumers, N.Y. DAILY NEWS (Sept. 23, 2021).
spirits laws.” Some distiller groups, including the Distilled Spirits Council of the United States (DISCUS) and the Kentucky Distillers Association, proposed a “Statement of Principles on Direct-To-Consumer Shipping of Spirits,” which, among other things, sought parity for shipment of spirits as compared to wine, but failed to gain the support of a group of state legislators.

Similarly, as to beer, one commenter raised concerns with the restrictions the three-tier system places “on brewers’ ability to access consumers directly via deliveries and shipments.” This commenter noted that while “[o]n-line shopping had been growing for years, and the COVID-19 pandemic greatly accelerated that trend . . . out-of-state breweries can only ship beer to consumers in eleven states plus the District of Columbia.”

On the other hand, some raised concerns with direct to consumer sales, saying that “by pushing the expansion of direct shipment, bypassing the wholesale tier entirely and adding to the risk of tainted alcohol entering the market, increase[s] the odds of failing to collect state alcohol taxes, and increasing availability to youth, since home delivery has an abysmal record of age-gating and ID-checking.” Many commenters worried, in short, that direct shipment restrictions to prevent sales to minors would be inadequately enforced by delivery companies. A 2003 FTC staff reported that there were few or no problems with sales to minors in states allowing direct shipment, while identifying less restrictive alternatives than direct sale bans to prevent such sales. States that allowed direct shipping of wine typically require that a supplier verify the recipient’s age and obtain an adult signature before delivering the wine. Many states also required that a supplier obtain a permit to ship wine to consumers within the state, and most reported few or no problems with direct shipments to minors. However, it is possible that wine may have a more limited appeal to younger audiences than other beverages, and it is certainly possible that beer and spirits raise different issues than wine in these respects.

It is evident from these comments that states face a choice with important public values on both sides. State officials need evaluate the direct-to-consumer distribution model, both in terms of the distribution opportunities it presents for small producers and the comparative risks it may present of making alcohol available to underage drinkers. Such balancing of public policy values is best addressed by a democratically-elected legislature.

3. Industry Overview

3.1. Production and Supply

3.1.1. Beer

The two largest brewers selling beer in the United States, Anheuser-Busch InBev SA/NV (“ABI”) and Molson Coors Beverage Company (“Molson Coors”), together account for an estimated 65 percent of the beer market nationwide, as measured by revenue, making the U.S. beer market highly concentrated under the standards that the federal antitrust agencies use to

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59 Id.

60 Brewers Association, Comment #477.

61 Community Anti-Drug Coalitions of America, Mass Comment #1.

assess market concentration. ABI is estimated to have 42.4 percent market share, by revenue, in 2021, and Molson Coors is estimated to have 22.4 percent market share, by revenue, in 2021, though their shares have declined modestly in recent years.

Other significant brewers selling in the United States include Constellation Brands, Inc., which imports into the United States the popular Corona and Modelo beer brands, Heineken, D.G. Yuengling and Son Inc., and the Boston Beer Company, among others, plus a large number of small craft brewers.

Although ABI and Molson Coors continue to dominate the market, the number of breweries has increased significantly. Indeed, in 1983, there were fewer than 100 breweries. At the end of 2020, there were 6,406 breweries reporting beer production in the United States. Many of these breweries are small. In 2020, for example, more than 90 percent of these 6,406 U.S. breweries made fewer than 15,000 barrels of beer.

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64 Lombardo, supra note 6.
### Number of Breweries by Production Size, 2020

<table>
<thead>
<tr>
<th>Barrels of Beer (31 gallons)</th>
<th>Number of Breweries</th>
<th>Total Barrels Produced</th>
</tr>
</thead>
<tbody>
<tr>
<td>6,000,001 Barrels and Over</td>
<td>14</td>
<td>116,815,215.28</td>
</tr>
<tr>
<td>2,000,000 to 6,000,000 Barrels</td>
<td>8</td>
<td>24,713,125.35</td>
</tr>
<tr>
<td>1,000,001 to 1,999,999 Barrels</td>
<td>6</td>
<td>7,915,427.46</td>
</tr>
<tr>
<td>500,001 to 1,000,000 Barrels</td>
<td>12</td>
<td>8,384,634.19</td>
</tr>
<tr>
<td>100,001 to 500,000 Barrels</td>
<td>44</td>
<td>9,409,404.42</td>
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<tr>
<td>60,001 to 100,000 Barrels</td>
<td>30</td>
<td>2,347,352.56</td>
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<td>30,001 to 60,000 Barrels</td>
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<tr>
<td>15,001 to 30,000 Barrels</td>
<td>103</td>
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</tr>
<tr>
<td>7,501 to 15,000 Barrels</td>
<td>156</td>
<td>1,626,496.61</td>
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<tr>
<td>1,001 to 7,500 Barrels</td>
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<td>2,659,986.59</td>
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<tr>
<td>1 to 1,000 Barrels</td>
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<td>36</td>
<td></td>
</tr>
<tr>
<td>0 Barrels</td>
<td>220</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>6,406</strong></td>
<td><strong>179,960,476.81</strong></td>
</tr>
</tbody>
</table>

Source: TTB

Industry associations estimate that in 2020, the U.S. beer market was $94 billion, as measured by retail dollar sales, down from $116 billion in 2019. Although the Covid-19 pandemic likely affected 2020 beer sales, beer production in the United States had been declining prior to 2020.

Beer sold in the United States is often segmented based on price and perceived quality. These segments—and their nomenclature—have evolved over time. For example, ABI, with the largest beer sales in the United States, currently groups beer into five segments: value, core, core-plus, premium, and super-premium (listed in order of increasing price and quality). Beer brands in the value segment include ABI’s Busch Light and Molson Coors’ Keystone Light, and in the core segment, Molson Coors’ Miller Lite and ABI’s Bud Light and Budweiser. The core-plus segment includes ABI’s Michelob Ultra brand. Beer brands in the premium segment include imported beers, such as Corona Extra and Heineken. Beer brands in the super-premium segment include other imported beers and many craft beers.

While the value and core segments account for the majority of all beer sold in the United States, consumer preferences have shifted in recent years toward Mexican imports and craft beers, resulting in the premium and super-premium segments growing in sales and gaining market share. This market trend toward the premium and super-premium segments has challenged ABI and Molson Coors, which have stronger positions in the value and core segments than in the premium and super-premium segments. This market trend also increases the choices.

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70 See United States v. Anheuser-Busch InBev, 1:16-cv-01483, Complaint, 5 (D.D.C. July 20, 2016) (the value and core segments were previously referred to as sub-premium and premium).
available to consumers as brewers innovate more premium and super-premium brands to meet increasing demand in those categories.\textsuperscript{71}

Beer consumers may “trade up” or “trade down” between segments in response to changes in price. For example, as the prices of core brands (e.g., Bud Light) approach the prices of premium brands (e.g., Corona Extra), consumers are increasingly willing to trade up from core brands to premium brands. Therefore, competition from brands in one segment (e.g., premium) may serve an important constraint on the ability of brewers to raise beer prices not only in that segment, but also in the other beer segments.\textsuperscript{72} That is, to the extent that price gaps shrink, competition from brands in other segments constrains the ability of brewers to raise prices. However, brewers with a broad portfolio of beer brands across segments, such as ABI and Molson Coors, seek to maintain “price gaps” between each beer segment to minimize competition across segments.

### 3.1.2. Wine and Spirits

Both wine and spirits products range dramatically in price, from products under $10 for a standard 750 ml bottle to those in the hundreds and even thousands of dollars for specialty products. The lowest-price products are often, though not exclusively, domestically produced, while many of the most expensive are imported. As with beer, production is concentrated with the largest producers.

<table>
<thead>
<tr>
<th>Taxable Withdrawals by Category (Proof Gallons)</th>
<th>Number of Distilleries</th>
<th>Total Proof Gallons</th>
</tr>
</thead>
<tbody>
<tr>
<td>8,484,845 PG +</td>
<td>15</td>
<td>299,604,154</td>
</tr>
<tr>
<td>1,441,433 - 8,484,845 PG</td>
<td>28</td>
<td>113,061,113</td>
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<tr>
<td>244,875 - 1,441,433 PG</td>
<td>40</td>
<td>25,181,835</td>
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<td>41,600 - 244,875 PG</td>
<td>107</td>
<td>10,211,768</td>
</tr>
<tr>
<td>7,067 - 41,600 PG</td>
<td>242</td>
<td>4,085,916</td>
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<tr>
<td>1,201 - 7,067 PG</td>
<td>515</td>
<td>1,545,138</td>
</tr>
<tr>
<td>204 - 1,201 PG</td>
<td>611</td>
<td>370,934</td>
</tr>
<tr>
<td>35 - 204 PG</td>
<td>284</td>
<td>30,476</td>
</tr>
<tr>
<td>6 - 35 PG</td>
<td>81</td>
<td>1,674</td>
</tr>
<tr>
<td>0 - 6 PG</td>
<td>19</td>
<td>63</td>
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<tr>
<td><strong>Total</strong></td>
<td><strong>1,942</strong></td>
<td><strong>454,093,071</strong></td>
</tr>
</tbody>
</table>

source: TTB

\textsuperscript{71} See United States v. Anheuser-Busch InBev, 4:20-cv-01282, Complaint, 8 (E.D. Mo. Sept. 9, 2020).

\textsuperscript{72} See id. at 4; see also United States v. Anheuser-Busch InBev, 1:16-cv-01483, Complaint, 6-7 (D.D.C. July 20, 2016).
### Number of Wineries, 2020

<table>
<thead>
<tr>
<th>Taxable Withdrawals by Category (Wine Gallons)</th>
<th>Number of Wineries</th>
<th>Total Wine Gallons</th>
</tr>
</thead>
<tbody>
<tr>
<td>14,902,970 WG +</td>
<td>14</td>
<td>418,281,881</td>
</tr>
<tr>
<td>2,378,168 - 14,902,970 WGs</td>
<td>26</td>
<td>169,835,502</td>
</tr>
<tr>
<td>379,500 - 2,378,168 WGs</td>
<td>106</td>
<td>102,800,375</td>
</tr>
<tr>
<td>60,559 - 379,500 WGs</td>
<td>297</td>
<td>42,095,014</td>
</tr>
<tr>
<td>9,664 - 60,559 WGs</td>
<td>1,134</td>
<td>25,649,657</td>
</tr>
<tr>
<td>1,542 - 9,664 WGs</td>
<td>2,392</td>
<td>10,179,068</td>
</tr>
<tr>
<td>246 - 1,542 WGs</td>
<td>1,795</td>
<td>1,382,756</td>
</tr>
<tr>
<td>39 - 246 WGs</td>
<td>695</td>
<td>93,806</td>
</tr>
<tr>
<td>6 - 39 WGs</td>
<td>179</td>
<td>3,991</td>
</tr>
<tr>
<td>0 - 6 WGs</td>
<td>30</td>
<td>112</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>6,668</strong></td>
<td><strong>770,322,162</strong></td>
</tr>
</tbody>
</table>

source: TTB

The supplier tier is significantly more highly concentrated with respect to lower-priced wines and spirits than higher-priced products. The largest suppliers of wine to the United States include Gallo, Constellation, The Wine Group, and Trinchero Family Estates. The largest suppliers of spirits to the United States include Diageo, Beam Suntory, Sazerac, Brown Forman, Bacardi, and Pernod Ricard.

### 3.2. Retail

The retail tier is typically classified into two categories, on-premise and off-premise. On-premise retailers, such as restaurants, bars, hotels, and casinos, are those that serve alcohol to patrons for consumption on the premises. Off-premise retailers, such as supermarkets, wine and liquor stores, club stores, and convenience stores, are those that sell alcohol for consumption off the premises. States heavily regulate alcohol sales by both groups of retailers. In many states, alcohol is sold in grocery, club, drug, and convenience stores, including both chain and independent stores. Other states allow alcohol sales in only a subset of these. Multiple states do not allow spirits to be sold in grocery stores, and some states apply the same restriction to wine and beer. Where these restrictions exist, private label alcohol brands, a significant source of competition in some states, are much less likely to be available.

### 3.3. Distribution

Distributors purchase, warehouse, transport, and sell beer, wine, and spirits, and they provide a variety of marketing and promotional services on behalf of suppliers. These services may include marketing brands to on- and off-premise retailers, setting up bottle displays and cleaning and arranging shelves, printing drink menus, and providing décor with brand names and logos. (Not every state allows each of these activities, and in some cases providing “free” labor may violate federal laws, as discussed later.) Wine and spirits are often distributed by the same companies, while beer distributors are usually limited to beer.

State regulation of the distributor tier has important effects on competition among beer, wine, and spirits brands. Because many states require suppliers to use a single distributor for a given brand, and in other states this practice is not required but is widely followed, competition among distributors is primarily interbrand rather than intrabrand. Distributors compete on
factors such as logistical capabilities, execution, marketing services, and financial terms to win and (franchise laws aside) retain the business of suppliers with desirable brands. Commonly, leading suppliers with closely competing brands will align themselves with different distributors in a given state. Competition among suppliers therefore often occurs through their proxies, the distributors, although major suppliers also have sales teams that promote their brands directly to chain retailers. Most retailers purchase from multiple distributors to acquire the brands they want to carry, but distributors attempt to influence the specific brands retailers purchase, as well the quantities purchased and shelf and menu placement of brands.

3.3.1. Distribution of Wine and Spirits

The distributor tier for wine and spirits has been consolidating in recent years, with larger, multistate distributors buying regional companies and merging with other multistate distributors. The country’s largest distributor, Southern Glazer’s Wine and Spirits, LLC, now operates in 44 states.73 Following a 2019 joint venture with the West Coast distributor Young’s Market Company, Republic National Distributing Company (“RNDC”) now has operations in over 35 states.74 In August 2021, RNDC announced plans to begin offering brokerage services in five additional control states.75 The next largest distributor, Breakthru Beverage Group, operates in 13 states.76 Another major distributor, Johnson Brother’s Liquor Company, operates in about 20 states but has a smaller presence in many of those.

Many commentators have described distributor consolidation as the greatest threat to competition in the alcohol market.78 One commenter argued that “much of the producer-level competition concerns in the alcohol marketplace could in fact be viewed as a distributor-level problem.”79 Another observed that “[c]onsolidation in the middle tier has not only led to far fewer wholesalers but has also resulted in a small number of very large wholesalers controlling a significant share of U.S. wine sales,”80 and another asserted that “[t]he market for wholesale spirits distribution in the US is effectively closed to new entrants.”81

Some distributors echoed these points, adding that large distributors “have begun to use their market power to further consolidate the market and reduce competition by driving independent distributors out of business.”82 Larger distributors may use long-term agreements with producers to “accomplish indirectly what regulators would never allow them to accomplish directly.”83 That is, distributors with a larger national footprint may be able to leverage their size and enter exclusive arrangements with producers that tend to push out smaller competitors. One distributor described this tendency as a “horizontal boycott”: producers refused to sell to them,

73 https://www.southernglazers.com/portfolio/.
74 https://www.rnrd-usa.com/locations/.
76 https://www.breakthru-bev.com/.
77 https://www.johnsonbrothers.com/locations/.
78 See, e.g., C. Jarrett Dieterle & Teri Quinby, Craft Alcohol Makers Thrive as Government Launches Antitrust Investigation, REASON (Oct. 11, 2021) (arguing for reform of the three-tier system instead of antitrust scrutiny and stating, “Any honest effort to [evaluate competition in the alcohol industry] quickly leads to only one conclusion: Alcohol markets are more competitive than ever-with the exception of the wholesale tier.”).
79 R Street, Comment #209.
80 Wine Institute, Comment #258.
81 Jetro Cash & Carry, Comment #230.
82 Empire Merchants, Comment #206.
83 Id.
citing exclusive contracts with their existing distributors.\(^\text{84}\) They further explained that without certain brands that have significant market share, “wholesalers cannot attract retailers seeking to purchase spirits.” Some describe a market in which smaller distributors have to buy from larger distributors.

The FTC has engaged in advocacy to support changes to state law that would increase competition among wine wholesalers. For instance, the FTC has supported the elimination of exclusive territory requirements, which limit suppliers’ ability to respond to changes in market conditions. Rigid territories prevent a supplier from combining territories to achieve scale efficiencies and prevent the entry of competing wholesalers into areas in which demand is growing.\(^\text{85}\) The FTC has also supported liberalization of laws governing supplier/distributor relations, arguing that such laws eliminate the competitive pressures on distributors to offer lower wholesale prices or better service. For instance, the FTC has argued that a proposal to prohibit a supplier or distributor from canceling, failing to renew, or otherwise terminating a distribution agreement unless there is “good cause” would shield the business of liquor distribution from market forces.\(^\text{86}\) Without such limitations, distributors would know that if they attempt to charge more than the competitive price, suppliers could move their business to new distributors that are willing to charge lower wholesale prices. Requiring proof of “good cause” would eliminate this competitive pressure by requiring suppliers to retain their current distributors, and those constraints would reduce competitive dynamism leading to higher consumer prices.

3.3.2. Distribution of Beer

Within the “three-tier” category, some states allow brewers to self-distribute, but that self-distribution is often restricted and tied to production size—and thus geared toward small brewers. For example, Indiana allows brewers producing up to 90,000 beer barrels annually within the state to self-distribute 30,000 barrels within the state. Brewers with larger volumes must use distributors.\(^\text{87}\) Some states allow a “two-tier system”, meaning that brewers are allowed to own distributors or to distribute their own beer without restriction. For example, ABI is vertically integrated and owns distributors in states such as California and Colorado. According to one commenter, these “‘wholly owned distributors’ typically carry ABI products exclusively, or carry ABI products plus a smattering of very small local brands.”\(^\text{88}\)

\(^\text{84}\) Jetro Cash & Carry, Comment #230.
\(^\text{87}\) IND. CODE ANN. § 7.1-3-2-7.
\(^\text{88}\) Brewers Association, Comment #477.
According to an industry association, there were 3,000 beer distributors in the United States as of 2020.89 Focusing on the overall number of distributors, even at a state level, however, can obscure local market realities as distributors’ contracts with brewers frequently contain territorial limits and prohibit distributors from selling beer outside their respective territories, often by function of state law.

Moreover, within the three-tier system, so-called “independent” beer distributors tend to be affiliated with either ABI or Molson Coors, because they sell large volumes of either ABI products or Molson Coors products, respectively. This leads to many local markets being served by two large distributors—each affiliated with either ABI or Molson Coors—and most other brewers must rely on one or the other to get to market. Consequently, the majority of other brewers’ beers are distributed either by the ABI-affiliated distributor or the Molson Coors-affiliated distributor in a given geographic area, although in some geographic areas, a handful of small boutique distributors are also present.90 One commenter described this dynamic as “a duopoly that together holds ninety percent or greater of the beer market in a specific geographic territory” and commented that “[t]his distribution choke point, in turn, helps entrench dominant beer suppliers by forcing smaller brands to compete for ‘share of mind’ in a highly consolidated distribution channel that prioritizes existing major brands.”91

The commenter continued to observe that in markets served by ABI’s wholly owned distributors “virtually every small supplier has no choice but to seek distribution through [the Molson Coors-affiliated distributor]”, leaving small brewers “with a single effective distribution option – a monopoly – in that territory.”92

There are currently no nationwide beer distributors, though recent years have seen substantial changes in beer distribution. For example, in addition to the distributors that are owned by ABI,93 the largest brewer in the United States, the distribution tier now includes large distributors that operate in a number of geographic areas. These distributors have grown by acquiring operations in geographic territories in which they were not yet present. With these acquisitions, some distributors have grown in scale and now have operations across multiple states. Reyes Beer Division, for example, with over 37 facilities across seven states and the District of Columbia,94 announced in 2021 the acquisition of four Molson Coors-affiliated distributors, with sales totaling over 10 million cases of beer. Similarly, Redwood Capital Investments has purchased large ABI-affiliated distributors in Houston, Texas, and Tampa, Florida.

91 Brewers Association, Comment #477.
92 Id.
93 At the time the Division filed its complaint in connection with the eventual consent decree for the ABI/SABMiller transaction, ABI-owned distributors distributed about nine percent of ABI’s beer in the United States. The consent decree governing the ABI/SABMiller transaction prohibits ABI from acquiring a distributor if the acquisition would cause more than 10 percent of ABI’s beer in the United States to be sold through ABI-owned distributors. The consent decree is set to expire in 2026.
94 Reyes Beer Division is part of Reyes Holdings, Inc. See Reyes Beer Division, at https://reyesbeerdivision.com/.
Several concerns may arise as a distributor grows. First, local craft brands may be concerned that the distributor will focus on large national brands at their expense. Additionally, as a distributor gains geographies and potentially holds more of a brewer’s footprint, the distributor may be able to require a brewer that is expanding into new geographies to use that distributor in multiple geographies. Finally, once a brewer is established with the distributor in multiple states, if the brewer becomes displeased with the distributor’s performance in one state, the brewer may want to terminate the contract for that state, but not elsewhere. However, because of the multi-state relationship and the difficulty of terminating a distributor contract under state franchise laws, the distributor may be able to strong-arm the brewer into staying with the distributor in both states or risk a degradation in performance in the other state. As discussed previously, state franchise laws severely limit a brewer’s ability to switch to a distributor that will better support its brand. Thus, while expansion and consolidation of distributors across states may not create horizontal overlaps or increase market concentration in a particular geographic territory, they can still raise concerns about conduct that reduces competition from smaller distributors by creating barriers to entry or expansion.

3.4 Competition Matters in Adjacent Industries

Some comments raised competition-related matters going beyond alcohol beverage markets yet with potential effects worth mentioning.

Aluminum, used in cans, is important for beer and cider makers. It stands to reason that the conditions of competition in aluminum affects alcohol markets. Cider makers have complained about packaging supply monopolization, stating “can supply access is nearly impossible for small cideries,” a serious problem when “canned products are a fast growing segment of the beverage alcohol sector.” Beer industry representatives state that their “industry became more reliant on aluminum cans during the [Covid-19] pandemic due to shifts in consumer demand.” Beer industry representatives state that their “industry became more reliant on aluminum cans during the [Covid-19] pandemic due to shifts in consumer demand.” Beer industry representatives state that their “industry became more reliant on aluminum cans during the [Covid-19] pandemic due to shifts in consumer demand.” They urged “coordinate[d]ion with the FTC and the Antitrust Division of the Department of Justice on providing to Congress and publishing for public review the report on competition issues in aluminum benchmarking in the U.S.” Section 232 tariffs have an effect on aluminum prices, and the comment also reports that “aluminum producers and other upstream suppliers charge end users in the beverage industry, including brewers, tariffed prices for cansheet” that is not even subject to these tariffs. The beer industry group has also urged support for legislation that would provide for additional federal oversight of the aluminum market, as well as Congressional action to provide further relief for food and beverage industry members who experienced inventory losses because of the Covid-19 pandemic.

A number of commentators raised supply chain disruptions and matters of international trade, including a comment urging support for permanent suspension of “retaliatory tariffs on

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95 Am. Cider Ass’n Comment, #268.
96 Beer Institute Comment, #262.
97 Id.
98 Id.
99 See, e.g., USA Rice Comment, #255 (noting “significant disruptions to the supply chain” facing brewers and impacting farmers, and citing Exec. Order 14017, “America’s Supply Chains”); Food Industry Ass’n Comment, #250 (expressing concern that additional regulatory burdens could “hurt our economic recovery,” in light of the “significant industry-wide challenges throughout the food and beverage industry, including facility closures and supply chain shortages in some cases.”).
wine and spirits” from the EU.\textsuperscript{100} While recognizing these are important concerns for the beverage alcohol markets, they are outside the scope of this report.

4. Competition in the Alcohol Markets and Federal Antitrust Enforcement

4.1. Department of Justice Enforcement in the Beer Markets

Over the last two decades, the global beer industry has undergone significant consolidation. The United States has not been immune to this trend, with the U.S. beer market becoming increasingly concentrated over time. Some of the increased concentration was “due to the growth of Anheuser-Busch, Miller and Coors, whose expansion was largely internal.”\textsuperscript{101} Some of the increased concentration may have resulted from the absence of consistent merger enforcement. With the 2008 joint venture of SABMiller plc and Molson Coors Brewing Company, for example, the second and third largest brewers in the United States combined.

Moreover, many arguments from merging parties in support of consolidation do not appear to have been borne out. For example, while efficiencies from the SABMiller plc and Molson Coors Brewing Company joint venture were contemplated, research finds that beer prices increased following its creation.\textsuperscript{102} Merging parties consistently advocate for transactions with bold predictions about efficiencies sufficient to prevent price increases, but the agencies are not aware of evidence that those efficiencies have been borne out in practice. Similarly, merging parties often argue against any likelihood of coordinated interaction after a merger consolidates the number of independent decisionmakers in an industry, but continued leader/follower dynamics in pricing suggest coordination should be a greater concern in merger reviews.

In a highly concentrated market such as this, several competitive concerns arise.

First, the higher a brewer’s market share, the greater its incentive to increase the price of its brands, because the brewer loses fewer sales to its rivals as a result of the price increases. For example, when ABI attempted to acquire Grupo Modelo (referenced below), the Antitrust Division alleged that ABI would recapture a significant portion of sales lost due to price increases on Grupo Modelo’s beers if ABI raised prices post-merger. This was because a significant percentage of those sales that would otherwise have been lost would have gone to other ABI-owned brands due to ABI’s market leading position in the value and core segments and portfolio of significant brands across other beer segments.\textsuperscript{103}

\textsuperscript{100} Southern Glazer’s Wine and Spirits Comment, #296.
\textsuperscript{101} Kenneth G. Elzinga & Anthony W. Swisher, The Supreme Court and Beer Mergers: From Pabst/Blatz to the DOJ-FTC Merger Guidelines, REV. INDUS. ORG. (2005) 26:245-267. This article reports that there were 170 horizontal mergers between 1950 – 1983, and that “most of the mergers in the beer industry did not involve firms of significant stature.” Id. at 247, 264. Rather, they generally “represented the demise of an inefficient firm which salvaged some remainder of its worth by selling out to another brewer.” Id. at 264. According to the article, after the Division initiated its first enforcement action in the beer market against Anheuser-Busch in 1958 (which resulted in a divestiture), Anheuser-Busch did not pursue another acquisition until 1980 when it acquired a Schlitz Brewing Company brewery in New York. Id. at 247-48.
\textsuperscript{102} See Nathan H. Miller, et al., Oligopolistic Price Leadership and Mergers: the United States Beer Industry, AM. ECON. REV., 111 (10): 3123-59 (2021) ("We show an abrupt increase in the prices of ABI and MillerCoors shortly after the 2008 consummation of the Miller/Coors merger, both in absolute terms and relative to the prices of Modelo and Heineken, the other large brewers."); Nathan H. Miller & Matthew C. Weinberg, Understanding the Price Effects of the MillerCoors Joint Venture, 85 ECONOMETRICA 1763 (Dec. 2017).
Second, the industry may be capable of tacit coordination among the largest firms, either with respect to prices or by the creation of joint barriers to entry. Tacit coordination occurs when companies in a concentrated market, without forming an agreement, (1) engage in conduct that “blocks or slows would-be market entrants”; or (2) “in effect share monopoly power.” For example, on the latter point, in several matters, the Antitrust Division has alleged that ABI has employed a “price leadership” strategy whereby ABI, as the largest U.S. brewer, seeks to establish industry-wide price increases by being the first brewer to announce its prices for the upcoming year. In most local markets, ABI is the market share leader and issues its price announcement first, purposely making its price increases transparent to the market so its competitors can follow its lead. The Antitrust Division has alleged that Molson Coors often follows ABI’s price increases. When rivals follow a leader’s price increases, that not only extends the higher prices to other brands, but it also makes an even larger price increase by the leader profitable because the leader is less likely to lose sales to those rivals.

Third, a large brewer, or large brewers acting in parallel, may be able to create barriers to entry and expansion by rivals through the brewer’s unilateral disproportionate influence on beer distributors. For example, with respect to ABI’s transaction with SABMiller (referenced below), the Antitrust Division alleged that ABI had used a variety of practices and contractual provisions to promote exclusivity with independent distributors that sell ABI beer, to the disadvantage of rival brands. As stated above, smaller brewers have expressed concern that their distributors favor the large brewers and make it difficult for them to expand sales.

4.1.1. Recent Acquisitions in the Beer Industry

Vigorous antitrust scrutiny as to mergers and conduct in this industry is warranted in light of its high concentration. In what follows, we highlight two cases where the Antitrust Division took enforcement actions to prevent significant further consolidation of brewers in the U.S. beer industry, prohibit ABI from engaging in certain distribution practices, and limit ABI’s vertical integration into distribution.

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104 See Miller, supra note 103 (presenting an empirical model of oligopolistic price leadership that can be evaluated with market level data on prices and quantities and applying the model to the U.S. beer industry, which exhibits such price leadership behavior).


108 See, e.g., Brewers Association, Comment #477.

109 In investigating and challenging large beer acquisitions, the Antitrust Division has found that beer is the relevant product market for analyzing the likely competitive effects. Beer’s taste, alcohol content, image (e.g., marketing and consumer perception), price, and other factors make it substantially different from other alcohol beverages, such as wine and distilled spirits. The Division has also found that both national and local geographic markets can be impacted by a merger, depending on the facts. The relevant geographic markets that the Division has used to analyze the likely competitive effects are best defined by the locations of the customers who purchase beer, rather than by the locations of breweries; the Division has thus considered the competitive impact of the acquisition in local metropolitan statistical areas. At the local level, beer brewers make many pricing and promotional decisions, reflecting local brand preferences and demand, demographics, and other competitive conditions and factors, which can vary significantly from one local market to another. Important competitive decisions, however, may also be
**ABI/Grupo Modelo**

In 2013, ABI, the largest U.S. brewer, sought to acquire for $20.1 billion Grupo Modelo, the third-largest brewer of beer sold in the United States (specifically, the remaining 64.7 percent interest of Grupo Modelo that ABI did not already own). Grupo Modelo’s Corona and Modelo brands competed closely with ABI’s Budweiser and Bud Light brands. In its complaint, the Division alleged that the transaction would likely result in ABI increasing prices across all of its brands because, with more brands in its portfolio, ABI was more likely to recapture a significant portion of any lost sales as a result of price increases. The Division also alleged that ABI and MillerCoors engaged in tacit price coordination through ABI’s “price leadership” strategy, but that Modelo put pressure on ABI to maintain or lower prices.

In a settlement, the Antitrust Division required ABI to divest Grupo Modelo’s entire U.S. business, plus a state-of-the-art brewery in Mexico, to Constellation Brands, Inc. Since the divestiture, Constellation has been very successful in expanding its sales of the Modelo brands in competition with ABI and others. According to Constellation, it has tripled its production capacity since the divestiture.

**ABI/SABMiller**

Two years later, the Division prevented ABI from acquiring SABMiller’s U.S. brewing business and effectively monopolizing the U.S. beer industry. At the time of the proposed acquisition, SABMiller was also the second largest beer brewer worldwide. In the United States, SABMiller owned 58 percent of MillerCoors LLC, which was a joint venture between SABMiller and Molson Coors responsible for brewing, importing, and selling the parent companies’ beers in the United States. MillerCoors was the second-largest brewer in the United States. The transaction would have combined the two largest beer brewers in the United States, together accounting for what was then more than 70 percent of beer sold in the United States at that time. The Division required ABI to divest SABMiller’s entire U.S. business to Molson Coors.

The Division further concluded that the divestiture to Molson Coors alone was insufficient to remedy the competitive harm arising from that transaction. Because Molson Coors and ABI have interactions outside the United States which could present opportunities post-merger for

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111 Constellation Brands, Inc., FY 2021 Form 10-K at Item 1 (filed Apr. 20, 2021), available at https://www.cbrands.com/investors/reporting?group=Annual%20Filings (“In the past eight years we have more than tripled our production capacity in Mexico allowing us the opportunity to further expand our leadership position in the high-end segment of the U.S. beer market.”).
anticompetitive conduct within the United States, the Division required additional relief aimed at protecting the competitive constraint that other brewers provide—in particular, brewers of craft and import beers—on ABI’s and Molson Coors’ ability to raise prices on their beers. The consent decree that memorializes these distributor-related requirements is set to expire in 2026.113

The consent decree prohibits ABI from instituting or continuing many practices and programs that limit the ability and incentives of independent beer distributors to sell and promote the beers of ABI’s rivals, including craft and import beers. For example, the consent decree prohibits ABI from, among other actions, penalizing an independent distributor based on the independent distributor’s sales of rival brands (e.g., ABI cannot withhold new ABI brands from the independent distributor based on that distributor’s sales of rival brands). ABI thus cannot use these distribution-related practices to prevent or limit rival brewers from securing the distribution necessary to effectively compete with ABI, which is especially important with respect to craft and import beers that constrain ABI’s ability to raise the prices of its beers. Additionally, ABI is barred from acquiring distributors if more than ten percent of ABI’s beer sold in the United States, measured by volume, would be sold through ABI-owned distributors after such an acquisition. This prohibition limits ABI’s ability to acquire distributors and then cause the distributor to cease to promote or expel rival brands from the distributors’ portfolios, which could impede the rival’s sales or force it to find another route to market.

Recent Craft Acquisitions

Even with these enforcement actions, the beer industry has nevertheless seen additional consolidation resulting from the larger brewers, namely ABI, and to a lesser extent Molson Coors, acquiring craft brands throughout the United States. ABI has been active in this space, acquiring over ten craft beers throughout the country since 2011.114 More recently, in 2020 Molson Coors acquired Michigan-based Atwater.

Smaller brewers often express concern that these acquisitions of leading craft beers across the country allow ABI and Molson Coors to extend their market power and to hinder the growth of competitive brands. One commenter noted, for example, that “suppliers leverage their position as the key partners to their wholesaler distribution networks to ensure that their brands in every category—established or emerging—receive outsized wholesaler sales and distribution efforts.”115 Small brewers highlight that by purchasing ownership of strong brands across all beer segments and wielding influence over distributors (or direct control in the case of ABI’s

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115 Brewers Association, Comment #477.
wholly-owned distributors), a large brewer can often obtain preferred shelf space in grocery stores and tap handles in bars and restaurants, displacing their rivals’ brands, especially smaller craft brands.

Small brewers are concerned that these acquisitions may pose the risk that larger brewers extend their market power into the super-premium (craft beer) segment and incentivize distributors to reduce their efforts to sell competing craft beers, drop them entirely, or refrain from taking on new craft beers.

While these craft beer acquisitions may not significantly increase market concentration in a particular geographic territory, they may still, by their effects on distribution, operate to protect the largest firms from competition, and substantially lessen competition in a manner that implicates Section 7 of the Clayton Act. If the craft brewers’ access to large distributors that sell ABI or Molson Coors beer were reduced or eliminated, these competing craft brewers could be forced to use smaller, less efficient distributors that typically receive inferior treatment at retail establishments. In addition, if a larger number of craft beer brands were pushed into a smaller distributor, that may increase the complexity and cost of distribution, which could also increase the distributor’s incentive to raise the price of all of its craft beer brands. Similarly, as the number of brands carried by a distributor increases, the distributor may become less focused on promoting the smaller brands that it carries.\footnote{See \textit{United States v. Anheuser Busch InBev}, 1:16-cv-01483, Competitive Impact Statement, 11 (D.D.C. July 20, 2016)} And, as discussed above, because state franchise laws often may make it very difficult for a brewer to switch distributors, brewers have little recourse should the distributor hamper the brewer’s growth.

4.2. FTC Enforcement in the Wine and Spirits Markets

The FTC has investigated proposed mergers and acquisitions involving wine and spirits suppliers as well as those in the distributor tier. In investigating wine and spirits supplier transactions, the FTC focuses on the relevant product markets where harm to competition is most likely to be experienced. The FTC evaluates the market structure and conditions, including current competitors, market shares, and barriers to entry. The FTC considers a transaction’s likely effect on factors including price, quality, choice, and innovation. Because competition is typically strongest among wine and spirits products with similar flavor, characteristics, and price, the FTC often defines a relevant product market by reference to product characteristics and product price. As discussed below, the FTC has taken action against proposed supplier mergers that were likely to cause harm in markets such as super-premium vodka, popular gin, and low-priced sparkling wine.\footnote{See Pernod Ricard/V&S (https://www.ftc.gov/enforcement/cases-proceedings/081-0119/pernod-ricard-sa-matter) and Gallo/Constellation (https://www.ftc.gov/enforcement/cases-proceedings/191-0110/e-j-gallo-winery-constellation-brands-matter).} With respect to the geographic location of harm, the FTC has often concluded that an anticompetitive transaction will harm competition in the United States as a whole. However, the FTC also examines whether a transaction that is not harmful in the United States generally might reduce competition in a narrower geographic region.

When investigating proposed wine and spirits distributor combinations, the FTC has looked for markets where distributors overlap geographically and with respect to the categories of products they carry. The FTC has considered whether the combining distributors compete to
win the business of the same wine and spirits suppliers as to the same products, and whether they compete to sell those products to the same retailers.

4.2.1. Supplier Mergers

In 2008, the FTC challenged Pernod Ricard SA’s proposed $9 billion acquisition of V&S Vin & Sprit AB, a Swedish spirits company that owned the Absolut vodka brand. Because Pernod owned the rights to sell Stolichnaya vodka in the United States, the proposed transaction would have eliminated U.S. competition between Absolut and Stolichnaya, then the two leading super-premium vodka brands. To avoid this harm, the FTC approved a Consent Order requiring Pernod to terminate its rights to sell Stolichnaya vodka in the United States.

The Consent Order also addressed the potential for harm to competition in four other distilled spirits markets. In purchasing V&S, Pernod would have assumed V&S’s role in a joint venture between V&S and the corporate parent of Beam Global Spirits & Wine, Inc. (“Beam Global”). Beam Global owned brands that competed with Pernod brands in the United States markets for Cognac, domestic cordials, coffee liqueur, and popular gin. The FTC found that Pernod’s participation in this joint venture would give Pernod access to competitively sensitive pricing and promotion information about the competing Beam Global brands. The FTC’s Order resolving competitive concerns about the joint venture imposed-firewalls to prevent Pernod from acquiring and using competitively sensitive information about the competing Beam Global brands. Shortly after the Commission’s Order was made final, Beam Global terminated its distribution joint venture with Pernod, ending the need for enforcing the firewall provisions of the Order.

In 2019, E. & J. Gallo Winery and Constellation Brands, Inc. entered into an asset purchase agreement by which Gallo would acquire more than 30 mostly low-priced wine, brandy, concentrate, and additive brands, along with several wine-making facilities, from Constellation. Following an extensive investigation, the FTC challenged the transaction over potential impacts on competition for multiple products: entry-level sparkling wine, low-priced sparkling wine, low-priced brandy, low-priced port and low-priced sherry fortified wines, and high color concentrates. The FTC analyzed the effects of this transaction within a relevant geographic market of the United States. To prevent harm to competition, the FTC, Gallo, and Constellation entered into a Consent Agreement that removed multiple brands and related assets from the transaction.

4.2.2. Distributor Mergers

In 2018, the large, multistate distributors RNDC and Breakthru Beverage Group announced an agreement to merge. RNDC and Breakthru had competing operations in six states and the District of Columbia. In a year-long investigation, FTC staff obtained evidence that the proposed merger would likely result in higher prices and diminished service in the distribution of wine and spirits in multiple states, adversely impacting both suppliers of wine and spirits and the retail customers that purchase those products. After FTC staff expressed their concerns about likely harm to competition, RNDC and Breakthru abandoned their proposed merger in April.

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2019. RNDC subsequently formed a joint venture with the West Coast distributor Young’s Market Company, with which it had no overlapping operations.

4.2.3. Anticompetitive Conduct

The FTC is attentive to the potential that firms in these markets, especially those with a large market share, could engage in collusive, coercive, or exclusionary conduct that harms competition. For instance, a dominant distributor that uses exclusive contracts with suppliers to impede effective competition by smaller distributors may violate the antitrust laws. That said, the Commission has not brought cases in this area in the last several decades. Given the complaints regarding exclusionary conduct by distributors, more attention to these markets may be warranted.

5. The Treasury Department’s Regulation of Competition in the Alcohol Sector

The 21st Amendment repealed Prohibition in 1933. In his repeal proclamation, President Franklin D. Roosevelt stated “The policy of the Government will be to see to it that the social and political evils that have existed in the pre-prohibition era shall not be revived nor permitted again to exist. We must remove forever from our midst the menace of the bootlegger and such others as would profit at the expense of good government, law, and order.”

Roosevelt established a Federal Alcohol Control Administration (FACA), which prescribed a Code of Fair Competition for the alcohol beverage wholesale industry. The Supreme Court later held the National Industrial Recovery Act of 1933, the authority behind FACA, unconstitutional.

Within months, on August 29, 1935, the Federal Alcohol Administration Act became law. The FAA Act largely continued FACA’s policies, prohibiting most of the activities delineated in the FACA codes. The FAA Act remains substantially unchanged more than 85 years later.

5.1. FAA Act’s Exclusive Outlet, Tied House, Commercial Bribery, and Consignment Sale Prohibitions

Section 105 of the FAA Act contains six categories of “unfair competition and unlawful practices,” four directed at the relationships between producers, wholesalers, and retailers, and two relating to advertising and labeling. The former group prohibits the following practices:

- The exclusive outlet provision bars a producer or wholesaler from “requir[ing], by agreement or otherwise” a retailer to purchase alcohol from that producer or wholesaler to the exclusion of alcohol sold by others.
- The tied house provision bars a producer or wholesaler from “inducing” a retailer to purchase its alcohol to the exclusion of others through certain specified means, such as partial ownership of the underlying property, offering credit, and repaying loans.

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120 48 Stat. 1721 (1933).
121 Exec. Order No. 6474 (Dec. 4, 1933).
125 The full list of inducements in current regulations (27 CFR § 6.21) includes:
The **commercial bribery** provision bars a producer or wholesaler from using money or gifts to induce a retailer or wholesaler to buy its products to the exclusion of others by giving things of value to its officers, employees, or representatives.

The **consignment sale** provision generally bars a producer or wholesaler from selling, or a retailer from purchasing, alcohol beverages on consignment or with the privilege of return.

The FAA Act prohibits the first three of these activities only if they require or induce purchases to the “exclusion” of products sold by a competitor. This is discussed in more detail below.

The legislative history indicates that the FAA Act’s tied-house, commercial bribery, exclusive outlet, and consignment sales prohibitions were written with an anti-monopoly spirit. Congress was concerned particularly with the power of large producers and wholesalers, but also other social evils, including the activity of bootleggers and other black market sellers, and overconsumption as might be caused by larger producers’ aggressive marketing techniques. As stated in the Senate Report:

> [C]ontrol by producers and wholesalers of retail outlets through the various devices such as those prohibited by the bill has been productive not only of monopoly but also of serious social and political evils which were in large measure responsible for bringing on prohibition.126

As the legislative history suggests, at the time of the Act’s passage, Congress was particularly concerned about the power of what was called the “Whisky Trust.” Additionally, small retailers struggled to cope with pressures exerted by larger manufacturing or wholesale interests.127 “The underlying premise [behind the FAA Act] is that a genuinely competitive

(a) By acquiring or holding (after the expiration of any license held at the time the FAA Act was enacted) any interest in any license with respect to the premises of the retailer;
(b) By acquiring any interest in the real or personal property owned, occupied, or used by the retailer in the conduct of his business;
(c) By furnishing, giving, renting, lending, or selling to the retailer, any equipment, fixtures, signs, supplies, money, services or other thing of value, subject to the exceptions contained in subpart D;
(d) By paying or crediting the retailer for any advertising, display, or distribution service;
(e) By guaranteeing any loan or the repayment of any financial obligation of the retailer;
(f) By extending to the retailer credit for a period in excess of the credit period usual and customary to the industry for the particular class of transactions as prescribed in § 6.65; or
(g) By requiring the retailer to take and dispose of a certain quota of any such products.

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127 See, e.g., 79 Cong. Rec. 11796 (“Nobody who believes in enforcement will want to go back to the old days where the saloon was controlled by the brewery or the distillery.”) (Congressman Vinson); 14568 (“The brewers, as everyone knows, are the ones who have caused the greatest trouble in the past. It is common knowledge that in the old days on almost every street corner in the big cities the brewers equipped saloons, and dominated them.”) (Congressman Fuller) (Aug. 24, 1935); Nat’l Distributing, 626 F.2d 997, 1008 (“The Members of Congress debating the bill repeatedly stated that the tied house provision was designed to prevent control by alcoholic beverage producers and wholesalers over retail outlets, especially saloons.” (citing legislative history)); accord Foremost, 860 F.2d at 237 (noting Congress’s “fundamental intention to prevent supplier control over retail outlets”—not merely to “interfere with a laundry list of disfavored transactions”).
market leads to low prices, and low prices remove any incentive for the creation of a corrupt black market—one of the prime evils of Prohibition.”

The FAA Act prohibitions on exclusionary and anticompetitive conduct are self-evidently not a mirror of those in contemporary antitrust law. They mainly are concerned with vertical conduct and vertical integration, and often take a categorical approach, while contemporary antitrust law has no explicit bans on vertical integration and with rare exceptions assesses vertical restraints on a “rule of reason” basis. In addition, the FAA Act provisions do not call for proof of market or monopoly power, as is common in contemporary antitrust caselaw, nor do all the provisions require evidence of an agreement, as does Section 1 of the Sherman Act. At the time the Act was passed, the House Report noted that the prohibitions were “analogous to those prohibited by the antitrust laws” but emphasized that conditions in the spirits industry were such that “Federal trade” laws were “insufficient” to achieve Congress’s goals.

5.1.1. Exclusion

5.1.1.1. Courts Limit Three Provisions to Exclusionary and Anticompetitive Activity

The exclusive outlet, tied house, and commercial bribery provisions of the FAA Act all require proof that the practice resulted in “the exclusion in whole or in part” of products offered for sale by others in interstate or foreign commerce. TTB’s predecessor agency, the Bureau of Alcohol, Tobacco, and Firearms, took the view that any conduct that led to any reduction in the sale of a competitor’s products constituted actionable exclusion. Under that view, the Bureau took a broad range of conduct as exclusionary under the rules, ranging from tying arrangements, to predatory pricing (i.e., selling below cost), to the provision of gifts to retailers, so long as the bureau could show a subsequent reduction in sales of a competitor’s product.

The advantage of the pre-1995 approach lay in its simple, bright-line nature, but decisions in the 1980s and 1990s in two federal circuits read the statute more narrowly. In 1980, the D.C. Circuit in *National Distributing v. Treasury* concluded that the tied-house provision did not generally prohibit below cost pricing, “so long as [the price cut] is not connected with an agreement or understanding to purchase products from one wholesaler to the exclusion of others” or “used as a ‘subterfuge’ to disguise a grant of financial assistance given to create a tied house, or to obtain an exclusive sales arrangement.” The D.C. Circuit, engaging in a read of the legislative history, based its reasoning on the premise that price competition was, in fact, among the things that Congress sought to promote, both for the benefit of consumers and to combat the black market.

In 1992, the D.C. Circuit, in *Fedway Assoc. v. Treasury* considered a wholesaler program that awarded microwave ovens and other appliances to retailers who bought a specified quantity

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128 *Fedway Assoc. v. Treasury*, 976 F.2d 1416, 1422 (D.C. Cir. 1992), citing *Nat’l Distrib.*, 626 F.2d at 1008 (“[I]n both Houses of Congress there appeared to be total unanimity on the conclusion that lower [alcohol] prices were desirable.”).
130 House Report at 12, 3.
131 626 F.2d 997, 1004, 1016 (D.C. Cir. 1980).
132 See also *Foremost Sales v. ATF*, 860 F.2d 229, 237 (7th Cir. 1988) (concluding that the tied house and commercial bribery provisions do not necessarily bar wholesalers from buying space in a retailer’s newspaper ads unless the “purpose or potential effect is to lead to supplier control over ostensibly independent purchasers.”).
of spirits. The Bureau considered the program exclusionary, based on its view that “exclusion” meant any inducement that led to a loss of competitors’ sales. The Court, which saw the appliance gifting program as analogous to a volume discount, and potentially pro-competitive, found the Bureau’s interpretation unreasonable. It concluded that

Both the statutory text and the relevant legislative history signal that Congress intended the “exclusion” criterion to direct the regulator to determine something more. Congress, we are satisfied, used “exclusion” to indicate placement of retailer independence at risk by means of a “tie” or “link” between the wholesaler and the retailer or by any other means of wholesaler control.

The court suggested that exclusion required “a factual showing that retailer independence is potentially threatened” by the conduct in question.

5.1.1.2. Treasury Regulations Following Fedway

ATF amended its trade practice regulations in 1995 in response to Fedway, stating that the courts had “raised questions concerning ATF’s traditional interpretation of the term ‘exclusion.’”134 These regulations, among other things, defined “exclusion,” borrowing significantly from the D.C. Circuit’s Fedway opinion.135 The current definition reads as follows:

(a) Exclusion, in whole or in part occurs:

(1) When a practice by an industry member, whether direct, indirect, or through an affiliate, places (or has the potential to place) [retailer or trade buyer] independence at risk by means of a tie or link between the industry member and [retailer or trade buyer] or by any other means of industry member control over the [retailer or trade buyer], and

(2) Such practice results in the [retailer or trade buyer] purchasing less than it would have of a competitor’s product.136

With respect to each of the prohibitions requiring proof of exclusion, the Bureau has imposed a further layer of presumptive categories, sometimes referred to as “red lights.” These further elaborate practices that, according to TTB, in their nature put “independence at risk” or constitute “exclusion.” Among the listed practices are “a threat or act of physical or economic harm,” the paying of a sloting fee (e.g., a fee for shelf space), partial ownership of a retailer (when used to influence its purchases), and the requirement to buy one product as a condition of buying another (tying), secret bribes, and others.137 The Bureau has also specified specific

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133 976 F.2d 1416 (D.C. Cir. 1992).
136 See 27 CFR § 6.151 (retailer independence); § 8.51 (retailer independence); and § 10.51 (trade buyer independence).
137 See 27 CFR §§ 6.152, 8.52, 10.52. For example, the full list of “practices which put retailer independence at risk”, in 27 CFR § 6.152, follows:
(a) The act by an industry member of resetting stock on a retailer’s premises (other than stock offered for sale by the industry member).
(b) The act by an industry member of purchasing or renting display, shelf, storage or warehouse space (i.e. sloting allowance).
exceptions for allowed inducements (such as product displays worth less than $300 and
samplings) under subpart D of the tied house regulations and an exclusive outlet green light for
as-needed supply contracts for less than a year.\textsuperscript{138}

In the more than 25 years since the revised regulations became effective, no industry
members have challenged TTB’s application of them in court. As a result, no courts have
assessed or interpreted the 1995 rules.

5.1.1.3. Sloting Fees, or “Pay to Play” Requirements

Sloting fees are a category of fees paid to retailers for stocking and displaying products,
and can be considered a subset of “pay to play” schemes more generally.\textsuperscript{139} For example, a
retailer may receive a fee to carry or provide preferential display space for a specific product.
Since 1995, the Bureau has regarded the payment of sloting fees to constitute a \textit{per se} threat to
retailer independence under the tied-house provisions. It has settled cases under the provision,
including offers in compromise totaling nearly $2 million in connection with a series of related
cases against certain suppliers who participated in a Las Vegas-area sloting fee program run by
Harrah’s.\textsuperscript{140}

The prohibition on sloting fees is similar to other bans on side-payments to gatekeepers
in other industries, such as the traditional bans on “payola” in the music industry, the bans on
rebates (side-payments) by large oil companies to the railroads, and the bans on “fast lane” side-
payments in Net Neutrality rules.\textsuperscript{141} In contrast, there is no ban on sloting fees or “pay to play”
in retail more generally.\textsuperscript{142}

While the ban on sloting fees in the alcohol industry has rarely been considered in this
light, it forms part of a long-standing debate, in recent decades centered on Net Neutrality rules,
over whether the banning of pay-to-play schemes aids competition and innovation.\textsuperscript{143} The
argument in favor of banning such side-payments is their tendency to distort competition among
producers and their potential to further entrench dominant players by serving as a barrier to entry
for new market participants, particularly innovators. The counterargument tends to either see the
fees as efficiency-promoting, as reasonable compensation for the gatekeeper, allocation of risk,
or a potential means for new and unknown entrants to gain access to a market.

5.1.1.4. Category Management

\begin{itemize}
\item (c) Ownership by an industry member of less than a 100 percent interest in a retailer, where such ownership
is used to influence the purchases of the retailer.
\item (d) The act by an industry member of requiring a retailer to purchase one alcoholic beverage product in
order to be allowed to purchase another alcoholic beverage product at the same time.
\end{itemize}
\textsuperscript{138} 27 CFR §§ 6.81 - 6.102 (tied house exceptions), § 8.53 (exclusive outlet green light).
\textsuperscript{139} Based on the language of TTB regulations, “pay to play” schemes only constitute sloting fees when the payment
relates to a specific location within the retailer’s premises. \textit{See} 27 U.S.C. § 205(b)(4); 27 CFR § 6.152(b).
\textsuperscript{140} https://www.winebusiness.com/content/file/press_release_fy-11-4_faa_oic.pdf; https://www.ttb.gov/press/press-
release-fy-19-16.
\textsuperscript{141} 47 U.S.C. § 508, California SB-822.
\textsuperscript{142} \textit{Cf.} FTC Wine Report, \textit{supra} note 49.
\textsuperscript{143} \textit{See, e.g.}, Christopher T. Marsden, \textit{Network neutrality: From policy to law to regulation} (2017), available at
https://library.oapen.org/handle/20.500.12657/31900 (survey of history of net neutrality debates); \textit{Keeping the
Internet Neutral?: Tim Wu and Christopher Yoo Debate}, 59 FED. COMM. L.J. 575 (2007) (debate over Net
Neutrality provisions).
Category management refers broadly to the purchasing, stocking, and display decisions that a retailer makes for a class of products such as laundry aids, soft drinks, or wine or beer. Wholesalers or producers seek to influence these decisions. This influence ranges from the provision of suggested shelving schematics, to the takeover of shelving by a wholesaler, to a “category captain” scheme, where a retailer may invite a large supplier to manage the category on behalf of the retailer. In the last case, a supplier then makes decisions on how much and which of a competitor’s product to buy and how to display them. It also provides the category captain with information on competitors’ marketing and product development.

Given the FAA Act’s interest in the promotion of fair competition and its concern with the power of large producers, category management practices raise obvious concerns. Category management practices are most obviously in tension with the tied house provision’s ban on “inducements” and its effort to maintain a distance between retailer and wholesaler or producer.

Category management practices may warrant renewed TTB attention. The comments received include complaints suggesting that exclusionary category management practices remain undeterred, and serve large producers and wholesalers while eroding retailer independence. TTB’s current approach, which allows the suggested shelf schematics but bans the provision of additional services is not successfully deterring conduct that is in tension with the goals of the statute.

The Bureau’s approach to category management began in 1986 with Stein Distributing. The Bureau (then the ATF) suspended the permit of a wholesaler who prepared shelf schematics proposing product arrangements for retailers and provided labor to arrange or “reset” the retailers’ products in accordance with such schematics. In the process, the wholesaler often moved both its own products and those of its competitors. The Ninth Circuit upheld the suspension on appeal. In 1995, the Bureau created an exception to the tied-house rules to allow industry members to provide retailers with a recommended shelf plan or shelf schematic, but that exception did not allow them to provide additional services. In a 2016 ruling, TTB found that “some industry members are providing schematics as well as additional services that far exceed the exception.” It clarified that providing additional services or items of value, sometimes referred to as “category management” or “category captain” activities, could be the basis of a violation.

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145 See Stein Distributing v. ATF, 779 F.2d 1407, 1409 (9th Cir. 1986).
146 Id. at 1407.
147 See TTB Ruling 2016-1, The Shelf Plan and Shelf Schematic Exception to the ‘Tied House’ Prohibition, and Activities Outside Such Exception (Feb. 11, 2016). Some of the additional services listed include:
   (1) Assuming, in whole or in part, a retailer’s purchasing or pricing decisions, or shelf stocking decisions involving a competitor’s products;
   (2) Receiving and analyzing, on behalf of the retailer, confidential and/or proprietary competitor information;
   (3) Furnishing to the retailer items of value, including market data from third party vendors;
   (4) Providing follow-up services to monitor and revise the schematic where such activity involves an agent or representative of the industry member communicating (on behalf of the retailer) with the retailer’s stores, vendors, representatives, wholesalers, and suppliers concerning daily
Despite the 2016 ruling, commentators complain that category management practices remain common in the industry, suggesting that the ruling may not have a sufficient deterrent effect. One commentator described category management as a threat to interbrand competition: “Anheuser Busch or Miller Coors run the software and process that produces the store planograms (what the shelves will hold.)” and “ply the category managers with trips, event tickets, discounted product etc. to perpetuate their grip on the in-and-out flow of product.”\(^{148}\) Another commenter stated that “a retailer surrenders control of its shelf spacing and product selection decisions” under these arrangements and noted that “[t]he arrangements undermine the retailer’s independent judgement on what products to carry and put one or two (some systems involve a second-fiddle industry member known as a ‘validator’) industry members in substantial control of the retailer’s shelf space.”\(^{149}\)

Outside of alcohol, some have defended category management as efficiency promoting. However, like fees, they are also criticized for favoring large producers with the resources or experience to run a category captain scheme. While retailers might prefer the services of a category captain, the takeover of the decision of what products to carry and how to display them is at odds with a statute meant to foster retailer independence. Nonetheless, TTB has not brought category management or shelf schematic cases in recent years. Given that these arrangements may hamper competitors, reduce consumer choice, and lead to higher prices, a reconsideration of the 1995 exception, and additional enforcement focus on the provision of services in addition to shelf schematics, may be in order.

5.1.1.5. Tying Arrangements/Tie-In Sales

The Bureau has a history of investigating tying arrangements, such as an arrangement where a wholesaler requires a retailer to buy its undesired brands as a condition of buying its desired brands. The potential to foreclose opportunities for independent craft competitors through such arrangements is obvious. One commenter reports, for instance, that he has “often heard from retailers that they have no choice but to provide excessive shelf space for products that they can barely sell in order for the few major distributors to be willing to sell them the bottles that their customers really want.”\(^{150}\) Another example might involve a distillery requiring that a retailer buy its non-premium brands as a condition to gaining access to a highly-sought brand. This creates potential for foreclosure of opportunities for new entrants. A commenter said “[t]he other ‘unfairness’ in playing in the same arena as those with goliath capital is that they get all ‘rare’ and ‘in demand’ labels based on their total expenditure to that supplier.”\(^{151}\)

The Bureau currently regards tying as a violation of the Tied House prohibitions, and Fedway recognized that certain tying arrangements “plainly [threaten] retailer independence.”\(^{152}\)

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\(^{148}\) Comment #146.
\(^{149}\) Brewers Association, Comment #280.
\(^{150}\) Jay Hack, Esq., Comment #486.
\(^{151}\) Comment #368.
\(^{152}\) Fedway, 976 F.2d at 1422.
However, neither TTB, FTC, nor DOJ has brought recent actions in this area. As these arrangements may in some cases threaten competition and the goals of the statute, greater focus on these arrangements may be warranted.

5.1.2. Consignment Sales

The prohibition on consignment sales, as the title suggests, is a *per se* ban on selling alcohol on consignment—for example, arrangements under which retailers have no obligation to pay for a product until it is sold. The provision differs from the other FAA Act prohibitions on anticompetitive practices by not requiring “exclusion.” Given the statute’s general concern with the power of large producers, Congress was presumptively concerned that established market players would be in a better financial position to offer such favorable terms and could use consignment sales to make their products more appealing to retailers than those of less well-heeled sellers. The drafters of the FAA Act also worried large retailers may have “sufficient economic power to compel the sellers to deal with them on a consignment basis.” In addition, when the FAA Act was passed, consignment sales were seen as closely associated with retail price maintenance.

While the statute’s ban on consignment sales is clear, some commentators have raised questions about the Bureau’s enforcement discretion and policy in this area. While it is true that the Bureau has accepted offers in compromise from the major brewers on consignment sales, one comment questioned investigations of small wine wholesalers and small wineries for consignment sale violations where it was obvious that the industry member lacked market power. It urged TTB to “focus investigative resources on stopping competitively-relevant conduct.” The commenter asserted that “by focusing resources on insignificant industry members, TTB may have incrementally helped giant incumbent wine wholesalers and suppliers.” TTB investigated a number of small wineries and small wine wholesalers in 2017 and 2018 as part of an investigation involving a single wholesaler who was buying on consignment. Because the provision “shall not apply to transactions involving solely the bona fide return of merchandise for ordinary and usual commercial reasons arising after the merchandise has been sold,” it also

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154 A comment described direct-to-consumer subscription plans as a tying arrangement that should be prohibited, positing that consumers could be required to subscribe for access to certain products that are difficult to find. Comments #189, 368.
155 27 U.S.C. § 205(d). The consignment sale provision also differs from the other provisions in that retailers who purchase on consignment also violate the consignment sale provision. Because retailers do not have FAA Act permits, exercising that authority requires federal court action.
156 See, e.g., Wine and Spirits Wholesalers of America, Comment #254 (asserting that consignment sales can have a negative impact on small businesses, because “[i]f such transactions were allowed to occur, large entities would certainly have an advantage over small businesses who could not afford to carry out such sales tactics.”).
160 Brewers Association, Comment #280.
161 *Id*.
may be possible for more sophisticated market participants to structure the terms of sales to avoid the consignment sales prohibition while achieving similar economic substance.

Currently, outside of the FAA Act, neither antitrust law nor other regulation takes consignment sales as inherently anticompetitive in nature. It is possible that offering consignment sales may serve as an aid to smaller producers, by encouraging retailers to take a risk on an unknown product. The TTB cases involving consignment sales suggest that some small businesses are willing to deal on a consignment basis despite the FAA Act prohibition. All this suggests that the Bureau should carefully consider its enforcement policies in this area and give greater attention to the competitive impact of its enforcement.

5.1.3. Appropriations for Enhanced Education and Enforcement

Beginning in 2017, Congress provided TTB with $5 million of appropriations for enforcement of and education regarding the FAA Act’s trade practice provisions.163 TTB has used this funding principally on the exclusive outlet, tied house, commercial bribery, and consignment sales prohibitions. TTB was averaging only two such investigations each year before 2017. Since 2017, TTB has initiated approximately 80 of these investigations. It has resolved 44, resulting in 34 permit suspensions and 11 offers in compromise (OICs).164 Settlement agreements have ranged from $325,000 to $5,000,000, and suspensions have ranged from one to 15 days. TTB determines the length of suspension and the amount of the OIC based on the egregiousness and scope of the conduct at issue. TTB has resolved cases with both large and small industry members engaged in these activities. Of the 44 cases that TTB has resolved, 22 cases involved only wholesalers, 16 cases involved only suppliers, and 6 cases involved both wholesalers and suppliers. TTB’s investigations that led to the 44 resolved cases often involved more than one type of trade practice violation, whether or not all these violations were part of the ultimate resolutions of these cases. Specifically, 35 of those investigations involved consignment sale allegations,165 12 involved exclusive outlet allegations, and 12 involved tied-house allegations.166 The Brewers Association commented that Treasury should develop guidelines so that offers-in-compromise “reflect the size and market share of the violator” and suggested that large corporations can absorb current offer amounts as the cost of doing business.167 TTB has also used this special appropriation to increase its educational efforts.168

5.1.4. Impact of Trade Practice Provisions on Competition

In their entirety, the trade practices provisions addressing exclusionary or anticompetitive behavior create different “rules of the game” for the sale of alcohol in the United States, most obviously through the ban on slotting fees and other inducements in some circumstances. While it is hard to measure the effects, it is true, as some commentators point out, that the results may speak for themselves: the industry is vibrant, has made room for thousands of new competitors,

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163 E.g., Consolidated Appropriations Act 2021.
164 One case involved both a suspension and an OIC.
165 The majority of the investigations involving consignment sale allegations involved the same wholesaler who TTB alleged purchased products on consignment from wineries and other wholesalers.
166 Although exclusive outlet violations involve a requirement (27 U.S.C. § 205(a)) and tied house violations involve an inducement (27 U.S.C. § 205(b)), the evidence will often be sufficient to prove both violations.
167 Brewers Association, Comment #280.
and offers consumers a great variety of alcohol beverages, often made locally. This is somewhat unusual in the contemporary U.S. economy, in which many markets are dominated by a small number of national brands. One commenter posited a comparison to the soft drink industry:

Compare the soda aisle of a grocery store with the inventory of a liquor store. The typical soda aisle will have 20 feet of Coke or Pepsi products with perhaps 18 to 24 inches of a few craft soda products. In stark contrast, the typical liquor store will carry the products of scores of different breweries.169

Such comparisons suggest that FAA Act trade practice provisions facilitate competition, or at least competitors, and that the existing regulatory structure continues to have effect today. Further research into the “natural experiment” of alcohol versus other products would be welcome.

Many industry members have sought greater clarity with respect to TTB’s competition-related regulations. Several commented that their complexity created uncertainty among industry members and an advantage for large firms that can afford the legal assistance necessary to navigate their shoals. One commenter noted that TTB’s tied house regulations have not kept up with modern marketplace realities and consumer expectations. The commenter recommended that these regulations be updated to further clarify what inducements are unlawful and to refine the criteria for determining retailer independence, taking into account “(i) the value of procompetitive promotions, and (ii) the uniqueness of the alcohol industry which suggests that special oversight and regulation are required.”170

Other commentators argue that certain competition provisions are insufficiently sensitive to the size of the regulated entities and can create barriers for new or smaller entrants. A cider industry group, for example, commented that tied-house laws prevent small producers from “promoting their retail locations.”171 They urge “[a] more right-sized approach to tied-house laws [that] might make an exception for small producers to cross-promote their products with single retailers.”172

A different complaint supports the current competition regulations but views them as underenforced and insufficiently deterrent of the practices they condemn. For example, one commenter suggested that “offering spiffs [incentives used to drive sales] or backchannel deals to buy the business for control of the restaurant or wine shop major programs” is a practice “common amongst larger distributors.”173 Another offered the vignette:

Say a local brewery wants their product in a certain stadium or grocery chain. They’re most certainly met with, “Wow! Your product is spectacular and we’d

169 Wholesale Beer Association Executives, Comment #218; see also American Distilled Spirits Alliance, Comment #260 (“tied-house laws and commercial bribery prohibitions have prevented the use of ‘slotting fees’ in the alcohol beverage industry, whereby suppliers pay or give other things of value to retailers for favorable product placement on store shelves or in retailer advertising circulars or coupon books.”).
170 DISCUS, Comment #276.
171 American Cider Assoc., Comment #269.
172 Id.
173 W. Hoard, Comment #47.
One obvious gap in the FAA Act scheme is its lack of rules for retailers. Apart from the consignment sale provisions, the prohibitions do not apply, on their face, to retailers. When a retailer proposes or requires participation in a pay-to-play scheme in violation of the rules, the Bureau may only take enforcement action against the wholesalers or producers who participate, as opposed to taking action against the retailer. TTB, like ATF before it, has maintained consistently that it can take action against wholesalers or producers even if the activity is retailer-initiated, though such action may be viewed as focusing on the less culpable party. The problem is made worse by the fact that many retailers appear to have considerable market power today (e.g., national grocery and restaurant chains and large event venues, in contrast to the independent local saloon discussed in the legislative history). When retailers demand sufficiently large, up-front cash payments that competitors cannot easily match, those demands have the potential to raise rivals’ costs and effectively exclude them from the market.

Another challenge for enforcement lies in the complexity introduced by the Fedway court, its treatment of “exclusion,” and the 1995 regulations. Before the courts “raised questions concerning ATF’s traditional interpretation of the term ‘exclusion,’” there was relatively little uncertainty surrounding the activities subject to ATF enforcement, if at the cost of the potential chill of procompetitive conduct. Fedway, however, held that exclusion requires “something more” than ATF had required, and the corresponding enforcement actions have therefore been resource intensive. Given the resources required for post-Fedway cases, there is a risk that the Bureau will focus on easier cases instead of more complex cases against large industry members.

There are several ways in which these concerns may be addressed. To provide greater clarity, the Bureau has previously elaborated what it considers to be conduct that, by its nature, fulfills an element of a violation (for example, the payment of slotting fees). In any future rulemaking under the Act, the Bureau might consider adding to its categorical approach by

174 Triplehorn Brewing Co., Comment #38.
175 See TTB Ruling 2016-1, at 1 (“Sections 105(a) through (d) of the FAA Act (27 U.S.C. 205(a)–(d)) prohibit certain marketing practices, irrespective of whether they are offered by an industry member or requested by a retailer, that are deemed to cause unfair competition.”); Unfair Trade Practices Under the Federal Alcohol Administration Act, 60 Fed. Reg. 20402, 20405 (Apr. 26, 1995) (citing ATF Industry Circulars 75-20 and 76-15 for the proposition that a producer or wholesaler could violate the exclusive outlet provisions by accepting a retailer’s offer of exclusivity).
176 See, e.g., DISCUS, Comment #276, at 12 (“the market has radically changed [since the FAA Act’s passage] and retailers are more frequently in a greater position of control as to what a consumer is able to buy”).
179 976 F.2d at 1423.
180 Other than the consignment sale investigations noted in Section 5.1.2, TTB’s enforcement efforts under the competition-related trade practice provisions have generally focused on larger industry members. See, e.g., Accepted Offers in Compromise, available at https://www.ttb.gov/fo/administrative-cases#offers (publishing trade practice offers in compromise with Anheuser-Busch, LLC (2020), Heineken USA, Inc. (2019), Crown Imports, LLC (2019), RN Acquisitions, LLC & City Beverage-Markham, LLC (2021), Stern Beverage, Inc. (2019), Carisam-Samuel Meisel (2019), Robert “Chick” Fritz, Inc. (2021), Iowa Beverage Systems, Inc. (2021), Brewers Distributing Company (2019)).
further specifying practices that threaten retailer independence, particularly focusing on practices that result in exclusion, consistent with the request of some commenters for more certainty in this area. In this process, it might consider new practices that have arisen since 1995.

When it comes to enforcement discretion, the Bureau should reconsider bringing cases against smaller industry members whose conduct does not have obvious effects on competition. Conversely, where categorical rulemaking is inappropriate and where cases involve large and sophisticated industry members, TTB should seek collaboration and bring joint cases with other enforcement agencies, including the DOJ and FTC, relying on their combined and complementary authorities.

5.2. Other Treasury Regulation of Alcohol Beverages that Affects Competition

In addition to the provisions discussed above, other Treasury regulations also affect competition in the alcohol industry. These other regulations, administered by TTB, are codified in 27 C.F.R. parts 1 – 31. They cover a wide range of matters, ranging from labeling requirements (Parts 4, 5, and 7) to basic permit requirements (Part 1) to identifying American Viticultural Areas (Part 9) to defining classes and types of distilled spirits (Part 5) to mandating bottle sizes (Parts 4 and 5). These regulations are rooted in FAA Act authority, as well as the Internal Revenue Code of 1986 (IRC) and the Alcoholic Beverage Labeling Act of 1988 (ABLA).

The IRC, in addition to imposing a federal excise tax on distilled spirits, wine, and beer, authorizes regulation of the operations of domestic industry members to protect revenue. ABLA requires that a health warning statement appear on the labels of all containers of alcohol beverages manufactured, imported, or bottled for sale or distribution in the United States. ABLA applies to all beverages containing not less than one-half of one percent of alcohol by volume.

5.2.1. Treasury Alcohol Beverage Labeling Regulation

The FAA Act sets forth requirements for labeling wine, distilled spirits, and malt beverages. It authorizes the Treasury Secretary to issue regulations to prevent consumer deception, to provide the consumer with “adequate information” as to the identity and quality of the product, to prohibit false or misleading statements, and to provide information as to the alcohol content, net contents, and the manufacturer, bottler, or importer of the product. The provisions essentially are unchanged since 1935, except for ABLA’s mandated health warnings on alcohol labels and the Supreme Court’s invalidation of the FAA Act’s prohibition of alcohol content on beer labels as unconstitutional.

While labeling may not be thought to be directly related to competition, the compliance burden is large enough to affect the competitive position of firms. Deceptive labeling also undermines fair competition. Treasury policy, rooted in the FAA Act, is that alcohol beverage labeling must not only be truthful, it must contain sufficient information about the product for the consumer to make an informed choice. Furthermore, the health risks and social ills caused by

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181 See, e.g., DISCUS, Comment #276.
alcohol abuse played an important role in enactment of the FAA Act, which was intended to prevent the excesses that led to Prohibition.

Some alcohol beverages (such as wines under seven percent alcohol by volume and certain beverages that are taxable as beer but are not made from both malted barley and hops) are outside the scope of the FAA Act. In these cases, the FDA regulates labeling under the authority of the Federal Food, Drug, and Cosmetic Act.

5.2.1.1. Certificates of Label Approval

The FAA Act generally requires alcohol beverage labels to be approved in advance of distribution. TTB received 195,706 applications for label approval in fiscal year 2021.

Industry members complained that it takes too long for labels to be approved. Congress then provided TTB with dedicated funding to improve label processing times in recent years, and TTB has been able to significantly reduce average approval times from 27 days in FY 2016 to six days in FY 2021. Industry members also requested more flexibility to make minor changes without resubmission for approval. TTB has an extensive list of such allowable changes.

FDA’s food labeling regulations do not require pre-approval. Accordingly, there is no prior label approval requirement for alcohol beverages that are not subject to the FAA Act’s labeling requirements. Some comments submitted in response to Treasury’s 2021 request for information complained that TTB labeling decisions are either arbitrary or excessively strict, and that the labeling regulations do not protect consumers. Despite the costs and time needed for approvals, many in the industry support the mandatory preapproval of labels, because they believe it provides certainty or at least results in mitigated impact when there is a subsequent agency decision that a previously approved label does not comply with labeling regulations.

It may also be less costly for the government to review labels in advance than to review products in the marketplace and take enforcement action. On the other hand, the appropriate cost-benefit test is not cost to the government alone, but rather net national cost. An appropriate comparison is to the effectiveness of other labeling regimes that do not require pre-approval. Another approach, which would require legislative change, would be to offer but not require pre-approval. A fee could also be levied for the service.

5.2.1.2. Content Labeling

In response to its 2021 Request for Information to inform this report, Treasury received numerous comments about public health concerns associated with alcohol abuse, which stated

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185 The definition of a “beer” under the IRC differs from the definition of a “malt beverage” under the FAA Act in several significant respects, for instance. Compare 27 U.S.C. § 211 (a)(7) and 26 U.S.C. § 5052(a).

186 Wines under seven percent alcohol by volume, for example, do not fall within the definition of a “wine” in the FAA Act.


189 See, e.g., R Street, Comment #207 (“These rules, written broadly as they are, are ripe for over-enforcement, which in fact is exactly what has happened.”); Comment #377 (“Most of our challenges with Federal level regulation center on seemingly arbitrary labeling requirements which do nothing to advance the cause of getting truthful information into the hands of consumers and preventing ‘confusion.’”).

190 See, e.g., DISCUS, Comment #276, at 6.
that, “[r]egarding labeling, where Treasury has clear authority[,] consumers are ill-served by the lack of ingredient, calorie, or nutritional labeling on alcoholic beverages. We ask that regulations be updated to require more transparency of listed ingredients and the adoption of standard drink sizes to make it more clear to the public and consumers what is in each product.”191 We agree that ensuring consumers are informed about the nature of alcohol beverages promotes public health goals. It also fosters fair competition.

5.2.1.2.1. Ingredient Labeling

Treasury has considered ingredient labeling requirements since at least 1972, when the Center for Science in the Public Interest petitioned for it.192 These efforts ultimately led to several rounds of rulemaking and litigation. TTB’s predecessor bureau, ATF, published regulations requiring ingredient disclosures in 1980.193 The regulations required that labels of all alcohol beverages sold in the United States disclose either the essential ingredients and additives (except incidental additives) or an address where this information could be obtained. Under the latter option, the regulations required that the producer or other responsible party provide on request an ingredient list that complied with the labeling rules. Before the regulations went into effect, ATF rescinded them through notice and comment rulemaking.194 Challenged by a public interest group, a court invalidated the rescission, holding that ATF failed to adequately explain the reversal of the prior rule and placed undue weight on cost factors.195 ATF then started a new rulemaking, which ultimately successfully rescinded their 1980 labeling rule but required disclosure of the color additive FD&C Yellow No. 5 when used in alcohol beverages because of evidence that some consumers may have allergic reactions.196 TTB and its predecessor agency have followed a policy, reflected in a 1987 Memorandum of Understanding with FDA,197 whereby TTB will initiate rulemaking on the disclosure of specific ingredients upon a determination by FDA “that the presence of an ingredient in food products, including alcoholic beverages, poses a recognized public health problem. . .” In addition to Yellow No. 5, TTB regulations currently require mandatory disclosure of sulfites at 10 or more parts per million, aspartame, and the color additives cochineal extract and carmine.

5.2.1.2.2. Allergen Labeling

TTB initiated rulemaking on allergen labeling after enactment of the Food Allergen Labeling and Consumer Protection Act of 2004, which amended the Federal Food, Drug, and Cosmetic Act. In 2006, TTB published a notice of proposed rulemaking regarding the mandatory labeling of major food allergens used in the production of wines, distilled spirits, and malt beverages that are subject to the labeling requirements of the FAA Act.198 This proposal has not been finalized. TTB, however, also published an interim rule allowing the voluntary labeling of major food allergens on the labels of wines, distilled spirits, and malt

191 Community Anti-Drug Coalitions of America, Mass Comment #1.
beverages. Producers, bottlers, and importers of alcohol beverages may voluntarily declare the presence of milk, eggs, fish, Crustacean shellfish, tree nuts, wheat, peanuts, and soybeans, as well as ingredients that contain protein derived from these foods, in their products, but they are not required to do so. The interim regulations, however, set forth rules that are mandatory for how industry members must undertake such labeling, should they choose to do so.

5.2.1.2.3. Serving Facts Labeling

In 2007, TTB proposed mandatory “serving facts” labels for alcohol beverages. The serving facts label would include information about the number of servings per container and the size of the serving, as well as the number of calories, and the number of grams of carbohydrates, fat, and protein per serving. The proposed rule would also have expanded existing alcohol content requirements to include all malt beverages and wines, and would have allowed alcohol content statements, as a percentage of alcohol by volume, as well as in terms of fluid ounces of alcohol per serving, to appear as part of the serving facts statement. The rulemaking was not finalized, although in 2013 TTB announced that producers could include serving facts statements on labels on a voluntary basis while the Bureau continues to consider the rule.

Serving facts labeling could be an effective means of conveying information relevant to health concerns (for example, calorie content and more detail about alcohol content) to consumers. Complying with labeling requirements to disclose nutritional content may be more challenging for small businesses and new market entrants because of the potential need for product testing (e.g., for serving facts panels and allergen labeling). Some also object on aesthetic grounds to the presence of such labels. Small producers of all other food, however, generally must comply with the FDA labeling rules, although there are statutory exemptions from certain requirements for small businesses.

Although labeling can directly affect public health, mandatory serving facts, allergen, and ingredient labeling proposals, have not been implemented. Both that and the fact that FTC has seen the need to police deceptive practices in alcohol labeling indicate that FAA Act labeling regulations have not have fully addressed public health and competition concerns.

5.2.2. Treasury Regulations on Alcohol Industry Process and Operations

5.2.2.1. Standards of Fill

“Standards of fill” are TTB regulations that prescribe the container sizes allowed for wine and spirits (but not malt beverages) generally intended for consumer purchase. Treasury originally established standard bottle sizes to facilitate inspection and calculation of federal tax liabilities and prohibit consumer deception, but standards of fill are “no longer necessary to

200 See Notice No. 73, 72 Fed. Reg. 41860 (July 31, 2007).
202 See In re Phusion Projects, LLC et al., supra note 17.
204 See 48 Stat. 1020 (1934); IRC § 2871 (1939) (providing the Treasury Secretary with authority to regulate, among other things, the size of retail spirits bottles as “necessary to protect the revenue”); see also John E. O’Neill, Federal Activity in Alcoholic Beverage Control, L. & CONTEMP. PROBS. (Autumn 1940), pp. 570-99, Vol. 7, No. 4.
ensure accurate calculation of tax liabilities or to protect the revenue”205 and consumers presumably have ample information on bottle size from labeling and point of sale displays.

In July 2019, TTB proposed rulemaking eliminating container size regulations, except for a minimum bottle size (to ensure containers would be large enough to accommodate required labeling) and a maximum bottle size for distilled spirits (needed to maintain the distinction between bulk and bottled distilled spirits).206 TTB also sought comments on the alternatives of 1) maintaining the standards of fill requirements, but creating a system to expedite approval of new container sizes, and 2) maintaining the standards of fill requirements, but adding several requested sizes.207 After reviewing the comments, TTB adopted the second alternative in December 2020, maintaining the standards of fill requirements but adding new container sizes, three for wine and four for spirits.208

Container size requirements can be a barrier to innovation and competition, insofar as producers must conform their packaging to the Treasury-mandated sizes. The governments of other countries have noted that the standards of fill prevent some of their producers’ products from being sold in the United States.209 In 2019, the United States and Japan signed an exchange of letters on alcohol beverages, as part of the U.S.-Japan Trade Agreement.210 In these letters, and at the request of the Government of Japan, the United States agreed to consider the addition of several new container sizes for wine and spirits.211 Consequently, TTB plans future rulemaking to propose additional new standards of fill.212 Because commenters, noting the recent addition of newly approved container sizes, still call for additional sizes, future rulemaking should again consider eliminating the standards of fill requirements and specifically examine whether their potential impact on competition outweighs potential consumer confusion.

5.2.2.2. Standards of Identity/Statements of Composition

Pursuant to the FAA Act’s mandate that labels provide consumers with adequate information about the identity and quality of the product, and IRC § 5388, the TTB regulations in 27 CFR parts 4, 5, and 7 generally require the labeling of wine, distilled spirits, and malt beverages, respectively, with a class or type designation.213 In the case of wine and distilled

206 Id. at 85515.
207 Id.
208 Id. at 85519.
211 See id.
212 See Addition of New Standards of Fill for Wine and Distilled Spirits; Amendment of Distilled Spirits and Malt Beverage Net Contents Labeling Regulations, 85 Fed. Reg. 85514, 85519 (Dec. 29, 2020) (“TTB will conduct rulemaking to propose the addition of new standards of fill…”)
213 The legislative history of the FAA Act indicates that the purpose of law was to “provide such regulations, not laid down in statute, so as to be inflexible, but laid down under the guidance of Congress, under general principles, by a body which could change them as changes were found necessary. Those regulations were intended to insure that the purchaser should get what he thought he was getting, that representations both in labels and in advertising should be honest and straight-forward and truthful. They should not be confined, as the pure-food regulations have been confined, to prohibitions of falsity, but they should also provide for the information of the consumer, that he should
spirits, these classes and types have specific standards listed in the regulations. These are known as "standards of identity." For malt beverages, the TTB regulations refer to certain classes but do not provide specific standards of identity for those classes. Instead, the regulations provide that statements of class and type must "conform to the designation of the product as known to the trade."

The main purpose of standards of identity is to provide consumers with adequate information about the identity of the product. The legislative history of the FAA Act indicates that the purpose of the law was to "provide for the information of the consumer, that he should be told what was in the bottle, and all the important factors which were of interest to him about what was in the bottle."

Standards of identity may promote competition by allowing new entrants to compete with established brands by creating uniform rules that are consistently applied to all products. At the same time, they can hinder competition by limiting the marketing of innovative new products and requiring innovative products to be labeled in a way that may not meaningfully inform consumers. The standards of identity may be amended when necessary to reflect new products or evolving consumer and trade understanding of what a designation means.

TTB also engages in rulemaking to propose amendments to standards of identity to designate products that are distinctive products of foreign countries, where the new standard not only reflects consumer understanding of the product designation, but is also the subject of a trade agreement or exchange of letters between the United States and one or more other countries.

Alcohol products that do not fit within any established standard of identity generally require a statement of composition. If a wine or distilled spirit does not fall within any class set out in the regulations, and if a malt beverage is not known to the trade under a particular designation, the regulations require that a truthful and adequate statement of composition appear on the label as the statement of class and type. For these beverages, the statement of composition is intended to provide the consumer with adequate information about the identity of the product.

While the term “statement of composition” is not currently defined in the regulations, TTB’s general policy has been to require that such a statement identify the base products and added flavoring or coloring materials.

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214 For example, there are 12 different classes of distilled spirits set out in 27 C.F.R. § 5.22, such as whisky, rum, gin, and brandy. As used in § 5.22, the term “type” refers to a subcategory within a class of spirits. “Bourbon whisky” and “rye whisky” are types of whisky, and “vodka” is a type of neutral spirit.
215 The FDA “began establishing food standards of identity to promote honesty and fair dealing in the interest of consumers shortly after the FD&C Act was enacted in 1938. Standards of identity describe in detail what a food product must contain, how it must be proportioned, and sometimes how it must be manufactured. For example, products like ‘milk chocolate,’ ‘bread’ and even ‘ketchup’ all have standards of identity.” Statement of Claudine Kavanaugh, Director, Office of Nutrition and Food Labeling, FDA Center for Food Safety and Applied Nutrition (Feb. 20, 2020), available at https://www.fda.gov/news-events/fda-brief/fda-brief-fda-reopens-comment-period-related-general-principles-food-standards-identity.
TTB should consider rulemaking to ensure that standards of identity and statements of composition are flexible enough to accommodate innovative products. One approach may be to provide that only products that meet a standard may be labelled as such, but such products may be labelled with another name along with an appropriate statement of composition, at the option of the producer. This would reflect what often is TTB current practice. TTB should also ensure that standards of identity do not confer property rights in or limit the use of designations in a manner that limits new entrants or otherwise hinders competition.

5.2.2.5. Formula Requirements – Winemaking Practices

Domestic producers and importers of wine, distilled spirits, or malt beverages may be required to submit formula applications before applying for a certificate of label approval. TTB requires formula approval most commonly for products made with flavoring or coloring materials. In fiscal year 2021, TTB received 28,387 applications for formula approval.

A formula includes a complete list of the ingredients used to make the beverage and a step-by-step description of how it is made. In some cases, TTB also requires the submission of samples of the product for laboratory analysis. TTB uses the information found in the formula to classify the product for tax and labeling purposes; check that the product does not contain any ingredients prohibited by FDA regulations; determine if certain ingredients are used within prescribed limitations or if their use will impact labeling; and provide a suggested statement of composition for labeling purposes.

TTB has recently eliminated several formula requirements for distilled spirits, wine, and beer through TTB Rulings. Treasury believes that this helps small businesses and new entrants get their products to market faster.

TTB has been working on improving the turnaround time for formula approvals, and the Annual Report for FY 2020 shows that the average processing time for formulas went from 35 days in FY 2016 to nine days in FY 2020. Total formula submissions, however, increased more than 20 percent in FY 2020. TTB should ensure formula requirements apply only when necessary.

Domestic wines must be made in compliance with the production standards set forth in the Internal Revenue Code (IRC), 26 U.S.C. §§ 5381–5387, and in the regulations found in 27 CFR part 24, Subpart L, the “Storage, Treatment and Finishing of Wine.” Some of the production standards for “natural wine” relate back to IRC distinctions that were eliminated by tax simplification reforms that took effect in 1980. There are still important limitations on wines not defined as natural wine under the IRC, however. For example, the IRC has provisions on the withdrawal from customs custody of bulk natural wines without payment of tax for transfer to

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218 See TTB Rulings 2015-1, Ingredients and Processes Used in the Production of Beer Not Subject to Formula Requirements (Dec. 17, 2015); 2016-2, TTB Approves General-Use Formulas for Certain Agricultural Wines (Sept. 29, 2016); 2016-3, TTB Approves General-Use Formulas for Certain Distilled Spirits Produced Using Harmless Coloring, Flavoring, or Blending Materials (Sept. 29, 2016).
219 TTB Annual Report Fiscal Year 2020, supra note 189, at 17; see also Processing Times for Beverage Alcohol Formulas, https://www.ttb.gov/formulation/fonl-processing-times(average formula processing times (without laboratory samples) ranging from eight to nine days).
220 See TTB Annual Report Fiscal Year 2020, supra note 189, at 15.
bonded wine premises. There are also certification requirements that apply to imported natural wine, as defined in the IRC.

If a material or process is not specifically authorized in part 24, a winery may file an application with TTB to show that the proposed material or process is a cellar treatment consistent with good commercial practice.\(^{221}\) TTB maintains on its website a list of materials and processes that have been approved by TTB pending rulemaking on the issue. However, until the materials and processes have been incorporated into TTB regulations, some foreign countries do not accept them.

This affects the ability of U.S. wineries to market new products or products using advanced techniques or materials. TTB should finalize proposed updates to the wine treating regulations and should also consider alternative ways of expediting the process of approving new materials and processes into facilitate competition by U.S. wine producers in foreign markets. In the longer run, TTB and Congress also could consider action to eliminate requirements that are not necessary to protect the public or the revenue.

### 5.2.2.6. Permits: Federal Qualification Requirements

A federal permit is required before one may engage in the business of producing distilled spirits or wine.\(^{222}\) A federal Brewer’s Notice must be filed before brewing beer for sale.\(^{223}\) TTB evaluates prospective market entrants and their operations to check that they meet legal requirements, are likely to maintain compliant operations, and that their premises are adequate to protect the revenue.\(^{224}\)

Historically, TTB and its predecessors have required submission of extensive details, such as serial numbers of equipment and information on physical locks used to secure premises. Many of these requirements date back to an earlier time, when alcohol industry operations were even more strictly regulated and under the direct supervision of government agents.\(^{225}\) TTB’s permit simplification initiative seeks to ensure that TTB collects only information that is necessary. TTB has already eliminated requirements to upload source of funds documentation, documentation substantiating state registration of trade names, and, for brewers, proof of ownership (or a lease) for the brewery premises. TTB has initiated rulemaking to simplify the qualification requirements for distilled spirits plants (DSPs) and to speed TTB’s review process.\(^{226}\) One industry group commenter noted that “[l]ong wait times for initial DSP permits exist,” noting that holding a lease for the time prior to obtaining a permit and commencing operations creates a barrier to entry.\(^{227}\) TTB has proposed to address that concern by

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\(^{221}\) See 27 CFR § 24.250.  
\(^{224}\) See 27 U.S.C. § 204(a)(2); 26 U.S.C. § 5721(c) (statutory grounds to deny federal permit applications).  
\(^{227}\) American Craft Spirits Association (ACSA), Comment # 209. While ASCA mentioned wait times of six months, see ASCA Letter to the White House National Economic Council (Sept. 27, 2021), attachment to ACSA Comment, # 492, TTB’s current average processing time for original DSP applications is approximately two months. See https://www.ttb.gov/nrc/statistics-original-applications-to-operate.
modernizing its regulations; for example, by eliminating the requirement that serial numbers of 
stills, tanks, and condensers be listed on the permit application, and that applications could be 
submitted to TTB before equipment that has been ordered is physically received. TTB continues 
to work to streamline the qualification process and reduce the amount of information it collects 
to evaluate permit applicants and registrants for all commodities, making it easier for new 
businesses to enter the alcohol industry. At the same time, TTB has engaged in a multi-year 
effort to reduce the length of time it takes for an industry member to get a permit. As a result of 
these efforts, TTB has reduced permit approval times from an average of over 120 days in FY 
2016 to an average of 34 days in FY 2021 across permit types.

Congress could amend the FAA Act or the Internal Revenue Code to allow TTB to issue 
permits conditionally without prior review of an applicant’s qualifications. Congress also could 
amend the applicable statutory provisions to allow one permit to cover multiple types of 
operations. TTB should continue to work to streamline the qualification process and reduce the 
amount of information it collects to evaluate permit applicants and registrants, making it easier 
for new businesses to enter the alcohol industry.

5.2.2.7. Impact of Regulatory Provisions on Competition

Restrictions on bottle sizes, mandatory classification of beverages, and requiring review 
of premises to qualify for a permit to produce alcohol all raise costs for businesses and can 
hinder competition by acting as barriers to new entrants or burdening small businesses. As noted 
elier, the FAA Act was a response to the particular conditions immediately following 
Prohibition. The Supreme Court’s *Coors* decision, which invalidated on First Amendment 
grounds the FAA Act’s prohibition on including alcohol content on beer labels, observed that 
“the irrationality of th[e] unique and puzzling regulatory framework” surrounding alcohol 
labeling “ensured” a ban on alcohol content on beer labels would fail to achieve its aim, when 
“other provisions of the same Act directly undermine and counteract its effects.”228 The Court’s 
critique underscores the need to evaluate regulatory requirements to ensure they serve a useful 
purpose. Regulations often reflect a balance between consumer protection, including public 
health concerns, and costs to industry. In some instances, regulations may present significant 
barriers to entry for potential new industry members while costs to incumbent industry members 
may be negligible.

Another factor in how regulation affects the competitive landscape is the degree to which 
navigating the regulatory scheme requires resources and sophistication. Larger, well-resourced 
firms too often have an advantage when seeking regulatory decisions or presenting their cases, 
even if agencies take steps to ensure that all parties can present their cases to policymakers. 
Complex or ambiguous rules may mystify new entrants or smaller firms less able to navigate a 
regulatory maze. The clearer and simpler rules are, the easier it is for regulators apply rules 
evenly.

6. Taxation

6.1. Federal Excise Taxes

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but prohibited it for beer. *Id.* at 484.
The alcohol beverage sector is subject to federal, as well as state, excise taxes that affect the competitive landscape. Congress has imposed federal excise taxes on alcohol to raise revenue throughout United States history: in 1791 to help pay down the national debt; in 1813 to help pay for the War of 1812; in 1862 to help pay for the Civil War; and continuing up to and following Prohibition.\textsuperscript{229} Currently, the public generally regards alcohol excise taxes as a means of discouraging consumption. Federal excise taxes are imposed on producers and importers. They generally are passed along to the consumer in the form of increased prices.\textsuperscript{230} In 2020, federal taxes collected on beverage alcohol amounted to over $10.79 billion, $8.09 billion on domestic production, and $2.7 billion on imports.\textsuperscript{231}

<table>
<thead>
<tr>
<th>FY 2020 Alcohol Tax Collections (in Thousands)</th>
<th>Distilled Spirits</th>
<th>Wine</th>
<th>Beer</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Domestic</td>
<td>$4,597,524</td>
<td>$728,475</td>
<td>$2,768,139</td>
<td>$8,094,138</td>
</tr>
<tr>
<td>Imported</td>
<td>$1,763,061</td>
<td>$325,552</td>
<td>$603,357</td>
<td>$2,695,970</td>
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<tr>
<td>Total</td>
<td>$6,360,585</td>
<td>$1,058,027</td>
<td>$3,371,496</td>
<td>$10,790,108</td>
</tr>
</tbody>
</table>

Source for domestic tax collection figures on this report is a TTB database that records tax collection data by tax return period end date. Imported tax data is from U.S. Customs Border Protection reports.

In 1990, Congress justified increasing alcohol excise tax rates on the grounds that higher consumer prices could benefit the public by reducing societal costs of alcohol consumption.\textsuperscript{232} In 2017, however, Congress passed the Craft Beverage Modernization Act (CBMA) provisions, which cut excise tax rates on distilled spirits, wine, and beer for both domestic producers and importers. Alcohol excise taxes are not indexed to inflation, leading to lower real revenue and more affordable alcohol over time.\textsuperscript{233}

Distilled spirits, wine, and beer are subject to different tax rates and tax bases under the Internal Revenue Code. In general, beer and wine are taxed less per unit of alcohol than spirits. For example, as the Congressional Budget Office noted in December 2020, setting aside the CBMA tax breaks, the IRC imposes a spirits tax rate of $13.50 per proof gallon, translating to


\textsuperscript{232} In addition to raising revenue, the House Committee on the Budget provided the following rationale for federal excise tax increases:

In deciding to increase alcoholic beverage excise taxes, the committee took note of numerous studies demonstrating that the direct and indirect social costs from alcohol consumption are far greater than the revenues generated from Government spending for highway safety, public health, and welfare are all increased by alcohol consumption. Moreover, alcohol consumption imposes substantial costs on society from accidents, disease, and reduced worker performance. Thus, increasing the alcoholic beverage excise taxes could help to place some of the costs of alcohol consumption on alcohol users and could reduce alcohol consumption among teenagers.


\textsuperscript{233} See, e.g., Nelson & Moran, supra note 231.
about 21 cents per ounce of pure alcohol. The CBO, comparing what are now the unreduced rates for beer wines and spirits, found the federal excise tax on beer is equivalent to about ten cents per ounce of pure alcohol, and federal excise tax on wine is about six cents per ounce of pure alcohol.234 These figures are based on beer and wine that contain 4.5 and 14 percent alcohol by volume, respectively. Note that wine and beer are taxed on total volume while distilled spirits are taxed on alcohol content.235 A neutral malt base used for a hard seltzer base could be brewed at as high as 18 percent ABV,236 translating to a federal excise tax of about 2.5 cents per ounce of alcohol, before any CBMA tax breaks. Consumers may not distinguish among such flavored beverages derived from wine, spirits, or malt base, but the tax implications could be very different.

Another feature of the complex alcohol tax regime is “cover-over,” which applies to certain products, including alcohol beverages, produced in Puerto Rico and the U.S. Virgin Islands and then brought into the rest of the United States. Most of the tax collected on these products is provided, or covered over, to the governments of Puerto Rico and the U.S. Virgin Islands, as is the excise tax on rum that is imported from outside the United States.237 In practice, much of these funds are used to benefit the producers, whose products in effect face lower tax rates than other domestically produced or imported products.238 Also, because tax for some shipments can be collected at the CBMA’s low distilled spirits rate ($2.70) and covered over at the maximum cover-over rate ($13.25), the amount of cover-over for a shipment can exceed the tax actually paid. This means that some products (typically some rums and products that contain rum) may have a competitive tax advantage over other distilled spirit products.

Several commenters noted that the disparity in the tax rates among beer, wine, and spirits creates a competitive disadvantage for distilled spirits-based drinks when compared to beer or wine-based drinks with similar alcohol content. The Distilled Spirits Council of the United States noted a trend toward “clear and growing cross elasticity of demand among beer, wine, and spirits,” disadvantages distilled spirits.239 The American Craft Spirits Association (ASCA) also recommended “parity in tax rates between the three beverage alcohol categories (beer, spirits, and wine).”240 The American Cider Association (ACA) commented that “All sparkling wine taxes limit innovation and competition for the cider, mead and wine segments as beer, malt

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234 Congressional Budget Office, Increase All Taxes on Alcoholic Beverages to $16 per Proof Gallon and Index for Inflation, Options for Reducing the Deficit: 2021-2030 (Dec. 9, 2020), available at https://www.cbo.gov/budget-options/56868 (and noting that “Other factors affect how alcoholic beverages are taxed. Specific provisions of tax law can lower the effective tax rate on small quantities of beer and nonsparkling wine for certain small producers. Additionally, small volumes of beer and wine that are produced for personal or family use are exempt from taxation.”); 26 U.S.C. §§ 5001 (distilled spirits), 5041 (wine), 5051 (beer).

235 In the UK, the Chancellor of the Exchequer announced a proposal to simplify alcohol excise taxes, assessing based on alcohol by volume across commodities. See, e.g., Judith Evans & Alice Hancock, UK drinks trade welcomes alcohol duty overhaul in Budget, FIN. TIMES (Oct. 28, 2021).


239 DISCUS, Comment #276.

240 ASCA, Comment #209.
beverages and hard seltzer are not subject to such ‘bubble taxes,’ as they are often referred to.”

Wineries also commented that their products competed against beer in the marketplace but were subject to a much higher tax burden than beer due to the “bubble tax.” Distillers commented that spirits-based ready-to-drink products were subject to three times the tax burden of similar malt-based products.

The alcohol excise tax regime provides a competitive tax advantage to small domestic producers. For example, small brewers have for many years received a preferential tax rate. From 1991 until 2018, the tax rate for beer was $7.00 per barrel on up to 60,000 barrels for those who brew under two million barrels per year, while larger brewers paid the full rate of $18.00 per barrel. Beginning in 2018, the CBMA further reduced the effective tax rate for small brewers to $3.50 per barrel.

This competitive tax advantage for small producers, however, was mitigated by other features of the legislation. The tax breaks are not limited to small or “craft” producers. Current law increases alcohol excise tax rates with the amount produced by each producer, imposing complex limitations on the lower rates for parties related by ownership or contract, and extends the lower rates to qualifying imports. In fact, large domestic and foreign producers enjoy most of the CBMA excise tax cut. The table below illustrates this with data for domestic taxable withdrawals (excise tax on alcohol is typically due when the product is removed or withdrawn from the bonded production facility) in 2018. The vast majority of domestic industry members do not remove enough taxpaid alcohol to receive the maximum CBMA tax benefit for a particular commodity. For domestic distilled spirits and beer, less than a third of the CBMA benefits taken that year (i.e., the difference between what would have been paid at the full tax rate compared to what was paid with CBMA tax benefits) went to businesses with production levels below the threshold to receive the lowest CBMA rate for all of their

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241 ACA, Comment #268.
242 Superstition Meadery, Comment #438 (recommending that Congress “remove the tax on [c]arbonated wine so that modern wineries can compete fairly”); MobCraft Beer, Comment # 436 (“A company can create hard seltzer by fermenting glucose or cane sugar which is taxed and classified as beer at $0.11 per gallon, yet when we use sugar derived from the agave plant we are taxed 2100% higher [as carbonated wine]!”). The ACA also explained that, because the “tax rate for small beer producers is lower than cider and wine and the production level threshold for benefiting from such a tax rate is much higher in beer,” the “result is a tax-incentive for mid-sized beverage producers to make beer instead of cider or wine.” DISCUS, Comment #276.
243 Federal Distilling, Comment #52 (“charging spirits based RTD’s 3X the tax of malt-based is simply putting spirits at a large arbitrary competitive disadvantage simply because the tax laws have not kept up with the innovation in the industry.”); see also Comment #316 (“To level the playing field with respect to hard seltzers and other ready-to-drink cocktail products, we believe that excise tax rate on all hard seltzers and ready to drink cocktails should be unified based upon the alcohol by volume percentage of the product.”). The ACA also found it “puzzling that a product made from fermenting pure fruit juice is taxed as wine at a much higher rate than a product made from fermenting liquid cane sugar which is taxed as beer.” ACA, Comment #268.
244 See, e.g., Report to Congress on Administration of Craft Beverage Modernization Act Refund Claims for Imported Alcohol (June 2021), 11, available at https://www.ttb.gov/images/pdfs/treasury-cbma-import-claims-report-june-2021.pdf (“For domestic distilled spirits and beer, less than a third of the CBMA benefits taken that year … went to businesses with production levels below the threshold to receive the lowest CBMA rate for all of their removals [taxable withdrawals]”). Adam Looney, How to close the loopholes in the Craft Beverage Modernization Act (Sept. 6, 2019), available at https://www.brookings.edu/blog/up-front/2019/09/06/how-to-close-the-loopholes-in-the-craft-beverage-modernization-act/ (“the vast majority of [CBMA’s] tax cuts go to large distillery corporations and foreign spirits importers, ballooning the cost of the bill, undercutting the ability of truly small businesses to compete, and threatening public health”).

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taxable withdrawals. This disparity is even starker for wine, with less than seven percent of all CBMA wine benefits received by wineries with production levels below 150,000 wine gallons, the maximum number of gallons for which a winery could have taken the largest wine tax credit prior to CBMA. This disparity is expected to further increase as larger industry members react to the newly permanent provisions by changing their business models to avoid paying the full tax rate.

<table>
<thead>
<tr>
<th>Size of Firm by Amount of Production</th>
<th>Number of Firms</th>
<th>Percentage of Total Firms</th>
<th>Removal Quantity for These Firms*</th>
<th>Tax Benefit Share</th>
</tr>
</thead>
<tbody>
<tr>
<td>Distilled Spirits</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&lt;100k Proof Gallons</td>
<td>1,455</td>
<td>94.2%</td>
<td>6,193,002</td>
<td>33.0%</td>
</tr>
<tr>
<td>100k-22.23m Proof Gallons</td>
<td>85</td>
<td>5.5%</td>
<td>335,200,730</td>
<td>57.6%</td>
</tr>
<tr>
<td>&gt;22.23m Proof Gallons</td>
<td>4</td>
<td>0.3%</td>
<td>150,325,439</td>
<td>9.2%</td>
</tr>
<tr>
<td>Beer</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&lt;60k Barrels</td>
<td>4,928</td>
<td>98.6%</td>
<td>9,658,609</td>
<td>30.7%</td>
</tr>
<tr>
<td>60k-2m Barrels</td>
<td>63</td>
<td>4.1%</td>
<td>14,677,362</td>
<td>31.8%</td>
</tr>
<tr>
<td>&gt;2m Barrels</td>
<td>5</td>
<td>0.3%</td>
<td>141,753,242</td>
<td>37.5%</td>
</tr>
<tr>
<td>Wine</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&lt;150k Wine Gallons</td>
<td>5,247</td>
<td>95.8%</td>
<td>51,524,029</td>
<td>6.9%</td>
</tr>
<tr>
<td>150k-250k Wine Gallons</td>
<td>71</td>
<td>4.6%</td>
<td>13,910,242</td>
<td>10.6%</td>
</tr>
<tr>
<td>&gt;250k Wine Gallons</td>
<td>161</td>
<td>10.4%</td>
<td>673,808,345</td>
<td>82.5%</td>
</tr>
</tbody>
</table>

*Data reflect domestic taxable withdrawals in 2018

For example, in addition to the $3.50 rate for the first 60,000 barrels produced and removed by small domestic brewers, all brewers receive a reduced rate of $16.00 per barrel on the first 6 million barrels that are produced and removed in the year. Even the largest brewers (over 2,000,000 barrels/year) could claim the intermediate rate of $16.00 on their first 6,000,000 barrels/year. Similar tiered rates apply to wine and distilled spirits. In 2020, Congress made the CBMA rates permanent, thus reducing the overall effective rates on all three commodities.

In calendar year 2020, 6,292 of 6,406 breweries produced 60,000 or fewer barrels of beer but accounted for less than five percent of total barrels produced.

While the bulk of tax benefits from CBMA accrue to the largest producers, the lowest rates for the smallest producers mitigate barriers to entry that may have resulted from the full rates.\(^{245}\) The complexity of the CBMA rates means that enforcement is difficult, increasing the possibility that non-compliant producers evade taxes resulting in a competitive advantage over compliant producers. Competitive advantages could be provided for small businesses with less

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\(^{245}\) The American Cider Association noted another anomaly, writing that as a result of CBMA, “Small cideries making less than 30,000 gallons a year are taxed at more than twice the rate than other wine producers making less than 30,000 gallons a year—16.4 cents vs 7 cents a gallon, respectively. As mid-size wine and cider producers making between 30,000 gallons and 130,000 gallons a year have tax parity at 17 cents a gallon, this is an odd artifact of the Craft Beverage Modernization and Tax Reform Act. We believe it was an error, but it creates an unfair tax disparity for the smallest cideries.” Comment #268.
complexity by providing tax relief for small producers through an income tax credit instead of the complicated tiered rate structure applicable to all producers.

The availability of reduced rates for foreign alcohol also undermines the competitive advantage of the low rates for domestic producers. One industry observer noted “[f]oreign producers from all over the world have never seen an incentive program like this before.”246 Another tax advantage for imported products is the availability of “double drawback” that ultimately results in imported products consumed in the United States not having to pay excise tax while domestic product consumed in the United States is fully taxed. (An exportation of alcohol can result in refund of both the tax on the exported product and also a refund of the tax on a comparable imported product.) Treasury promulgated regulations to prohibit this loophole,247 but industry successfully challenged the regulations in court.248 Double drawback provides a significant competitive advantage to foreign product that is not available for home grown products.

6.2. Tax-Related Reporting Requirements

Tax-related reporting is a burden on industry, though one necessary to protect revenue. One commenter proposed simplified recordkeeping, writing:

Get rid of production, storage, and processing paperwork and just ask how many gallons did you sell and tax that. We waste a good part of a day every month making sure our reporting is accurate and a lot of time inter-month entering data into software that costs $5000 a year just so we can accurately pay our taxes.249

TTB is working to reduce the burden on industry while improving tax administration by changing the information collected on tax returns and operational reports substantially to meet modern needs. TTB’s current tax returns and operational reports require taxpayers to submit information that TTB does not routinely use for tax administration purposes. At the same time, current regulations and forms fail to require taxpayers to submit certain items of information that are needed to confirm they are paying the correct rates under the Craft Beverage Modernization Act provisions. The goal is to design new forms that would combine the excise tax return and the operational reports for each commodity. Although Congress has reduced the tax on alcohol recently, the taxation scheme has become more complex. This necessarily presents burden to taxpayers. Reforms could include simplification that is revenue neutral for domestic taxpayers. Providing reductions equivalent to the current excise scheme (focused on small producers) through an income tax credit, suggested above, would permit that kind of simplification.

6.3. State Alcohol Taxes

In addition to federal taxes, all states tax alcohol in some fashion. According to the Urban Institute, state and local governments collected $7.5 billion in alcohol taxes in 2018, 0.2 percent of general revenue, in addition to $10.1 billion from government-owned liquor stores.250

249 Charleston Distilling Co., Comment #17.
Rates vary considerably across states, and comparison is difficult given different taxing schemes. Some jurisdictions, for example, levy a special, higher sales tax on alcohol, in addition to a per-gallon excise tax.251 At least one state levies a property tax on aging whiskey.252 Profit taking by control states can have the effect of taxation. The Distilled Spirits Council of the United States developed a methodology for comparing state tax burdens on spirits by imputing an excise tax rate to control state sales.253 They determined that Washington, Oregon, Virginia, Alabama, and Utah tax spirits the most, while New Hampshire and Wyoming set prices so low in their state stores that they are comparable to selling without any state tax.254 Numerous commenters for this report said the complex differences in state tax regimes were a barrier to growth and competition. State and local taxes likely affect competition in the beer, wine, and spirits sectors, and also sales in bordering jurisdictions, but are beyond the scope of this report.

7. Public Health

Several commenters admonished the Treasury Department for overlooking the impact on public health in its request for comments on the state of competition in the wine, beer, and spirits markets. These comments are well taken: that omission does not reflect Treasury policy with regard to the impact of alcohol consumption on public health, nor the intent of Congress to ensure that alcohol labels enable consumers to make informed choices.

In addition to Treasury’s FAA Act mandate to require labeling that “will provide the consumer with adequate information as to the identity and quality of the products,”255 the FTC, as noted earlier, has taken action to quell misleading labeling for public health reasons.256

Numerous public health interests commented on the lack of ingredient, allergen, or calorie labeling required for alcohol beverages. As discussed in section 4.4.6.2 above, TTB has proposed rules requiring “serving facts” panels, which would include alcohol, calorie, and other basic content,257 but that proposal has not been finalized. The proposed regulations also specified serving sizes. As noted above, TTB has provided for voluntary use of serving facts statements on labels and in advertisements on a voluntary basis,258 and published an interim rule

251 See id. (providing the example of the District of Columbia, which “levies both per gallon taxes on beer ($0.09), wine ($0.30), and liquor ($1.50), which are built into the retail price of alcohol, and a 10.25 percent alcohol sales tax on the final purchase price”).
256 See, e.g., In re Phusion Projects, LLC et al., supra note 17.
allowing the voluntary labeling of major food allergens,\textsuperscript{259} and a notice of proposed rulemaking regarding the mandatory labeling of major food allergens.\textsuperscript{260}

Some public health groups commented that “attacks on ‘tied house’ laws and the removal of restrictions on marketing practices between the tiers have led to aggressive sales tactics, which in turn promote heavy consumption and harm.” They advocate “shoring up the three-tier system.”\textsuperscript{261} The point is well-taken, though the relationship between the FAA Act’s competition provisions and public health is not entirely straightforward. It is true that, strictly enforced, they ban certain promotional activities (for example, producers giving retailers certain high-priced materials), and also favor smaller firms without extensive marketing campaigns. On the one hand, those may be but a fraction of the total promotional effort. In addition the tied-house rules, enforced strictly, can weaken monopolies and lower prices, which, all else being equal, increases consumption. This, however, seems an indirect and inefficient approach of limited efficacy. Public health officials also expressed concern that “state legislatures are currently, or on the verge of, codifying measures that extend alcohol availability during the pandemic, such as home delivery, [and] takeout alcohol, and expanded outdoor dining.”\textsuperscript{262} Finally, health officials commented that “concentration in the producer and wholesaler tiers should be examined more closely, as it leads to oligopoly profit-taking and outsized political power for these giant players” and “the size of the big players gives them an outsized voice in national and state policy-making bodies: as of 2017, alcohol companies reported 303 lobbyists in Washington D.C. and spent nearly $12 million on state-level lobbying.”\textsuperscript{263}

Lobbying is a feature of our political system and particularly so for closely regulated industries, and regulatory capture is always a concern in government oversight of such industries. It is, of course, beneficial to establish networks to promote the free flow of information between government and industry members; however, it is critical—particularly in the enforcement and rulemaking arenas—that the appropriate “arm’s length” nature of the regulator/industry relationship be maintained. The nature of the regulatory scheme can play a role in maintaining that necessary separation, and the impartiality and objectivity of regulatory officials. Regimes with clear rules that facilitate compliance are to be preferred to ambiguous standards which officials are pressed to implement to the advantage of the regulated parties.\textsuperscript{264}

\textsuperscript{259} Major Food Allergen Labeling for Wines, Distilled Spirits, and Malt Beverages, 71 Fed. Reg. 42260 (July 26, 2006).

\textsuperscript{260} Major Food Allergen Labeling for Wines, Distilled Spirits and Malt Beverages, 71 Fed. Reg. 42329 (July 26, 2006).

\textsuperscript{261} Hawai‘i Alcohol Policy Alliance, Mass Comment #2.

\textsuperscript{262} See Federal Trade Commission, Possible Anticompetitive Barriers to E-Commerce: Wine, (July 2003), at 3, available at https://www.ftc.gov/sites/default/files/documents/reports/possible-anticompetitive-barriers-e-commerce-wine/finereport2_0.pdf (reporting few or no problems with sales to minors in states allowing direct shipment, while identifying less restrictive alternatives than direct sale bans to prevent such sales).

\textsuperscript{263} See, e.g., Iowa Alliance of Coalitions for Change, Comment #167.

8. Conclusions and Recommendations

Public Health

Public health and the social costs associated with alcohol consumption are fundamental concerns in both regulation and taxation of beverage alcohol. Regulation of labeling and advertising are the federal alcohol regulatory authorities that most directly affect public health. **TTB should revive or initiate rulemaking proposing ingredient labeling and mandatory information on alcohol content, nutritional content, and appropriate serving sizes.**

Horizontal Consolidation

Despite the entry of many new producers in recent years, a small number of large firms dominate production, especially in beer markets. Distribution has experienced consolidation. The comments indicate that many feel that this consolidation has led to large producers having the market power to restrict competition from smaller firms. This raises the question of whether the size of the larger firms inhibits competition and, if so, how best to address the issue. Neither state three-tier mandates nor the FAA Act, which focus on vertical arrangements, directly address horizontal arrangements. **We encourage the Justice Department and the Federal Trade Commission, who have consulted on this report, to continue their antitrust scrutiny of the alcohol markets, including by:**

- examining their approach to horizontal consolidation as to producers and distributors and evaluating the effectiveness of their remedies in the alcohol markets;
- the DOJ considering the effects on distribution stemming from the acquisition of craft brewers by major brewers;
- the DOJ and the FTC applying particular skepticism to claims of efficiencies, and particular attention to concerns relating to coordination, in assessing mergers and in considering revisions to merger guidelines;
- the DOJ, contingent on resources and working with the FTC as appropriate, considering conducting a retrospective on the pricing, innovation, and distribution impacts from craft acquisitions by major brewers; and
- the DOJ and the FTC, as part of assessing revisions to merger guidelines, considering guidance as to markets that are already highly concentrated.

State Regulation

The intent behind both the three-tier system and several of the federal trade practices prohibitions was to separate the production, distribution, and retail functions to prevent monopolistic control through vertical integration. That approach appears consistent with the current thinking on preventing monopolistic control, particularly in regulated industries. But the addition of state franchise laws, post-and-hold laws, and other state restrictions constrain the ability of new entrants to expand and find new markets.

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265 Martenet, *supra*.
266 OECD, *supra*. 
The intersection of the 21st Amendment and the Commerce, Contract, and Equal Protection Clauses leaves the alcohol market subject to both state and federal oversight, each with its own focus. Even though the three-tier system is not a federal creation, many consumers, small businesses, and new entrants submitted comments criticizing the three-tier system. Commenters were also critical of restrictive state franchise laws and restrictions on direct-to-consumer shipping. States might explore changes in these areas to eliminate anticompetitive effects and to bolster competition. For example, state legislatures might consider if the benefits of the three-tier system outweigh its costs to competition and study markets without a three-tier system. Similarly, states might explore amending their franchise laws and consider revisiting post-and-hold regulations, which have been struck down in some states as preempted by the Sherman Act.267 State officials should evaluate the direct-to-consumer distribution model, both in terms of the distribution opportunities it presents for small producers and the comparative risks it may present of making alcohol more readily available to underage drinkers. Additionally, the FTC and the Antitrust Division should continue their antitrust scrutiny of the alcohol markets, both as to consolidation and as to conduct, and continue to analyze how state regulations affect competition in the alcohol markets. The FTC and DOJ should also engage with state actors on these laws, including by submitting letters in response to state legislative requests for technical assistance.

**FAA Act Trade Practice Enforcement**

As described above, TTB has had an active enforcement docket in recent years with respect to the FAA Act’s competition provisions. Numerous commenters suggested, however, that the rules are underenforced and in some cases fail to capture exclusionary behavior. Others note the burden involved in complying with the FAA Act. These matters can be attributed in part to ambiguity in the statutory requirement of proof of exclusion, particularly as interpreted by the courts. TTB should consider rulemaking to update its trade practice regulations.

Among other things the Bureau should, to the extent possible in light of D.C. Circuit precedent, adopt easily understood rules of conduct that promote open and fair competition. This can be accomplished through three measures. The first is expanding and sharpening the categorical identification of practices that violate the trade practice rules, and in such course address practices that result in exclusion. The Bureau might also specifically strengthen the rule on category management to improve deterrence.

At the same time, the Bureau should limit the unintended negative effects on competition of categorical rules, especially on harmless practices, as well as enforcement actions against entities without discernable market power. It can do so in two ways. The first is by updating its regulations with an eye to giving a green light to practices that are essentially harmless and inherently procompetitive as it already does for matters such the holding of tastings or the provision of whimsical handles for beer taps. In addition, the Bureau should continue to exercise enforcement discretion to avoid bringing cases that target entities lacking discernable market power.

The Bureau should, as a matter of enforcement policy, focus its efforts against large entities presumed to have market power, such as the larger brewers, distributors, and similar

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actors. In bringing such cases, which may be complex, it should collaborate with states, as is current practice, but also with the DOJ and the FTC to the extent they have similar concerns.

Overall, the FAA Act’s competition provisions take a distinct approach than the antitrust laws. Congress established “rules of the game” intended to ensure that networks, both wholesale and retail, should remain open and available to all competitors (in some ways resembling a common carriage or public callings approach of general availability). It seems contrary to Congressional intent to completely harmonize the substantive content of the FAA Act and the antitrust laws. It is true that some of the original justifications for the law, such as combating criminal alcohol bootleggers, are no longer public priorities, and also true that some entities, like retailers, have grown in ways not contemplated in the 1930s. But other then-extant public concerns, such as combatting the power of the Trusts, concerns over retailer independence, and the promotion of lower prices, retain their relevance despite the passage of nearly a century. We leave it to Congress to determine whether reform of the FAA Act trade practice provisions is necessary.

Unjustified Regulatory burden

Several instances of restrictive Treasury regulations that are not justified by public health, revenue, or competition goals have been noted. TTB should consider amending those regulations or recommending statutory changes where necessary. TTB could continue to explore streamlining certificates of label approval under the existing statutory requirement, if doing so would reduce barriers to entry without reducing consumer protections, including public health concerns. Congress could consider a statutory change to remove the pre-approval requirement from the FAA Act. TTB should consider rulemaking on standards of identity that would allow flexibility and innovation within the existing regulatory framework to recognize changes in industry practices and consumer expectations. These might help small businesses and new entrants get their products to market faster.

Regulatory Independence

A final consideration in evaluating federal regulatory schemes is the extent that regulators are separated from the influence of industry. Federal regulation of the alcohol industry, whether looked at from the perspective of competition or public health policy, may be more effective if the regulators are charged with enforcing clear rules rather than licensing, approval, and permitting schemes. The former puts the agency in an oversight role where officials are motivated to enforce the rules (to protect consumers, competition, and public health), while the latter involves arrangements unique to the industry that are more susceptible to being used to suppress competition and to giving an advantage to large, more deep-pocketed entities. Any future rulemaking or legislation should be written with an eye to clarity and simplicity, not only to promote compliance and competition, but also to ensure a level playing field for small businesses and new entrants.