
CRAFTING A BETTER INDUSTRY: ADDRESSING PROBLEMS OF
REGULATION IN THE CRAFT BEER INDUSTRY

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Beginning in the late 1970s, the story of craft beer has been one of impressive economic growth and success. In 1978, there were fewer than 100 breweries in the United States; today, there are more than 7,000. Yet, as the craft beer industry matures, growth in the industry has begun to slow, competition has increased, and consolidation has become more prevalent. Lurking in the background is pressure from Big Beer companies, who have greater resources and who are increasingly acquiring craft breweries to shore up their own positions within the market, and beer distributors, who are often aligned with or controlled by Big Beer companies to the detriment of craft brewers. In response to these unfavorable conditions, this Note proposes three changes to the legal landscape, all of which are designed with lobbying influences in mind: 1) expanded self-distribution laws or the creation of state-run distribution centers that would operate alongside private distributors; 2) additional legislation in the form of a “retailer’s law,” which would correct power imbalances in the brewer-distributor relationship; and 3) further changes to federal excise taxation on beer.

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I. INTRODUCTION

According to the Brewers Association, a not-for-profit trade association of American brewers, the craft beer industry contributed \$76.2 billion to the U.S. economy in 2017.¹ This reflects a relatively substantial increase from 2016, when the economic contribution totaled \$67.8 billion—already a 21.7% increase from 2014 (the last time the biennial study was conducted).² To generate this impressive income, the industry employed 500,000 full-time equivalent employees; more than 135,000 of these employees were employed directly by breweries and brewpubs.³ Between 2008 and 2016, the number of workers in breweries grew by 120%.⁴

While these numbers might suggest that the craft beer industry is currently experiencing a boom, sales have begun to stagnate in recent years.⁵ Stasis in the industry may be due to external factors, such as an increase in the consumption of wine and spirits,⁶ or internal factors, such as an oversaturation of the market.⁷ On the other hand, some industry insiders believe that this data reflects the stabilization of a maturing industry, one that could not have maintained the same growth rates going forward.⁸ Lending further credence to this argument is the

1. *Economic Impact*, BREWERS ASS'N, <https://www.brewersassociation.org/statistics/economic-impact-data/> (last visited May 11, 2019). This number reflects income from all levels of the three-tiered system of breweries, wholesalers, and retailers, as well as non-beer products sold at brewpubs and taprooms such as food and merchandise. *Id.*

2. Jim Vorel, *Craft Beer Had a \$67.8 Billion Economic Impact in 2016*, PASTE MAG. (Sept. 26, 2017, 11:39 AM), <https://www.pastemagazine.com/articles/2017/09/craft-beer-had-a-678-billion-economic-impact-in-20.html>.

3. *Economic Impact*, *supra* note 1.

4. Derek Thompson, *Craft Beer Is the Strangest, Happiest Economic Story in America*, ATLANTIC (Jan. 19, 2018), <https://www.theatlantic.com/business/archive/2018/01/craft-beer-industry/550850/>.

5. See *Craft Beer in America Goes Flat*, ECONOMIST (July 8, 2017), <https://www.economist.com/news/business/21724864-slowing-beer-market-and-might-ab-inbev-has-small-brewers-worried-craft-beer-america>.

6. *Id.*

7. See Brad Tuttle, *Too Much of a Good Thing? Concerns About Craft-Beer Saturation*, TIME (July 4, 2013), <http://business.time.com/2013/07/04/too-much-of-a-good-thing-concerns-about-craft-beer-saturation/>.

8. John Kell, *How Craft Beer's Popularity Is Hurting Craft Beer*, FORTUNE (Mar. 28, 2017), <http://fortune.com/2017/03/28/craft-beer-sales-fall/>.

fact that market consolidation has become abundant, a phenomenon that often occurs after market maturation.⁹

Consolidation is not necessarily negative; studies have shown that there can be both benefits and detriments from market consolidation.¹⁰ Market consolidation in the beer industry, and in general, increased during Ronald Reagan's tenure as the Department of Justice ("DOJ") relaxed enforcement of antitrust laws.¹¹ The beer industry has seen a plethora of consolidation: over the last thirty years, forty-eight major breweries have consolidated to become two giant breweries today.¹²

Jim Koch, the founder of Samuel Adams, has pointed out that market consolidation has not been benign in the beer industry.¹³ Discussing the merger of Molson Coors and SABMiller (then "MillerCoors"), and the merger of Anheuser-Busch and InBev (then "AB InBev"), Koch noted:

The immediate result was a 6 percent increase in beer prices and the end of a decades-long decline in real beer prices. Drinkers began paying almost \$2 billion a year more for their beer. At least 5,000 Americans lost their jobs, and cost cutting followed, saving the new owners an estimated \$2 billion.¹⁴

Eight years later, the DOJ further approved the merger of SABMiller and AB InBev (on the condition that SABMiller sell off its stake in MillerCoors),¹⁵ now the largest brewery in the world.¹⁶

The harmful effects of recent consolidation in the industry have been twofold. First, brewery consolidation has indirectly led to consolidation in a related industry: wholesalers.¹⁷ Wholesalers, also known as distributors, are legally

9. For a timeline of craft beer company acquisitions, see *The Definitive Timeline of Craft Beer Acquisitions*, VINEPAIR, <https://vinepair.com/craft-beer-sales/> (last visited May 13, 2019). See also *Industry Lifecycle*, INVESTOPEDIA, <https://www.investopedia.com/terms/i/industry-lifecycle.asp> (last visited May 13, 2019).

10. Daniel Thomas, *Are Big Mergers Bad for Consumers?*, BBC NEWS (Oct. 30, 2015), <http://www.bbc.com/news/business-34666150>.

11. Thompson, *supra* note 4.

12. *Id.*

13. Jim Koch, *Is It Last Call for Craft Beer?*, N.Y. TIMES (Apr. 7, 2017), <https://www.nytimes.com/2017/04/07/opinion/is-it-last-call-for-craft-beer.html>.

14. *Id.*

15. The 58% stake was sold back to Molson Coors for \$12 billion. Lisa Brown, *A-B InBev Finalizes \$100B Billion Acquisition of SABMiller, Creating World's Largest Beer Company*, CHI. TRIB. (Oct. 11, 2016, 7:22 AM), <http://www.chicagotribune.com/business/ct-megabrew-ab-inbev-sabmiller-merger-20161010-story.html>. Because MillerCoors is now owned by Molson Coors, operating as the company's United States division, any non-historical references below are used interchangeably.

16. See Tara Nurin, *DOJ Approves Largest Beer Merger in Global History, with Significant Conditions*, FORBES (July 20, 2016, 3:34 PM), <https://www.forbes.com/sites/taranurin/2016/07/20/doj-approves-largest-beer-merger-in-global-history/#49dc27e413df>. For an *ex ante* discussion of the merger, see Andre Barlow, *I Drink Too Many: Why Consumers Will Lose with Beer Merger*, LAW360 (Nov. 12, 2015, 5:21 PM), <https://www.law360.com/articles/726137/1-drink-too-many-why-consumers-will-lose-with-beer-merger>.

17. Koch, *supra* note 13 ("This brewer's duopoly has led to a second consolidation: wholesalers, the crucial intermediaries who distribute our beer to retailers. In 1980, there were 4,600 wholesalers in the country, and most markets had four or five competing wholesalers. Today, fewer than 3,000 remain, and in most local markets over 90 percent of the beers is controlled by distributors for these same two companies—one of which is dependent on AB InBev for most of its volume, and the other on Miller Coors.")

mandated middlemen between producers and retailers of beer.¹⁸ Under the existing three-tiered structure of distribution, distributors—who are often aligned with “Big Beer” companies like Molson Coors and AB InBev—have the final say as to which beers are placed with retailers; as a result, the products of Big Beer companies are more likely to appear in bars, restaurants, and liquor stores.¹⁹ This has an overall anticompetitive effect and allows Big Beer companies to raise their prices and increase their own margins at the expense of smaller breweries.²⁰

Acquisitions by Big Beer companies are not always on such a grand scale. For example, AB InBev, in response to the impressive growth in the craft beer market, has been steadily purchasing craft breweries and adding them to its beer portfolio. Some of these brands include: Goose Island Brewing, Kona Brewing (through AB InBev’s 32% stake in the Craft Brew Alliance), Blue Point Brewing Company, Elysian Brewing, Breckenridge Brewing, Wicked Weed Brewing, and others.²¹ Likewise, Molson Coors has purchased its own set of craft breweries, including Blue Moon, Leinenkugel, Terrapin, Hop Valley, and Revolver Brewing.²² Interestingly, the rationale that breweries provide for their decision to sell is quite telling about the state of the market: partnership provides them with greater distribution opportunities, as well as greater resources.²³

Many craft brewers have been calling on consumers to boycott these brands, arguing that they are attempts by Big Beer companies to benefit from the current market power of craft beer.²⁴ Importantly, the Brewers Association has defined a “craft brewer” as “small and independent brewers” whose beer is “generally made with traditional ingredients.”²⁵ To fit these criteria, the brewery must

18. Marc Sorini, *Understanding the Three-Tier System: Its Impacts on U.S. Craft Beer and You*, CRAFTBEER.COM (Mar. 6, 2017), <https://www.craftbeer.com/craft-beer-muses/three-tier-system-impacts-craft-beer>.

19. *Id.*

20. See Travis Hoium, *How Big Beer Companies Exert Their Dominance*, MOTLEY FOOL (Feb. 5, 2017, 8:14 AM), <https://www.fool.com/investing/2017/02/05/how-big-beer-companies-exert-their-dominance.aspx>.

21. Kate Taylor, *Craft Brewers Are Calling for the Boycott of These 14 ‘Imposter’ Beer Brands*, BUS. INSIDER (May 25, 2017, 10:37 AM), <http://www.businessinsider.com/craft-brewers-boycott-brands-acquired-by-anheuser-busch-2017-5/#1-goose-island-1>.

22. John Kell, *MillerCoors Inks Third Craft Brewer Deal This Summer*, FORTUNE (Aug. 11, 2016), <http://fortune.com/2016/08/11/millercoors-craft-brewer-deal/>. These breweries are held under a separate unit called Tenth and Blake. *Id.*

23. Kate Taylor, *People Are Furious That This Craft Brewer ‘Sold Out’ to Anheuser-Busch—Here’s Why the Founders Say They’re Wrong*, BUS. INSIDER (May 3, 2017, 5:03 PM), <http://www.businessinsider.com/wicked-weed-founders-take-on-sell-out-criticism-2017-5>.

24. Taylor, *Craft Brewers Are Calling*, *supra* note 21. As part of these efforts, craft breweries have introduced a seal that started appearing on bottles and cans beginning in 2017. More than 4,000 craft breweries had adopted the seal at the time this Note was written. *About the Independent Craft Brewer Seal*, BREWERS ASS’N, <https://www.brewersassociation.org/business-tools/marketing-advertising/independent-craft-brewer-seal/> (last visited May 13, 2019). The seal is intended to “certif[y] that the beer came from one of the nation’s independently owned and small-scale breweries and signal[] that these upstarts are fighting back against the corporations trying to co-opt their authenticity and craftiness.” Ellis Jones & Daina Cheyenne Harvey, *Fed Up with Big Beer’s Incursion, Independent Craft Breweries Push Back*, CNBC (Feb. 3, 2018, 3:23 PM), <https://www.cnbc.com/2018/02/03/fed-up-with-big-beers-incursion-independent-craft-breweries-push-back.html>.

25. *Craft Brewer Defined*, BREWERS ASS’N, <https://www.brewersassociation.org/statistics/craft-brewer-defined/> (last visited May 13, 2019).

produce less than 6 million barrels per year and have less than 25% of its ownership or control in the hands of an alcohol industry member that is not a craft brewer.²⁶ By adding craft beers to their beer portfolio, Big Beer companies are able to capitalize on craft beer's success while concealing the fact that many of these breweries are no longer "craft."²⁷

In order to alleviate problems presented by harmful market consolidation and the modern three-tiered system of distribution, changes are necessary. Part II of this Note will discuss the history of the three-tiered system of alcohol distribution, the history of franchise laws and distributor lobbying efforts to keep franchise laws on the books, and the current system of excise taxation on beer. Part III will analyze existing state distribution laws, existing state franchise law protections, rationales behind excise taxation on beer, and will conclude by exploring alternative systems of excise taxation abroad. Finally, Part IV presents three recommendations: 1) expanding self-distribution laws or, alternatively, exploring a hybrid system with both state-run and private distribution methods; 2) adopting a "retailer's law," designed to allow consumers and retailers to influence product placement and to respond to beer franchise laws; and 3) further amending federal excise taxes on beer, with the intent to specifically lower tax rates on craft and other smaller brewers.

II. BACKGROUND

Long before the formation of the United States, beer was a part of the nation's history. When the *Mayflower* set sail in 1620, among the provisions the Pilgrims chose to transport was a quantity of beer, which was superior to water on long voyages because of the preservative property of hops.²⁸ The decision to land in Plymouth Harbor itself was motivated in part by a lack of beer (from various storms along the way, as well as general consumption).²⁹ From then on, greater quantities of beer were shipped to the colonies, and colonists quickly learned to brew their own beer with the resources of the fertile land that they had found.³⁰

Centuries later, on January 16, 1920, American citizens frantically flocked to liquor stores.³¹ Beginning on January 17, 1920, the only alcoholic beverages that Americans would be able to drink—Prohibition did not make the consumption of alcohol illegal, just the manufacture or sale³²—would be the ones that

26. *Id.* There is a separate requirement that a brewery be a "Brewer," which is not as relevant for purposes of this Note. *Id.*

27. For a recent discussion of Big Beer benefiting from the craft beer image, see Rich Duprey, *Is Craft Brew Alliance the Craft Brewer to Watch?*, MOTLEY FOOL (Aug. 20, 2018, 8:10 AM), <https://www.fool.com/investing/2018/08/20/is-craft-brew-alliance-the-craft-brewer-to-watch.aspx>.

28. DANE HUCKELBRIDGE, *THE UNITED STATES OF BEER: A FREEWHEELING HISTORY OF THE ALL-AMERICAN DRINK* 33 (2016).

29. *Id.* at 33–34.

30. *Id.* at 36.

31. DANIEL OKRENT, *LAST CALL: THE RISE AND FALL OF PROHIBITION* 1–2 (2010).

32. Evan Andrews, *10 Things You Should Know About Prohibition*, HISTORY (Jan. 16, 2015), <http://www.history.com/news/10-things-you-should-know-about-prohibition>.

they had in their home the day before.³³ While Prohibition would not turn out the way that its proponents might have imagined, its lasting consequences are reflected in the modern day laws governing the distribution of alcohol.

To understand the need for the changes presented in Part IV, Part II of this Note will examine the Prohibition amendment and the periods preceding its enactment and following its repeal. Prohibition, which was mired in corruption and criminal enterprise, had a great influence on how legislators responded to the regulation of alcohol. This Part also discusses the rise of beer franchise laws in the 1970s, which govern the relationship between brewers and distributors, and expands on these laws' importance through an examination of lobbying efforts by distributors. Finally, an overview of the current system of excise taxation is provided.

A. *Prohibition & the History of Three-Tiered Distribution*

For a nation that was founded on individual liberty, adopting a constitutional amendment that would eliminate the freedom to choose whether or not to partake in alcohol consumption would appear to be completely contrary to that principle. Although Prohibition ultimately failed, the legacy that it left behind has controlled the way in which alcohol is regulated today, for better or worse. Many of the legislative outcomes reflect moral judgments about alcohol that existed prior to and following Prohibition.

1. *Pre-Prohibition*

Prohibition—the period of thirteen years following the ratification of the Eighteenth Amendment—may seem alien in today's social environment, but the movement behind the amendment grew out of very real social concerns. In 1830, almost 100 years prior to the Prohibition amendment, consumption of alcohol in America was at its greatest.³⁴ In the century preceding Prohibition, it was perceived that high levels of consumption were arguably one of the most substantial causes of a myriad of social issues such as crime, spousal abuse, reckless spending, declining public health, and unemployment.³⁵ It was largely in response to these harms, as well as a general belief in the decline of public morals, that the temperance movement began to grow.³⁶

Long before a constitutional amendment was contemplated, temperance groups first began to emerge in the 1820s.³⁷ Groups such as the Washingtonians,

33. OKRENT, *supra* note 31, at 1.

34. *Prohibition: A Nation of Drunkards* (PBS television broadcast Oct. 2, 2011) [hereinafter *A Nation of Drunkards*] (“By 1830, the average American over fifteen years of age drank the equivalent of eighty-eight bottles of whiskey every year, three times as much as their 21st-century descendants drink. Americans spent more money on alcohol each year than the total expenditures of the Federal Government.”).

35. *Id.*

36. *Id.*

37. Dominic Sandbrook, *How Prohibition Backfired and Gave America an Era of Gangsters and Speakeasies*, GUARDIAN (Aug. 25, 2012, 7:05 PM), <https://www.theguardian.com/film/2012/aug/26/lawless-prohibition-gangsters-speakeasies>.

which was founded in the 1840s in Baltimore, were created with the hope of reforming fellow alcoholics through the sharing of stories and mutual support (much like a modern Alcoholics Anonymous group).³⁸ Many temperance groups, such as the Woman's Christian Temperance Union, which was founded much later in 1873, were run by women; for many women, this was their first experience in politics.³⁹ Membership in a temperance organization was often a foundation for later involvement in women's suffrage organizations.⁴⁰

The temperance movement began as a movement of moderation, rather than outright prohibition, though it quickly grew to a policy of total abstinence.⁴¹ Suddenly, after a decades-long period of incredible growth, temperance faltered in the 1860s when the country was ravaged by the Civil War.⁴² In desperate need for revenue, the Federal Government turned to alcohol taxation in order to pay its debts and fund the army.⁴³ To do so, liquor retailers were charged a \$20 licensing fee and manufacturers were taxed \$0.20 per gallon of distilled spirits and \$1 for every keg of beer.⁴⁴ In the years that followed, a full one-third of the federal budget was funded by the taxes on alcohol.⁴⁵

Following the Civil War, immigration skyrocketed, bringing with it the return of the temperance movement—this time, pressing for the outright prohibition of alcohol.⁴⁶ Prohibition had been attempted before, though on a much smaller scale.⁴⁷ On June 2, 1851, Maine became the first state to pass a law banning the sale of alcohol.⁴⁸ The mayor of Portland, Maine and founder of the Maine Temperance Society, Neal Dow, pushed for passage of the law, which would ban the manufacture and sale of alcohol with a few exceptions for medicinal, mechanical, or manufacturing purposes.⁴⁹

The “Maine Law,” as it became commonly known, did not lead to temperance, but instead, quite presciently forced citizens to find other ways to acquire alcohol.⁵⁰ On June 2, 1855, four years after the passage of the law, roughly 3,000 citizens circled Portland's City Hall and attempted to force their way in to haul

38. *A Nation of Drunkards*, *supra* note 34.

39. *Id.*

40. See Kathryn Kish Sklar, *Temperance & Suffrage*, PBS, <https://www.pbs.org/kenburns/not-for-ourselves-alone/temperance-suffrage> (last visited May 13, 2019); see also *A Nation of Drunkards*, *supra* note 34 (“For the next fifty years, temperance, and a far more radical cause, women's suffrage, would be inextricably linked.”) (discussing the creation of the first women's temperance society).

41. *A Nation of Drunkards*, *supra* note 34.

42. *Id.*

43. *Id.*

44. *Id.*

45. OKRENT, *supra* note 31, at 54–55.

46. *A Nation of Drunkards*, *supra* note 34.

47. Kat Eschner, *Why Was Maine the First State to Try Prohibition?*, SMITHSONIAN.COM (June 2, 2017), <https://www.smithsonianmag.com/smart-news/maine-first-state-try-prohibition-180963503/>.

48. *Id.*

49. Madeline Bilis, *Throwback Thursday: Maine Becomes the First State to Outlaw Alcohol*, BOS. MAG. (June 2, 2016, 8:00 AM), <http://www.bostonmagazine.com/news/2016/06/02/maine-alcohol-history/>.

50. *Id.*

off the alcohol that was rumored to be stored within.⁵¹ The riots ended with the death of one man and the injury of several others.⁵²

Despite the lessons to be learned from the Maine Law, the Anti-Saloon League (“ASL”), founded in Ohio in 1893, and others greatly increased the efforts of the temperance movement by focusing on politicians and political power.⁵³ By electing anti-alcohol politicians—even those who themselves made the personal choice to drink—the ASL was able to mobilize the American public.⁵⁴ In 1913, the ASL helped to pass the Sixteenth Amendment, which would allow the Federal Government to levy an income tax against citizens, thereby ending the influence that alcohol had on federal revenues.⁵⁵ Then, in 1917, with the help of World War I and anti-German propaganda,⁵⁶ the ASL successfully called for a temporary ban on the sale of grains to brewers and distillers; within months, the number of breweries in the United States had been halved.⁵⁷ Riding the success of these efforts, the Eighteenth Amendment was passed, with the condition that seven years would be allowed for ratification.⁵⁸ On January 16, 1919, the thirty-sixth state ratified the amendment, and Prohibition became the law of the land.⁵⁹

2. *Prohibition*

Mere minutes after Prohibition went into effect, masked gunmen in Chicago robbed two freight cars full of whiskey, four casks of grain alcohol were stolen from a warehouse, and a truck loaded with bourbon was hijacked.⁶⁰ Though the ills of alcohol were allegedly over, new problems were just over the horizon. While some citizens respected the new law and gave up alcohol,⁶¹ many others rejected Prohibition from the start.⁶² Over the thirteen years that followed, America would be wracked by crime and corruption, from bribery to gang wars, with much of the crime being perpetrated by otherwise law-abiding citizens.⁶³

51. *Id.*

52. *Id.*

53. *A Nation of Drunkards*, *supra* note 34.

54. *Id.*

55. OKRENT, *supra* note 31, at 58.

56. One “dry” politician, John Strange, was quoted as saying, “We have German enemies across the water. We have German enemies in this country too. And the worst of all our German enemies, the most treacherous, the most menacing, are Pabst, Schlitz, Blatz, and Miller.” *Id.* at 100.

57. *A Nation of Drunkards*, *supra* note 34.

58. *Id.*

59. OKRENT, *supra* note 31, at 105–06.

60. *A Nation of Drunkards*, *supra* note 34.

61. *Prohibition: A Nation of Scofflaws* (PBS television broadcast Oct. 2, 2011) [hereinafter *A Nation of Scofflaws*] (“Alcohol consumption went down by at least a third, alcohol-related deaths fell. So did arrests for public drunkenness.”).

62. *Id.*

63. *Id.*

In 1923, Federal District Attorneys were spending 44% of their time on Prohibition-related cases, most of which were petty violations.⁶⁴ The agency responsible for enforcement, the Prohibition Bureau, was understaffed, underfunded, and rife with corruption.⁶⁵ The DOJ, under the Harding Administration, was filled with heavy drinkers that did not care for the law, who would sell pardons, paroles, and protection to the bootleggers who produced and sold illegal alcohol.⁶⁶ Despite the best intentions of Prohibition's proponents, the amendment did more to damage citizens' perceptions of the law than change their perspectives on alcohol.

By the late 1920s, it had become clear that Prohibition was not functioning in the way that many Americans thought it would. On February 14, 1929, Al Capone gunned down members of an opposing gang in what would later be termed the "St. Valentine's Day Massacre."⁶⁷ Later that year, the stock market crashed, beginning the Great Depression, which accelerated the support for repeal.⁶⁸ When the economy crashed, income tax revenues fell with it, once again instilling the need for the Federal Government to collect tax revenue on the sale of alcohol.⁶⁹ In addition, public support for repeal was centered on a belief that a revival of the alcohol industry would bring back much-needed jobs at a time when unemployment was skyrocketing.⁷⁰ On December 5, 1933, the Twenty-First Amendment was ratified after being submitted to state conventions only nine months before.⁷¹

3. *Post-Prohibition*

In the wake of Prohibition and the repeal of the Eighteenth Amendment by the Twenty-First Amendment, regulation of alcohol was left to the individual states.⁷² During the time of resulting regulatory uncertainty, John D. Rockefeller, Jr., a well-known teetotaler,⁷³ funded a study aimed at providing guidance to the states and removing the criminal element that had plagued the production and

64. OKRENT, *supra* note 31, at 255.

65. *A Nation of Scofflaws*, *supra* note 61.

66. *Id.*

67. *Prohibition: A Nation of Hypocrites* (PBS television broadcast Oct. 2, 2011) [hereinafter *A Nation of Hypocrites*]. Capone was never directly linked to the murders but is largely considered to have been the cause. *Id.*

68. OKRENT, *supra* note 31, at 328.

69. *Id.*

70. *Id.*

71. *A Nation of Hypocrites*, *supra* note 67.

72. See U.S. CONST. amend. XXI; see also U.S. CONST. amend. XVIII.

73. Merriam-Webster defines "teetotalism" as "the principle or practice of complete abstinence from alcoholic drinks." *Definition of Teetotalism*, MERRIAM-WEBSTER, <https://www.merriam-webster.com/dictionary/teetotalism> (last visited May 13, 2019).

distribution of alcohol prior to and during Prohibition.⁷⁴ That study, titled *Toward Liquor Control*, recommended a state-controlled monopoly on the retail of alcoholic beverages, or alternatively, a licensure system.⁷⁵

Following the study, a minority of states chose a state-run monopoly, while the remaining states chose to implement a licensing system.⁷⁶ The latter was to be implemented by a state licensing board consisting, somewhat naively, of a “politically independent” board.⁷⁷ The board would have permanent tenure and would be responsible for regulations such as the locations where liquor could be sold, the classification of alcohol by strength, off and on-premises sales, advertising, and certain payment plans and structures like I.O.U.s and “bargain days.”⁷⁸

Interestingly, *Toward Liquor Control* makes no mention of a three-tiered system. This system, now the predominant system used by the states, came into being later, presumably in conjunction with “tied house” laws.⁷⁹ The recommendations made in *Toward Liquor Control* were largely in response to pre-Prohibition establishments known as tied houses,⁸⁰ saloons that were economically tied to breweries through mutual ownership.⁸¹ By buying saloons, brewers were able to ensure that their beers would be the exclusive product sold at whatever price the brewery chose.⁸² While anticompetitive pricing was only one harm associated with tied houses, they had also become associated with a number of other vices.⁸³ With an eye towards curbing the immoral behaviors of both breweries

74. Andrew D’Aversa, Comment, *Brewing Better Law: Two Proposals to Encourage Innovation in America’s Craft Beer Industry*, 165 U. PA. L. REV. 1465, 1473–74 (2017).

75. RAYMOND B. FOSDICK & ALBERT L. SCOTT, *TOWARD LIQUOR CONTROL* 35 (1933) (“Apart from prohibition, which attempts to meet these problems by bold statutory abolition, there are two main classifications of government control: the license method and the public monopoly method.”).

76. D’Aversa, *supra* note 74, at 1474–75.

77. FOSDICK & SCOTT, *supra* note 75, at 41–42.

78. *Id.* at 41–52.

79. Sorini, *supra* note 18.

80. FOSDICK & SCOTT, *supra* note 75, at 43 (“‘Tied houses,’ that is, establishments under contract to sell exclusively the product of one manufacturer, were, in many cases, responsible for the bad name of the saloon. The ‘tied house’ system had all the vices of absentee ownership. The manufacturer knew nothing and cared nothing about the community. All he wanted was increased sales. He saw none of the abuses, and as a non-resident he was beyond local social influence.”).

81. *Bottoms Up: Wisconsin’s Historic Bars and Breweries* (Wisconsin Public Television broadcast Nov. 12, 2012).

82. *Id.*; see also *Neel v. Tex. Liquor Control Bd.*, 259 S.W.2d 312, 316 (Tex. Civ. App. 1953) (“We need not dwell upon the evils of the ‘tied house.’ It is obvious that one result of such control could be the creation of a monopoly for certain brands of liquors as well as dictating prices.”); *A Nation of Drunkards*, *supra* note 34 (“By agreeing to sell just one brand of beer, almost anyone could go into the saloon business. The brewery paid for his license, provided the pool table and artwork, the bar and barstools, even the spittoons—everything needed to keep its beer flowing.”).

83. See Benjamin Grubb, Note, *Exorcising the Ghosts of the Past: An Exploration of Alcoholic Beverage Regulation in Oklahoma*, 37 OKLA. CITY U. L. REV. 289, 298 (2012) (“After tied-house arrangements gained a foothold, they quickly spiraled out of control, incubating several social ills associated with alcohol consumption, including prostitution, gambling, and general moral corruption. To effectively market the products of their principals, saloons offered free lunches and goods (such as glassware), stayed open for all hours of the day and night, and engaged in price wars with competitors. These practices made alcoholic beverages ubiquitous, and the role of the saloon within the community became more sinister.”).

and their customers, the first federal-tied house law was enacted on August 29, 1935.⁸⁴ The law remains on the books today, largely unchanged.⁸⁵

Even after Prohibition ended, states were slow to change. Mississippi held onto Prohibition until 1966.⁸⁶ In other jurisdictions, Prohibition still exists in the form of “dry” counties.⁸⁷ In 2002, sixteen states repealed laws banning the sale of alcohol on Sundays.⁸⁸ Other states have laws that place caps on alcohol content or provide specific locations in which alcohol can be sold.⁸⁹ While these decisions are squarely within the sphere granted to states by the Twenty-First Amendment, they showcase a rigidity and strict adherence to traditional views on alcohol consumption that has continued in the regulation of alcohol today. Inconsistent regulations today reflect a clear disagreement between states as to how regulation should occur. Much like the Prohibition amendment, which arose and died in a conflict between competing concerns of social control and individual choice, differing views on the role of alcohol in society have led to the inefficient and ineffective system of regulation in place today.

B. Beer Franchise Laws & Distributor Lobbying

Beginning in the 1970s, franchise laws were a response to an abundance of distributors and a very low number of breweries.⁹⁰ In the late 1940s, the five largest breweries had a 19% market share; by 2001, their share was 87.2%.⁹¹ These laws provide a number of protections for distributors, who had historically run the risk of investing in large amounts of equipment, advertising materials, and storage space, only to be dropped by the brewery for another distributor.⁹² With bargaining power lying solely with brewers, distributors lobbied for greater contractual protections, which they found in the establishment of beer franchise laws.⁹³

The first beer franchise law—which was technically not exclusive to beer, but also covered other alcoholic beverages—was enacted in Massachusetts in 1971.⁹⁴ Over the next two decades, nearly every state would follow in enacting

84. Pub. L. No. 74-401, 49 Stat. 977 (1935).

85. 27 U.S.C. § 205(b) (2018).

86. *The Remnants of Prohibition*, PROHIBITION: AN INTERACTIVE HISTORY, <http://prohibition.themobmuseum.org/the-history/the-end-of-prohibition/the-remnants-of-prohibition/> (last visited May 13, 2019).

87. *Id.*

88. *Id.*

89. *Id.*

90. Steve Hindy, *Free Craft Beer!*, N.Y. TIMES (Mar. 29, 2014), <https://www.nytimes.com/2014/03/30/opinion/sunday/free-craft-beer.html>.

91. Andrew Tamayo, Comment, *What's Brewing in the Old North State: An Analysis of the Beer Distribution Laws Regulating North Carolina's Craft Breweries*, 88 N.C. L. REV. 2198, 2212 (2010).

92. Stephan Michaels, *Beer and Loathing on the Distribution Trail*, ALL ABOUT BEER MAG. (Sept. 1, 2009), <http://allaboutbeer.com/article/beer-and-loathing-on-the-distribution-trail/>.

93. *Id.*

94. MASS. GEN. LAWS ch. 138, § 25E (1971).

similar franchise laws.⁹⁵ Two states, Alaska and Hawaii, as well as the District of Columbia, remain in minority and do not have beer franchise laws at all.⁹⁶ These laws vary from state to state, with the variation having increased over time, but typically they grant considerable leverage to distributors in their relationships with breweries.⁹⁷

Today, with consolidation playing an increasing role in the distribution market, the top two beer distributors control around 10% of the market.⁹⁸ The number of distributors has fallen, while the number of breweries is on the rise.⁹⁹ The National Beer Wholesalers Association,¹⁰⁰ a trade association made up of 3,300 distributors across the United States, has divisions in every state that aggressively lobby to maintain the status quo.¹⁰¹ The benevolent goals recited in the association's mission statement,¹⁰² while not without merit, may not provide the whole picture—distributors have an economic incentive to lobby against self-distribution, to protect the three-tier system, and to uphold beer franchise laws, which grant them powerful contractual protections.¹⁰³

Examples of the effects of these lobbying efforts are abundant. In early 2015, Rhinegeist, a brewery in Cincinnati, Ohio, invested in trucks and new employees in an effort to expand its beer distribution to Kentucky.¹⁰⁴ Shortly after the distribution plan went into effect, the legislature, under pressure from distributors, voted to prevent brewers from owning a license to self-distribute.¹⁰⁵ During the same year, a similar situation occurred in North Carolina: breweries seeking an expansion to self-distribution laws met stiff resistance from the North

95. For a list of beer franchise laws by State, see *Franchise Laws*, BREWERS ASS'N, <https://www.brewersassociation.org/government-affairs/laws/franchise-laws/> (last visited May 13, 2019) (select individual states from drop-down list).

96. *Id.*

97. See *infra* Section III.B.

98. Bart Watson, *Franchise Laws: Leveling the Playing Field*, BREWERS ASS'N (Dec. 17, 2014), <https://www.brewersassociation.org/insights/franchise-laws/>.

99. See *supra* notes 13–20 and accompanying text; see also *infra* note 183 and accompanying text.

100. *About NBWA: Mission Statement*, NAT'L BEER WHOLESALERS ASS'N, <https://www.nbwa.org/about> (last visited May 13, 2019) (“The purpose of the National Beer Wholesalers Association is to provide leadership which enhances the independent beer distribution industry; to advocate before government and the public; to encourage the responsible consumption of alcohol; and to provide programs and services that will benefit its members.”).

101. For information on the NBWA's lobbying efforts, see *National Beer Wholesalers Assn*, OPENSECRETS.ORG, <http://www.opensecrets.org/orgs/summary.php?id=D000000101> (last visited May 13, 2019). Another source shows that in 2014, alcohol manufacturers contributed around \$5.3 million and retailers contributed around \$2 million, while distributors contributed \$14.6 million to state elections and \$5.9 million to congressional elections. Liz Essley Whyte, *Alcohol Distributors Ply Statehouses to Keep Profits Flowing*, TIME (Aug. 6, 2015), <http://time.com/3986536/alcohol-distributors-lobbying/>.

102. See *About NBWA*, *supra* note 100.

103. Whyte, *supra* note 101 (“Daniel Okrent . . . called the public health arguments sanctimonious and said there's no evidence that wholesalers protect public health. ‘They are essentially protecting what is in effect a quasi-monopoly business,’ he said. ‘They are very powerful political lobbies with a great deal of money.’”).

104. *Id.*

105. *Id.* The lobbyists were not actually attempting to shut down Rhinegeist's distribution operation but were looking to close this loophole to the three-tier system in order to force AB InBev to sell off distributors that they owned in Kentucky. *Id.* These distributors were likely in competition with the independent distributors in that State. *Id.*

Carolina Beer & Wine Wholesalers Association.¹⁰⁶ Due to the greater financial position of distributors, brewers in the state were unable to match their lobbying efforts.¹⁰⁷

More recently, in 2017, the Texas legislature passed a law requiring brewers that produce more than 225,000 barrels annually to go through a distributor, even if the distributor would be delivering that beer to the brewer's own taproom.¹⁰⁸ Going a step further than the laws in Kentucky and North Carolina, the Texas law, which proponents argued would maintain the three-tier system and regulate large companies purchasing craft brewers, explicitly provided exceptions for three breweries that had recently been purchased by AB InBev, MillerCoors, and Heineken.¹⁰⁹

C. Taxes on Beer

Between federal, state, local, and business taxes, and business taxes, more than 40% of the price of a beer goes towards taxation.¹¹⁰ When a consumer purchases beer, the tax on that purchase is almost 70% higher than the average purchase in the United States.¹¹¹ A number of reasons are cited for having this higher tax burden on beer: disapproval of alcohol consumption, social costs (such as drunk driving, public health, and other economic losses resulting from overconsumption), and, at the most basic level, revenue generation.¹¹² Whether or not taxation is the appropriate enforcement mechanism for these goals, high excise taxes present a barrier to entry for enterprising craft brewers, as well as a burden to those already in the industry who are attempting to maintain their independence from larger brewers.¹¹³

106. *Id.* Tim Kent, the executive director for the organization, was quoted as saying, "North Carolina already has by far the most progressive beer laws of any state from Virginia to Texas You've got a small group of brewers who are trying to deregulate the industry . . . at the expense of public health." *Id.*

107. *Id.*

108. Andy Duehren, *New Law Means Extra Costs for Large Craft Brewers—Unless They're Owned by Brewing Giants*, TEX. TRIB. (Sept. 13, 2017, 12:00 AM), <https://www.texastribune.org/2017/09/13/new-beer-law-puts-upper-bound-craft-brewers/>. Tom Spilman, the executive vice president of Wholesale Beer Distributors of Texas, authored an op-ed in the *Dallas Morning News* defending these regulations and attributing the growth of craft beer in Texas to the three-tiered system of distribution. Tom Spilman, *Texas Craft Beer Thrives Because of Good Regulation*, DALL. MORNING NEWS (Apr. 23, 2018), <https://www.dallasnews.com/opinion/commentary/2018/04/23/texas-craft-beer-thrives-good-regulation>.

109. Duehren, *supra* note 108 ("This has nothing to do with protecting the three-tier system.").

110. BEER INSTITUTE, BEER TAX FACTS: THE ECONOMIC AND SOCIETAL IMPACTS OF STATE AND FEDERAL TAXES ON BEER 2 (2004), <https://www.finance.senate.gov/imo/media/doc/Beer%20Institute%2004.pdf>. With recent tax reform, this number may be in flux. See *infra* note 116 and accompanying text.

111. BEER INSTITUTE, *supra* note 110, at 2.

112. David Brunori, *Taxing Beer*, FORBES (Aug. 13, 2015, 10:40 AM), <https://www.forbes.com/sites/taxanalysts/2015/08/13/taxing-beer/#781766618110>.

113. See, e.g., Simon Loretz & Harald Oberhofer, *When Helping the Small Hurts the Middle: Beer Excise Duties and Market Concentration*, in WORKING PAPERS IN ECON. AND FIN., UNIV. OF SALZBURG 2 (Working Paper No. 2014-05) (2014).

1. Federal Excise Taxes

In late 2017, federal excise taxes on beer were amended for the first time since 1991.¹¹⁴ As part of the Tax Cuts and Jobs Act,¹¹⁵ provisions of the proposed Craft Beverage Modernization and Tax Reform Act (“CBMTRA”)¹¹⁶ were adopted that reduce the federal excise tax rate to \$16 per barrel (down from \$18 per barrel) for the first 6 million barrels produced.¹¹⁷ After the first 6 million barrels, taxes return to the \$18 per barrel rate.¹¹⁸ As an additional incentive to smaller breweries, the rate is reduced to \$3.50 per barrel (down from \$7 per barrel) for the first 60,000 barrels produced by any domestic brewer producing no more than 2 million barrels annually.¹¹⁹ These provisions are currently fixed to “sunset” on December 31, 2019, after which time the tax rates will return to the 1991 levels.¹²⁰

Brewpubs and microbreweries which market and distribute their own products are the most likely to benefit from the law. Because these breweries are already limited in the amount of beer they are allowed to produce by law,¹²¹ they are likely to fit into the tax bracket under 60,000 barrels. Even still, Big Beer companies stand to save a considerable amount of money, as the first 6 million barrels they produce will be taxed at a rate of \$16 per barrel, rather than the previous rate of \$18 per barrel.

The change in law carries additional benefits, such as an increased ability to collaborate with other brewers. Excise tax liability is created at the moment of production but is not determined and payable until the alcohol is removed from

114. The pre-1991 rate was \$9 per barrel, which doubled after passage of the bill. *See* Pub. L. No. 94–529, 90 Stat. 2485 (1976) (codified as amended at 26 U.S.C. § 5051 (2017)). The \$9 rate had been introduced in 1951. DAVID H. JERNIGAN & HUGH WATERS, JOHNS HOPKINS BLOOMBERG SCH. OF PUB. HEALTH, *THE POTENTIAL BENEFITS OF ALCOHOL EXCISE TAX INCREASES IN MARYLAND* 2 (2009). The purported reason for the bill, which was addressed at a declining number of breweries, was to “enable small domestic brewers to compete more effectively against the large national breweries.” *Miscellaneous Minor Tax Bills: Public Hearing on H.R. 3605 Before the Comm. on Ways and Means*, 94th Cong. 45 (1975). That 1976 bill also first introduced the reduced excise tax on brewers producing less than 2 million barrels. For a table of federal excise taxes on beer dating back to 1862, see *Historical Tax Rates*, ALCOHOL & TOBACCO TAX & TRADE BUREAU, https://www.ttb.gov/tobacco/94a01_4.shtml (last updated Sept. 4, 2012) (table 7).

115. The colloquial short name of the law is used throughout this Note, although it is technically not the actual name of the law, as it ran afoul of Senate rules. *See* Eli Watkins, *Senate Rules Force Republicans to Go with Lengthy Name for Tax Plan*, CNN (Dec. 19, 2017, 10:14 PM), <https://www.cnn.com/2017/12/19/politics/tax-bill-name-delay/index.html>.

116. *See* Craft Beverage Modernization and Tax Reform Act of 2017, H.R. 747, 115th Cong. (2017). Industry insider groups had estimated that the reduction would provide savings of \$30.3 million to craft breweries. *Craft Beverage Modernization and Tax Reform Act*, BREWERS ASS’N, <https://www.brewersassociation.org/government-affairs/craft-beverage-modernization-and-tax-reform-act/talking-points-and-resources/> (last visited May 13, 2019).

117. 26 U.S.C. § 5051(a)(1)(B)–(C) (2018). Barrels are limited to “not more than 31 gallons of beer.” *Id.* § 5051(a)(1)(D).

118. *Id.* § 5051(a)(1)(B).

119. *Id.* § 5051(a)(2)(A).

120. *Id.* § 5051(a)(1)(C); *id.* § 5051(a)(2)(A).

121. *See infra* Section III.A.

the premises for consumption or sale.¹²² Prior to 2018, beer could only be transferred between commonly-owned breweries without assessment of the tax.¹²³ With the passage of the Tax Cuts and Jobs Act, beer may now be transferred between bonded facilities without payment of the tax.¹²⁴ Bonded facilities include breweries owned by the same person or entity, a brewery owning a controlling interest in another brewery, or an agreement between breweries where the transferor brewery has divested itself of all interest in the beer transferred and the transferee has agreed to pay the future tax.¹²⁵ While this development may seem small in comparison to the tax savings, it has large implications for smaller breweries attempting to partner with one another (or with larger players in the industry) to create innovative recipes and beers that they may not otherwise be able to brew on their own due to the tax burden.

2. State Excise Taxes & Tax Credits

State taxes, on the other hand, are much less uniform than their federal counterparts and can vary quite drastically.¹²⁶ These taxes can include per-volume taxes, wholesale taxes, and case or bottle fees.¹²⁷ State taxes—like many state laws—are highly reflective of social conditions and expectations of the state’s constituents, accounting for judgments on whether drinking alcohol is a morally or socially desirable activity.¹²⁸ While an argument could be made that there is need for reform on the state level, concerns over Federalism, as well as the differing economic and social realities touted above, make uniformity in state excise tax laws nearly impossible. Even if such reform were possible, a uniform state excise tax on beer would likely be undesirable for the same reasons.

While some state excise taxes can be excessive, tax credits may be available to brewers. In Pennsylvania, the state government passed a tax credit that provides breweries with up to \$200,000 in tax credits which are applied against the excise tax that would otherwise be levied against the brewery.¹²⁹ The only caveat is that the credit must go towards capital expenditures to expand breweries and brewpubs.¹³⁰ On the federal level, brewers may qualify for the federal R&D tax

122. 26 U.S.C. § 5054(a)(1).

123. Keith Gribbins, *Senate Tax Reform Bill Fairly Freakin’ Awesome for the Brewing Industry*, CRAFT BREWING BUS. (Dec. 4, 2017), <https://www.craftbrewingbusiness.com/featured/senate-tax-reform-bill-fairly-freakin-awesome-brewing-industry/>.

124. 26 U.S.C. § 5414(a)–(b).

125. *Id.*

126. For a map laying out state excise taxes for all fifty states, see Jared Walczak, *How High Are Beer Taxes in Your State?*, TAX FOUND. (June 7, 2017), <https://taxfoundation.org/beer-taxes-state/>; see also *Beer Excise Tax Rates in the United States as of January 2018, by State (in U.S. Dollars per Gallon)*, STATISTA, <https://www.statista.com/statistics/324598/us-beer-excise-tax-rates-by-state/#0> (last visited May 13, 2019).

127. Walczak, *supra* note 126.

128. See, e.g., Brunori, *supra* note 112.

129. Acacia Coast, *Pennsylvania Guild Secures Beer Tax Credit*, BREWERS ASS’N (Aug. 25, 2016), <https://www.brewersassociation.org/activities/pennsylvania-guild-secures-beer-tax-credit/>; see also 72 PA. CONS. STAT. § 9010 (2017).

130. 72 PA. CONS. STAT. § 9010(b)–(c); Coast, *supra* note 129.

credit, so long as they satisfy a three-requirement test.¹³¹ Tax credits may help to offset the costs of some craft breweries, but they are unlikely to stimulate continued growth in the industry on their own.

III. ANALYSIS

With the rise of Big Beer companies, the three-tier system has largely given way to a system in which the largest breweries are able to influence which beers are placed with retailers. In the middle of AB InBev's merger with SABMiller in 2015, the company unveiled a new incentive program.¹³² As part of this program, distributors that sold 98% of their beer from AB InBev's brand portfolio would receive reimbursements from the company.¹³³ Those that sold 95% from AB InBev could be eligible to have up to one-half of their marketing expenses covered by the company.¹³⁴

In addition to these incentive programs, many Big Beer companies own distributors. According to Anheuser-Busch's website, the corporation owns and operates distributors in ten states.¹³⁵ On its face, ownership of these distributors should be a violation of the three-tier system.¹³⁶ In reality, lobbying groups have created loopholes in the three-tiered system, which allow breweries to legally own distributors in these states.¹³⁷ In allowing the acquisition of SABMiller by AB InBev, the DOJ has precluded the company from purchasing distributors in the future, at least without department review of the possible effects on competition.¹³⁸ Despite this, the bargaining power of large breweries will continue to make it difficult for craft brewers to get their beer into the market through the increasingly small number of distributors not affiliated with or owned by Big Beer companies.

131. David Natan, *R&D Tax Credit Opportunities for Craft Breweries*, CRAFT BREWING BUS. (Oct. 24, 2016), <https://www.craftbrewingbusiness.com/business-marketing/research-and-development-tax-credit-advice-for-craft-brewers/>.

132. Ashlee Kieler, *Anheuser-Busch Distributor Incentive Program Raises More Concerns of a Stifled Craft Beer Market*, CONSUMERIST (Dec. 10, 2015, 4:19 PM), <https://consumerist.com/2015/12/10/anheuser-busch-distributor-incentive-program-raises-more-concerns-of-a-stifled-craft-beer-market/>.

133. *Id.*

134. *Id.*

135. *We Make the Inside and the Outside Count*, ANHEUSER-BUSCH, <http://www.anheuser-busch.com/about/wholesaler.html> (last visited May 13, 2019).

136. Brad Tuttle, *Big Beer's 5-Point Plan to Crush the Craft Beer Revolution*, MONEY (Oct. 16, 2015), <http://money.com/money/4073371/anheuser-busch-sabmiller-craft-beer/>.

137. Sarah Bennett, *Budweiser Is Trying to Fool You into Thinking Its Beer Is Still Craft. Don't Buy It*, L.A. WEEKLY (May 16, 2017, 5:30 AM), <http://www.laweekly.com/restaurants/budweiser-continues-buying-craft-breweries-around-the-us-8221119>.

138. Press Release, U.S. Dep't of Justice, Justice Department Requires Anheuser-Busch InBev to Divest Stake in MillerCoors and Alter Beer Distributor Practices as Part of SABMiller Acquisition (July 20, 2016), <https://www.justice.gov/opa/pr/justice-department-requires-anheuser-busch-inbev-divest-stake-millercdoors-and-alter-beer>.

A. Three-Tiered Distribution Model Today

The three-tiered system was originally implemented to address both temperance concerns and to curb abuses by breweries.¹³⁹ These concerns, though relevant in the 1930s, are not as relevant today with the relative decline in alcohol consumption and the nature of the modern beer industry.¹⁴⁰ Although there are undoubtedly benefits arising from the three-tiered system, the manner in which it functions can hurt consumers and craft brewers. Some of the primary issues stem from loopholes in the law and the pressures that can be exerted by larger breweries.

In markets where brewers are able to purchase and operate distributors, there is no question: the three-tier system is not operating in the manner that it was originally intended. In these jurisdictions, Big Beer companies are able to act as “quasi” tied houses through their ownership interests in distributors. In other markets, where distributors and brewers are still separated by law, other forces can similarly limit competition by craft breweries. Many markets today are made up of just two distributors: one aligned with AB InBev and one aligned with MillerCoors.¹⁴¹ In either instance, a competing craft brewery will be confined to a distributor that is controlled in part by one of their competitors and will have to fight for shelf and tap space.¹⁴² Even without direct control, distributors aligned with Big Beer companies are benefiting from the sheer volume of beer that these companies sell and are unlikely to run the risk of losing those contracts by focusing too heavily on craft beer companies.¹⁴³

Even in states that do not allow for brewery-owned distributors, other coercive and anticompetitive tactics can have just as harmful an effect on smaller breweries. With the purchase of SABMiller in 2016, AB InBev acquired SAB Hop Farms, a producer of South African hops that had previously sold any excess hops not used in their own production to craft breweries.¹⁴⁴ In 2017, AB InBev announced that due to a shortage over last year’s production, they would be unable to sell any of the hops.¹⁴⁵ The decision closely followed AB InBev’s acquisition of craft beer company Wicked Weed Brewing.¹⁴⁶ While this particular decision may not have been rooted in anticompetitive motivations, many in the industry see the move as an ominous one.

In a separate incident in May 2017, the Massachusetts Alcoholic Beverages Control Commission charged AB InBev with illegally providing retailers with

139. Brian D. Anhalt, Comment, *Crafting a Model State Law for Today’s Beer Industry*, 21 ROGER WILLIAMS U. L. REV. 162, 171 (2016).

140. Scheherazade Daneshkhu, *Beer Sales Slide as Global Alcohol Consumption Falls*, FIN. TIMES (June 3, 2017), <https://www.ft.com/content/5b7fab74-47a2-11e7-8d27-59b4dd6296b8>.

141. Sorini, *supra* note 18.

142. *Id.*

143. *See* Hoium, *supra* note 20.

144. Mike Pomranz, *AB InBev Cuts Off South African Hops from Craft Brewers*, FOOD & WINE (May 12, 2017), <http://www.foodandwine.com/news/ab-inbev-cuts-south-african-hops-craft-brewers>.

145. *See id.*

146. *Id.*

nearly \$1 million in branded equipment in violation of Massachusetts law.¹⁴⁷ AB InBev has stated an intention to fight the charges, denying that their behavior constitutes “pay-to-play” sales tactics that would promote their brands over other breweries.¹⁴⁸ Pay-to-play refers generally to the practice of “providing compensation . . . to establishments in order to secure the right to serve alcoholic beverages, most often to the exclusion of competitors.”¹⁴⁹ What constitutes pay-to-play can be contentious, but no one in the industry doubts that it is a common occurrence.¹⁵⁰ These stories are not atypical, and many more charges of play-to-play tactics have been levied against Big Beer companies over the years.

For craft brewers that may already face steep competition from within their distributors—who they are likely stuck with¹⁵¹—other avenues of distribution have become appealing. Brewpubs, one of the most popular avenues of self-distribution, are defined as “[a] restaurant-brewery that sells 25 percent or more of its beer on site.”¹⁵² The beer at a brewpub is primarily sold in the restaurant and bar and is dispensed from the brewery’s own storage tanks.¹⁵³ Other models such as micro-breweries or contract breweries¹⁵⁴ are not as popular as brewpubs, due to restrictions that accompany each of them,¹⁵⁵ but can be an option for brewers in some states.

Brewpubs essentially provide a small exception to tied house laws, which would otherwise prohibit the integration of manufacturers, distributors, and retailers under the three-tiered system. Today, thirty-seven states and the District of Columbia have laws that allow brewpubs.¹⁵⁶ Many of these laws provide outer limits, such as limits on off-premises sales or barrel production limits, which may frustrate the purpose of the brewpub.¹⁵⁷ Colorado provides a very liberal take on

147. Jacqueline Cain, *Shock Topper: State Says Anheuser-Busch Is Anticompetitive*, BOS. MAG. (May 10, 2017, 10:08 AM), <http://www.bostonmagazine.com/restaurants/2017/05/10/massachusetts-abcc-anheuser-busch-pay-to-play/>.

148. *Id.*

149. Martin Pomeroy & Eric Speed, *The Impact of ‘Pay-to-Play’ on Craft Brewers*, CRAFT BREWING BUS. (Dec. 1, 2014), <https://www.craftbrewingbusiness.com/business-marketing/pay-play-craft-brewers/>.

150. Tara Nurin, *The Pay-To-Play Scandal in the Beer Biz: How Far It Goes Nobody Knows*, FORBES (Mar. 31, 2016, 9:00 PM), <https://www.forbes.com/sites/taranurin/2016/03/31/the-pay-to-play-scandal-in-the-beer-biz-how-far-it-goes-nobody-knows/#35ac4fd6b0d5>.

151. *See infra* Section III.B.

152. *Craft Beer Industry Market Segments*, BREWERS ASS’N, <https://www.brewersassociation.org/statistics/market-segments/> (last visited May 13, 2019).

153. *Id.*

154. *Id.*

155. Microbreweries are limited to 15,000 barrels annually, and contract brewing is when a business hires a brewery to produce their beer. *Id.*

156. For a list of self-distribution laws by State, see *Self-Distribution Laws*, BREWERS ASS’N, <https://www.brewersassociation.org/government-affairs/laws/self-distribution-laws/> (last visited May 13, 2019) (select individual states from drop-down list).

157. Justin M. Welch, Note, *The Inevitability of the Brewpub: Legal Avenues for Expanding Distribution Capabilities*, 16 REV. LITIG. 173, 176 (1997).

brewpubs: brewpubs may self-distribute their beer to retailers in addition to selling the beer on premises.¹⁵⁸ Because of the success of this model, beer distributors in the state have attempted to introduce legislation intended to restrict brewpubs.¹⁵⁹

In 2017, there were 2,252 brewpubs in the United States.¹⁶⁰ This represents a 10.3% increase over 2016 and constitutes just over one-third of the total number of breweries that year.¹⁶¹ The increasing popularity of brewpubs derives from a number of benefits that they provide, not least of which being that the brewer retains more of the profits by operating like a retailer and selling directly to consumers.¹⁶² Having recognized that brewpub laws can increase competition by bypassing the second tier, many large brewers have lobbied to preserve tied house statutes and to prevent current brewpub laws from expanding in states that have chosen to go that route.¹⁶³

State legislators should realize that expanding brewpubs can only benefit their state. Self-distribution allows a brewery to grow in its respective community, which in turn can provide more jobs, more sales (and therefore more tax revenue), and even tourism.¹⁶⁴ Big Beer companies will continue to provide their products in as many states as possible, and craft breweries may choose to leave if they feel that their prospects are better in a neighboring state with more relaxed regulations on self-distribution.

B. Current Franchise Laws

Franchise laws, which were originally intended to protect distributors from unfair bargaining by a much larger number of breweries, have become an anachronism as they no longer reflect the prevailing market conditions. There are many flaws in modern franchise laws, all of which shift power in favor of distributors. Because franchise laws govern the relationship between brewers and distributors—whom by law most brewers need in order to get their alcohol to retailers—and most states have franchise laws in place,¹⁶⁵ contracts between breweries and distributors are almost always subject to these provisions to the detriment of the brewer.

Generally, state franchise laws contain four kinds of protection for distributors: territorial, transfer, termination, and dispute resolution and remedy provisions.¹⁶⁶ Territorial protections often require brewers to grant an exclusive sales

158. *Id.* at 189–90.

159. *Id.* at 190.

160. *Number of Breweries*, BREWERS ASS'N, <https://www.brewersassociation.org/statistics/number-of-breweries/> (last visited May 13, 2019).

161. *Id.*

162. D'Aversa, *supra* note 74, at 1488. Other benefits listed include: additional source of revenue from food sales, surveying customer reactions to beers, and informal marketing of beers. *Id.* at 1487–88.

163. Welch, *supra* note 157, at 181.

164. *See generally* D'Aversa, *supra* note 74.

165. *Franchise Laws*, *supra* note 95.

166. Barry Kurtz & Bryan H. Clements, *Beer Distribution Law as Compared to Traditional Franchise Law*, 33 FRANCHISE L.J. 397, 402 (2014).

territory for their brands to the distributor.¹⁶⁷ This, in essence, creates a regional monopoly, one through which breweries must rely solely on their distributor for exposure to consumers as well as for revenue.¹⁶⁸ If the distributor neglects that brewery's beer or does not attempt to move the product at all, the brewery is likely stuck with the results. Breweries that have the ability to self-distribute may not be limited by their franchise relationship, but self-distribution is still statutorily capped in most states and prevents breweries from expanding beyond certain barrelage limits.¹⁶⁹

Transfer protections afford distributors the ability to transfer their distribution rights.¹⁷⁰ Most laws require notice to the brewery, as well as their prior approval of the transferee, but generally, the brewer cannot unreasonably withhold consent.¹⁷¹ By contrast, distributors are allowed to transfer their own interest in the distribution business without consent, which may land the brewery with an owner that they never would have agreed to in the first place.¹⁷² For a brewer being transferred from one distributor to another, the prospect of costly litigation over the choice to withhold their consent may be enough to deter them from doing so.

Termination protections are arguably the most damaging to brewers. Beer franchise laws often limit the grounds for termination, cancellation, or renewal of an agreement, stating that brewers may only do so for "good cause."¹⁷³ In addition, many states require brewers to provide their distributor with written notice of their breach and give them a period of time to cure the alleged fault.¹⁷⁴ Finally, remedy protections provide distributors with the right to recover damages, including treble damages, in the event that a brewer breaches various other franchise laws or contract provisions, and dispute resolution protections void choice of law provisions in favor of a distributor.¹⁷⁵ Many of these provisions are extremely troubling to small brewers. According to Marc Sorini, Counsel for the Brewers Association, good cause is defined to include a "significant breach of a 'reasonable' and 'material' term in the parties' agreement."¹⁷⁶ This can be a high burden of proof for breweries,¹⁷⁷ whose problems may be substantial enough that their distributor fails to properly market their products, to which the distributor is also granted the exclusive right to sell in that territory. In addition, state fran-

167. *Id.*

168. Joshua D. Aubuchon, *How the Beer Industry Can Brew Better Franchise Laws*, LAW360 (May 13, 2016, 12:40 PM), <https://www.law360.com/articles/795550/how-the-beer-industry-can-brew-better-franchise-laws>.

169. *See Self-Distribution Laws*, *supra* note 156.

170. Kurtz & Clements, *supra* note 166, at 403.

171. *Id.*

172. *Id.*

173. Aubuchon, *supra* note 168.

174. Kurtz & Clements, *supra* note 166, at 405.

175. *Id.* at 406.

176. Marc E. Sorini, *Beer Franchise Law Summary*, BREWERS ASS'N (2014), <https://s3-us-west-2.amazonaws.com/brewersassoc/wp-content/uploads/2017/04/Beer-Franchise-Law-Summary.pdf>.

177. *Id.* ("The burden is generally on the brewer to demonstrate cause for termination.")

chise laws may contain a supremacy clause, which makes it impossible for brewers to contract around the protections granted to distributors.¹⁷⁸ All of this combines to make brewers hesitant to enter into distribution agreements, and those that choose to may not have the necessary skills to decide which distribution agreement is going to best represent their interests in the market.

It is generally well known in the beer industry that each market will only be served by a few large distributors, each of which is aligned with a Big Beer company.¹⁷⁹ It is also generally known that these distributors have a primary goal of selling the brand that they align with, to the detriment of small brewers.¹⁸⁰ Small distributors exist in some markets, and these distributors may be a good option for fledgling breweries, however, there are downsides to the brewer.¹⁸¹ After selecting a distributor, the brewer must market their products to the distributor, who has the final say on whether or not the products will be added to their portfolio.¹⁸² These issues, and the rest of the issues outlined in this Section, may be amplified in the case of brewers who are attempting to distribute across state lines.

To reiterate, beer franchise laws are an anachronism in today's market. Beginning around 1990, distributors themselves began to consolidate, with the number of distributors falling from 4,595 to less than 3,000 in 2015.¹⁸³ States that have enacted self-distribution laws—allowing for the creation of brewpubs and other forms of direct-to-consumer sales—have alleviated some of the pressure on breweries. Even in states where self-distribution is allowed, this method only allows breweries to cater to local markets, where they may not be able to turn a profit (due to market saturation) or reach a wider audience than they would through a distribution network (that would be subject to franchise laws).

C. Excise Tax Rationales

Excise taxes on beer accounted for \$3.65 billion dollars in federal tax revenue in 2016.¹⁸⁴ On the state side, excise taxes totaled \$1.76 billion dollars.¹⁸⁵ Excise taxes do not paint the entire picture, however, as the beer industry also contributes in the form of business and personal taxes.¹⁸⁶ Because growing the beer industry will help to grow state and federal revenues, reducing excise taxation can benefit the entire economy as well as state and local communities.

Revenue generation is not the sole reason for excise taxation on beer. Taxation can also be an effective tool in curbing overconsumption, which carries

178. Aubuchon, *supra* note 168.

179. Tom McCormick, *Distribution 101: A Short Course in Distribution Basics*, PROBREW.COM, <http://www.probrewer.com/library/distribution/distribution-101/> (last visited May 13, 2019).

180. *Id.*

181. *Id.*

182. *Id.*

183. Aubuchon, *supra* note 168.

184. *A Study of the U.S. Beer Industry's Economic Contribution in 2016*, BEER INST. 1, 9 (2017) <http://beer-servesamerica.org/wp-content/uploads/2017/05/2017-Beer-Serves-America-Report.pdf>.

185. *Id.*

186. *Id.*

high social costs.¹⁸⁷ The National Institute on Alcohol Abuse and Alcoholism has found that when the cost of an alcoholic drink increases by 10%, people will drink at least 5% less.¹⁸⁸ Studies on alcohol consumption have shown both health benefits and burdens, but the benefits generally only accrue when alcohol is consumed in moderation.¹⁸⁹ All of these considerations play into excise tax decisions, at least when setting the initial rate.

Despite what these statistics might indicate, a decrease in excise taxation will have little effect on consumption levels.¹⁹⁰ The demand for beer, craft or not, is inelastic: rather than increasing alcohol consumption, a decrease in taxes and prices would simply cause consumers to shift their preferences from one beer to another.¹⁹¹ In today's market, consumers will pay more for craft beer than an equivalent quantity of any macrobrew.¹⁹² Reducing the tax burden on craft brewers should therefore allow them to pass these savings on to consumers. In this way, a change in excise tax rates will not have a large effect on consumption or public health, but would instead go a long way towards growing the craft beer industry and providing for greater investment in the economy and workers by craft breweries.

D. *Excise Taxation Abroad—The Progressive Beer Duty*

In the United Kingdom, excise taxation of beer, commonly referred to as “beer duty,” has taken on a rather different and innovative form from that used in the United States.¹⁹³ This system, known as the Progressive Beer Duty (“PBD”), was introduced in 2002 by chancellor Gordon Brown.¹⁹⁴ Introduced at a time when U.K. beer was in decline, the PBD has revitalized the U.K. beer

187. See Emily Sullivan, *Health Experts Worry Brewer Tax Cuts May Increase Costs to Nondrinkers*, NPR (Jan. 9, 2018, 6:00 AM), <https://www.npr.org/2018/01/09/575100047/health-experts-worry-brewer-tax-cuts-may-increase-costs-to-nondrinkers> (“The Centers for Disease Control and Prevention estimates that the cost of excessive alcohol use is \$2.05 per drink—costs that create financial burdens for federal, state, and local governments.”); see also *Excessive Drinking Is Draining the U.S. Economy*, CTRS. FOR DISEASE CONTROL & PREVENTION (July 13, 2018), <https://www.cdc.gov/features/costsofdrinking/index.html>.

188. Sullivan, *supra* note 187.

189. See *Health Benefits of Craft Beer*, CRAFTBEER.COM (Feb. 5, 2014), <https://www.craftbeer.com/craft-beer-muses/craft-beer-and-your-health>. But see Jamie Ducharme, *A New Study Says Any Amount of Drinking Is Bad for You. Here's What Experts Say*, TIME (Aug. 24, 2018), <http://time.com/5376552/how-much-alcohol-to-drink-study/>.

190. See Bryce Pfalzgraf, Note, *Taxing the Keg: An Analysis on the Potential Effects of Changing the Federal Excise Tax on Beer*, 2015 U. ILL. L. REV. 2141, 2174–75 (analyzing the effect of a decrease in federal excise taxes on “externalities,” such as negative health and social consequences).

191. *Id.*; see also Stanley I. Ornstein & David Levy, *Price and Income Elasticities of Demand for Alcoholic Beverages*, in RECENT DEV. IN ALCOHOLISM 303, 318 (Marc Galanter ed., 1983).

192. Joe Satran, *Here's How a Six-Pack of Craft Beer Ends Up Costing \$12*, HUFFINGTON POST (Sept. 12, 2014, 11:39 AM), https://www.huffingtonpost.com/2014/09/12/craft-beer-expensive-cost_n_5670015.html. Macrobrew, as the article suggests, is a term for the beer produced by Big Beer companies. *Id.*

193. Sara Hussein, *Breweries Unite for Small Beer Relief Reform*, MORNING ADVERTISER (Jan. 19, 2017, 9:35 GMT), <https://www.morningadvertiser.co.uk/Article/2017/01/19/Breweries-unite-for-small-beer-relief-reform>.

194. Abigail Beall, *Here's an Idea: Quit Your Job and Start Your Own Microbrewery*, WIRED (July 18, 2017), <http://www.wired.co.uk/article/how-to-start-your-own-microbrewery>.

industry. In 2000, there were roughly 500 breweries in the U.K., and in October of 2016, there were 1,700 breweries, with the trend looking to continue.¹⁹⁵

Using the previous calendar year's production rate (or an estimated rate for new breweries), brewers producing less than 5,000 hectoliters ("HL")¹⁹⁶ are able to reduce the taxes they pay by up to 50%.¹⁹⁷ After 5,000 HL, but only up to 60,000 HL, the brewer is still eligible for a reduced rate, calculated based on a formula. If beer production is between 5,000 and 30,000 HL, the brewer reduces their production value by 2,500 HL and multiplies the resulting figure by the standard rate (£19.08, or \$26.56 in U.S. dollars).¹⁹⁸ For production between 30,000 and 60,000 HL, the calculation is slightly more difficult: the production value is still reduced by 2,500 HL but it is further reduced by 8.33% of production in excess of 30,000 HL.¹⁹⁹

While calculations under the PBD can be complicated, excise taxes in the United States do not depend on alcohol by volume ("ABV") like U.K. beer duty does—this simplifies taxation. Imposing a flat rate across the board (*e.g.*, the current \$16 rate for breweries producing between 60,000 and 6 million barrels)²⁰⁰ may make the calculation even easier for brewers. This flat rate, however, also has the consequence of charging higher taxes to manufacturers that may be producing well under the production bracket limit that they are categorized under. To solve this problem, introducing a sliding-scale progressive system of taxation would have a marginal effect on tax revenue, while maximizing the amount of profit that a brewer would be able to reinvest in their business and therefore the economy.

IV. RECOMMENDATION

Distributors, who have an economic incentive to maintain the status quo in the market, are hostile to any attempts to change state laws and will continue their lobbying efforts to prevent self-distribution where it does not currently exist and to limit it where it does. If brewers were able to drum up public support to defeat lobbying efforts, laws introducing brewpubs and self-distribution would have to be greater than most existing models. States often impose a barrelage

195. *Id.* Even with these great strides, concerns have arisen that the PBD may not be enough; the structure of the tax system, the argument goes, makes it difficult for brewers to grow past 5,000 HL, after which they will receive a reduced tax incentive and eventually, if they surpass 60,000 HL, face the full brunt of excise taxation. Hussein, *supra* note 193.

196. This number works out to be just shy of 4,261 barrels. *Convert Hectoliter to Barrel [US, Beer]*, CONVERTUNITS.COM, [https://www.convertunits.com/from/hectoliters/to/barrel+\[US,+beer\]](https://www.convertunits.com/from/hectoliters/to/barrel+[US,+beer]) (last visited June 2, 2019).

197. *UK Trade Tariff: Excise Duties, Reliefs, Drawbacks and Allowances*, HM REVENUE & CUSTOMS, <https://www.gov.uk/government/publications/uk-trade-tariff-excise-duties-reliefs-drawbacks-and-allowances/uk-trade-tariff-excise-duties-reliefs-drawbacks-and-allowances#beer> (last updated Jan. 19, 2019). U.K. beer is taxed differently than U.S. beer, based on the additional consideration of alcohol by volume ("ABV"). The standard rate is charged for every 1% of strength per HL. *Id.*

198. *Id.* The formula is laid out as: $(GP - 2,500 \text{ HL}) / GP \times \text{£}19.08$. GP refers to "the actual or deemed production in the previous calendar year." *Id.*

199. *Id.* $GP - (2,500 \text{ HL} - 8.3\% \text{ of } GP \text{ in excess of } 30,000) \times \text{£}19.08$.

200. See *supra* notes 114–20 and accompanying text.

limit on breweries, after which self-distribution is unavailable and breweries must return to distributors for expansion. If states were to somehow adopt or expand to greater thresholds, brewers may still be reliant on distributors to distribute across state lines. Lobbying efforts must be kept in mind when considering any changes that would greatly upset the status quo.

In order to stimulate growth and foster continued independence in the craft beer industry, this Note argues that a number of fundamental changes to existing laws need to be made. First, changes that facilitate better access to consumers for craft brewers must be made to the “three-tiered” system. Two solutions are offered: greater adoption of self-distribution laws or, alternatively, adoption of parts of the control-model of distribution. Second, states should adopt a “retailer’s law,” which would address current distribution agreement imbalances. Finally, an even greater change in the system of excise taxation, which may already seem quite generous for craft breweries, would further help to maintain craft brewery independence and encourage growth for craft brewers, who compete in a marketplace with Big Beer companies that may own the vast majority of the resources, control the distributors, and receive even greater benefits from recent excise tax reductions.

A. *Changes to the Three-Tiered System*

The most obvious solution to the problems presented by the modern three-tiered system is an expansion of self-distribution laws by states. Self-distribution allows breweries to reach consumers directly by marketing and selling their products without the use of a distributor. Current self-distribution laws often place arbitrary caps on the amount of beer that may be sold in this manner, and state laws are extremely varied.²⁰¹ Increasing barrelage limits or eliminating them entirely for breweries that meet the definition of “craft”²⁰² reduces the cost on brewers who otherwise must deal with distribution networks for marketing and sales. Such a move is often suggested in discussions of reform to the industry,²⁰³ but, as discussed previously, distributor lobbying efforts have often proven fatal to any legislative efforts.

Apart from expanding self-distribution, another model that has shown some promising results in the sale of liquor and wine may be considered. As of today, seventeen states (and smaller jurisdictions in Alaska, Maryland, Minnesota, and

201. See *Self-Distribution Laws*, *supra* note 156.

202. Of course, the definition of craft is itself based on barrelage limits. States would either need to determine their own definition of craft or adopt the current definition as provided by the Brewers Association. See *Craft Brewer Defined*, *supra* note 25. Theoretically, at 6 million barrels the concern would shift from the need to grow a fledgling brewery back to the concern for anticompetitive effects.

203. See Anhalt, *supra* note 139, at 210–14; Luke Basha, *It’s Still 1970 Somewhere: How North Carolina’s Small Craft Breweries Hope to “Craft Freedom” from Antiquated Statutes Friendly to Distributors and National Macrobreweries*, 18 WAKE FOREST J. BUS. & INTELL. PROP. L. 340, 357–85 (2018) (discussing self-distribution laws in the context of a recent lawsuit challenging North Carolina’s particularly low barrelage limits); D’Aversa, *supra* note 74, at 1490–93. But see Adam Star, *Getting a Handle on Growler Laws*, 39 SEATTLE U. L. REV. 1079, 1086 (2016) (“[S]elf-distribution . . . does not completely correct market access issues that small brewers face.”).

South Dakota)²⁰⁴ have retained the “control” model of alcohol regulation, originally argued for by Fosdick and Scott in *Toward Liquor Control*.²⁰⁵ Few, if any, of these states have retained full control over the distribution of beer—most have maintained the system for liquor—opting instead to outsource to private distributors.²⁰⁶ For states that maintain these monopolies on liquor distribution, the results are mixed: some states have tough regulations designed to limit consumption, which makes the resulting system unpalatable to consumers, while others, such as New Hampshire and Michigan, have had an entirely different and more positive experience.

In 2015, the New Hampshire Liquor Commission (“NHLC”) opened a 24,000-square-foot retail store.²⁰⁷ Later that year, the NHLC opened an even larger store, totaling 33,000-square-feet.²⁰⁸ The NHLC has moved away from a policy of high prices and low selection, opting instead to be one of the more progressive control states. The result has been lower prices, expanded operating hours, and a selection of liquors and wines that generally exceeds that found in license states.²⁰⁹ Like New Hampshire, the Michigan Liquor Control Commission has also moved to expand its distribution operations.²¹⁰ The state has also been buffered by a number of other advancements in liquor laws such as the ability to sell alcoholic beverages at farmer’s markets.²¹¹

The benefit of such a system is that a state-run distributor is actually independent, in the way that many private distributors are not, and has the ability to keep prices low. A state-run distributor would not be dependent on one product but would be free to focus on any number of products without worrying that they would lose revenue or contracts by not focusing on Big Beer. Although beer distributors argue that they are protecting consumer choice in the marketplace,²¹² franchise law territory protections and incentives for distributors to focus on larger breweries’ products can limit consumer choice. Having a state-run distributor willing to give small and craft breweries access to consumers could expand consumer choice, as well as developing the breweries until the time that a private distributor relationship becomes feasible. Because state-run distribution centers would also function as retailers, the second and third tiers could be condensed,

204. *Control State Directory and Info*, NAT’L ALCOHOL BEVERAGE CONTROL ASS’N, <http://www.nabca.org/control-state-directory-and-info> (last visited May 13, 2019).

205. See generally FOSDICK & SCOTT, *supra* note 75.

206. *Control State Directory and Info*, *supra* note 204.

207. *Control States Up Their Game*, MARKET WATCH MAG. (June 8, 2016), <http://marketwatchmag.com/control-states-may-2016/>.

208. *Region’s Largest Liquor Store to Open Thursday in Nashua*, NASHUA TELEGRAPH (Aug. 17, 2016), <http://www.nashuatelegraph.com/life/health-lifestyle/2016/08/17/region-8217s-largest-liquor-store-to-open-thursday-in-nashua/>.

209. *Control States Up Their Game*, *supra* note 207.

210. *Id.*

211. *Id.*

212. See Craig Purser, *The New Reality for Retailers: Is Consumer Choice at Risk?*, NAT’L BEER WHOLESALERS ASS’N (Mar. 9, 2017), <https://www.nbwa.org/news/new-reality-retailers-consumer-choice-risk>. A quick Google search will uncover numerous other defenses of the status quo by beer distribution industry insiders.

thereby cutting costs. Prices, which are always a concern to the consumer, would likely remain unaffected, or even fall.²¹³

This proposal is largely theoretical and would undoubtedly be subject to the same lobbying issues as many other proposals. Additionally, to truly test the effectiveness of such a system of distribution, a current control state would need to serve as a proving ground. If such a system were found to be beneficial, adoption in license states would be an even greater uphill battle. Only by existing alongside private distributors could such a system hope to be implemented and survive;²¹⁴ distributors would need to feel that their prospects were not damaged by competition from state-run distributors and that state-run distribution would not completely take over the current private system of distribution.

B. *Circumventing Franchise Laws*

Despite the criticisms that this Note has made of beer franchise laws, the existing model of distribution is still a necessity for any mid-sized brewery that has hopes of continued growth. Distributors can be beneficial to breweries: they can provide advertising,²¹⁵ transportation for beer, and warehousing services that brewers may be otherwise unable to provide on their own due to limited financing, a lack of space, or legal limitations.²¹⁶ Likewise, self-distribution laws may not reach across state borders, and brewers may need to resort to distributors if they want to appeal to a greater consumer base.

The implementation of franchise laws has significantly reduced the market entry rate and production levels of craft brewers, and these reductions have been even starker in states that do not allow self-distribution.²¹⁷ One proposed solution has been an exemption from beer franchise laws for craft and other small brewers.²¹⁸ While an exemption from franchise laws would certainly be the best option, distributors and Big Beer companies are unlikely to take such a move lying down; lobbying efforts have been successful in blocking laws exactly like these

213. When Washington State voted to privatize their liquor sales, prices increased, despite a decrease in taxes. Sales volume also increased. Chad Sokol, *5 Years After Privatization, Washington Liquor Sales Are Up Despite Price Increase*, SPOKESMAN-REVIEW (Dec. 13, 2017, 5:30 AM), <http://www.spokesman.com/stories/2017/dec/13/5-years-after-privatization-washington-liquor-sale/#/0>.

214. This Note does not argue for a completely state-run system of distribution, as such a system would be just as unpalatable as the current system and would likely run into a multitude of issues on its own. With most, if not all, control states having privatized beer distribution, the argument in this Section instead envisions a number of state-run distributors operating alongside—and competing with—private distributors.

215. Advertising is a somewhat contentious topic. While distributors claim that they provide this service, the reality is that many brewers must provide their own advertising in one form or another. McCormick, *supra* note 179.

216. *Id.*

217. Jacob Burgdorf, *Trouble Brewing? Brewer and Wholesale Laws Restrict Craft Breweries*, MERCATUS CTR. (Sept. 15, 2016), <https://www.mercatus.org/publications/trouble-brewing-brewer-and-wholesaler-laws-restrict-craft-breweries>.

218. See Anhalt, *supra* note 139, at 199–210; Tammy Lam, Note, *Brew Free or Die? A Comparative Analysis of U.S. and E.U. Craft Beer Regulations*, 23 CARDOZO J. INT'L & COMP. L. 197, 218–19 (2014); Suzanne Laucks, Note, *Brewing Up Changes: Pennsylvania Should Modernize Its Tax Laws and Policies to Encourage the Growth of Its Craft Brewing Industry*, 14 PITT. TAX REV. 119, 142–43 (2016).

proposals.²¹⁹ Any proposed solution addressing franchise laws, therefore, must cut a balance between the interests of the craft brewer and the interests of the larger players in the market.

The ideal solution may come in the form of a check on distributors by retailers. A retailer's law would give retailers the ability to request that distributors carry new or different products and allow distributors to continue to profit from their current distribution networks, while simultaneously allowing consumers and retailers to have greater say in what products they believe should be sold. In order to make such a law effective, retailers would gain the right to purchase directly from brewers if the distributor does not make "reasonable efforts" to acquire the product within a limited period of time. A model law would provide the following:

- (a) A retailer of alcoholic beverages²²⁰ may make a request to a distributor of alcoholic beverages, in writing, that:
 - (1) names and locates a manufacturer of alcoholic beverages that the retailer would like to have added to the distributor's portfolio;
 - (2) lists the products of the manufacturer that the retailer would have the distributor provide; and
 - (3) estimates the volume and price of the product to be provided.

If the distributor so requested fails to make reasonable efforts, as evidenced by a written statement to the retailer, to acquire the manufacturer's products within sixty days, then the retailer shall have the right to purchase the products directly from the manufacturer.

- (b) Despite the right granted to a retailer pursuant to subsection (a), a distributor shall retain the right to enter into contractual agreements with any manufacturer of alcoholic beverages.

The law envisions that brewers could, with minimal effort, advertise their products directly to consumers and retailers, who could together lobby a distributor to carry that brewer's products. While this may not completely eliminate the issue of distributors focusing on Big Beer products, it does provide an additional incentive for distributors to focus on small breweries, as neglecting them would allow a retailer to bypass the second tier and the breweries to sell the products themselves. Subsection (b) provides an additional right to distributors: a "buy-back," in the event that they later choose to carry the products of a brewer. The buy-back provision has been added so that distributors would be able to evaluate the profitability of breweries on an ongoing basis and would still be able to distribute these products in the future.²²¹

219. See *supra* Section II.B.

220. For ease of drafting, the provision refers to "alcoholic beverages." The actual law would likely be limited to beer, as the liquor and wine industries are regulated differently.

221. In this way, the proposal in this Section functions similarly to the state-run distributors suggested in Section IV.A. Breweries grow through greater access to consumers, and distributors can eventually reap the

The solution is more palatable to distributors than an exception to franchise laws for smaller breweries because it grants them the option to contract with breweries that they are aware there is existing consumer demand for. If a distributor believes that the brewery requested is not worth the investment, they will be able to simply pass on the opportunity, knowing that they can easily attempt to enter into contractual arrangements with that brewery at a later date. Only the retailer that requested the brewery's products would be allowed to purchase directly from the brewery, which would not have a large effect on the distributor's profits.

Next—and in order to address the protections that distributors are granted by franchise laws—the model law would have to provide a relatively strong definition of “reasonable efforts.” The reasons for this are twofold. First, if reasonable efforts were defined loosely—or not defined at all—distributors would be able to point at the most meagre of attempts and claim that they had made a reasonable effort to acquire a brewer's products (thereby making the first provision ineffective). Second, a definition of reasonable efforts would need to be strong enough to combat the territorial protections that franchise laws currently provide to distributors. This additional provision would provide:

- (c) Reasonable efforts, as used in subsection (a), shall include:
- (1) identifying and entering into negotiations with the requested manufacturer;
 - (2) negotiating and offering contractual terms that are reasonably comparable to terms that the distributor offers to other manufacturers in its portfolio that have a similar production level to the requested manufacturer; and
 - (3) an effort to negotiate with other parties that may have an existing distribution agreement with the manufacturer.

Subsection (3) specifically addresses the possibility that a brewery may already have a contractual arrangement with another distributor, which may include territorial protections. Including this in the definition of reasonable efforts incentivizes distributors to negotiate with other distributors in spite of territorial protections.²²²

Finally, in the case of distributors that already have an agreement with a brewery but are neglecting that brewery's products, a final provision would include a protection for brewers that would supersede the termination provisions provided by franchise laws. The brewery would be allowed to terminate their contract with the distributor for good cause, with a period allowed for the distributor in question to cure.

benefits of products that have already proven themselves within the market. Such a system of regulation theoretically results in a more mutually beneficial arrangement.

222. Of course, this Section cannot be the sole remedy to territorial protections. Once a brewery is locked into a contract, other distributors would not be able to impair those obligations by operation of state law. Such efforts would therefore be subject to a lesser burden of proof on the part of distributors.

- (d) If a distributor has an existing agreement with a manufacturer of alcoholic beverages to provide that manufacturer's products, a failure to make commercially reasonable efforts²²³ to distribute those products when requested by a retailer will constitute "good cause" under the termination provisions of that agreement.
- (e) A distributor who has been deemed to have failed to make commercially reasonable efforts to distribute a manufacturer's products under subsection (d) shall have a period of 30 days in which to cure the default under the agreement.

Each of these provisions are drafted in such a manner as to make the law more agreeable to distributors.²²⁴ By only superseding franchise laws in very limited circumstances, this law would allow distributors to maintain the protections that they argue are necessary in their business while simultaneously granting retailers, consumers, and breweries the ability to join together and decide what products belong in the marketplace. In a market that some view as being oversaturated, greater input from these parties would ensure that breweries that add the most value to the market are the breweries that prosper.

C. Reducing Taxes on Craft and Other Small Breweries

Recent changes to federal excise taxes on beer are a first step in the direction of bolstering an industry that makes substantial contributions to the U.S. economy.²²⁵ One additional step that legislators could take immediately would be to extend the provisions of the Tax Cuts and Jobs Act that reduce excise taxes on beer permanent past their current sunset date of 2020.²²⁶ Yet, this may not go far enough. While the law will reduce the tax burden on smaller breweries, it also greatly reduces the tax burden on larger breweries.²²⁷ Big Beer companies like AB InBev can in turn take these additional funds and continue to purchase and harass craft breweries that are struggling to grow or that are being boxed out of markets by local distributors.

What could be done in addition to the savings generated by the Tax Cuts and Jobs Act?²²⁸ Legislation that would create an additional tier—depending on

223. This term would also need to be defined, though an existing definition used by courts interpreting contracts would likely suffice.

224. Provisions (d) and (e) are an exception to this statement, as they directly abrogate franchise law protections in relatively broad circumstances. These are the most contentious provisions suggested.

225. See *supra* Section II.C.

226. See *supra* notes 114–20 and accompanying text.

227. Carlos Frias, *Trump Tax Cut Might Keep the Cost of Craft Beer Down—or Put It Out of Business*, MIAMI HERALD (Jan. 24, 2018, 9:56 AM), <http://www.miamiherald.com/entertainment/restaurants/article196333249.html> (noting that breweries producing less than 6 million barrels annually will only see \$80 million of the \$4.2 billion in tax savings); see also Matthew Gardner, *New Tax Breaks for Craft Beer Are a Drop in the Barrel: 76 Percent of Tax Bill's Beer Tax Cut Goes to a Handful of the Biggest Producers*, ITEP (Jan. 10, 2018), <https://itep.org/new-tax-breaks-for-craft-beer-are-a-drop-in-the-barrel-76-percent-of-tax-bills-beer-tax-cut-goes-to-a-handful-of-the-biggest-producers/>.

228. See *Beer Institute Praises U.S. Congress and President Trump for Passage of Tax Relief for Brewers and Beer Importers*, BEER INST. (Dec. 20, 2017), <http://www.beerinstitute.org/press-releases/beer-institute->

the production volume of the brewery—would better allocate the tax burden and benefit small brewers that are most in need of funds. Indeed, the recent tax cuts disproportionately favor larger brewers, even with the rate reduction disparities.²²⁹ According to 2017 numbers, there were 5,533 breweries with a production value under 60,000 barrels annually.²³⁰ In the 60,000 to 500,000-barrel categories, there were a total of eighty-three breweries, and from 500,000 to 6 million barrels, there were only thirty-one breweries.²³¹ The Tax Cuts and Jobs Act cut taxes to \$16 on the first 6 million barrels produced—*regardless of the size of the brewery*.²³² Most of the savings from the tax cuts, then, are going to the breweries that need it the least.

How would this system then look? Cutting the tax rate to \$3.50 for the first 60,000 barrels will undoubtedly spur growth for new and smaller craft breweries, so this tier would remain in place. A second tier, with rates up to \$10.75²³³ for the next 440,000 barrels would help mid-sized breweries continue to grow and establish themselves in the market. Breweries in the second tier are the most likely to be able to compete with Big Beer companies. Tax reductions focused on these breweries allow for growth through reinvestment in marketing and distribution networks.²³⁴ By limiting the tax savings to craft breweries with small market shares, the law could also foster greater competition in the market and drive down the price of craft beer.²³⁵ In general, these changes would only affect consumer preferences, not the overall consumption of beer.²³⁶

Alternatively, or in addition to the additional tier proposed above, a system akin to that used in the U.K. could be adopted.²³⁷ Basing excise taxation on actual production values, breweries could receive excise tax relief on a progressive rate scale depending on their output.²³⁸ For breweries producing up to 60,000 barrels annually, the \$3.50 rate would remain in place. At the next proposed tier, brewers producing between 60,000 and 500,000 barrels annually would be assigned a rate based on their production for the previous year (or an estimated production value in the event that a brewery could produce greater than 60,000 barrels in their first

praises-u-s-congress-president-trump-passage-tax-relief-brewers-beer-importers (estimating that federal excise tax relief “could create an additional \$320 million in annual economic growth”).

229. See generally Jeff Stein, *Republicans Say They’ve Slashed Taxes on Small Breweries. But Big Alcohol May Be the Biggest Winners.*, WASH. POST (Jan. 3, 2018), https://www.washingtonpost.com/news/wonk/wp/2018/01/03/republicans-say-theyve-slashed-taxes-on-small-breweries-but-big-alcohol-may-be-the-biggest-winners/?noredirect=on&utm_term=.b627e8adb54a.

230. ALCOHOL & TOBACCO TAX & TRADE BUREAU, NUMBER OF BREWERS BY PRODUCTION SIZE—CY 2017 (2018), https://www.ttb.gov/statistics/production_size/2017_brew_prod_size_ttb_gov.pdf.

231. *Id.*

232. See *supra* note 117 and accompanying text.

233. This number was chosen as the midway point between the lowest and highest existing rates. Other figures could of course be provided by the legislature.

234. Naomi Jagoda, *Alcohol Industry Pushes Lawmakers to Uncork Excise Tax Relief*, HILL (May 16, 2018, 6:00 AM), <https://thehill.com/business-a-lobbying/387874-alcohol-industry-pushes-lawmakers-to-uncork-excise-tax-relief>.

235. *Id.*

236. See Pfalzgraf, *supra* note 190, at 2174–75.

237. See *supra* notes 193–99 and accompanying text.

238. See *supra* notes 193–99 and accompanying text.

year). That rate would be the sum of the difference between the \$10.75 rate and the \$3.50 rate, reduced by the percentage which the brewer is under 500,000 barrels.²³⁹

Of course, reductions in excise tax rates would lead to an equal reduction in excise tax revenues. In order to make up the difference, which may not be palatable to the government or to taxpayers, one possibility would be to raise the tax rate back to \$18 on every barrel produced by brewers that are expected to exceed production of 500,000 barrels annually. Doing so would also address an additional concern raised by the Tax Cuts and Jobs Act: that Big Beer companies are being handed large sums of money in the form of tax relief that they can in turn use to further harass craft breweries.²⁴⁰

As this Note has attempted to take a practical approach to legal change in the industry, it must be acknowledged that any tax cuts (and raises) would have to be supported by Big Beer companies and distributors, due to their pervasive lobbying efforts. In this vein, it is unlikely that Big Beer companies would support a raise in their own excise taxation. The cuts provided by the Tax Cuts and Jobs Act were the first changes to excise taxes in almost thirty years, and in order to make it through the legislature, the bill required the support of the entire industry.²⁴¹ For this reason, there may not be a good solution as far as lobbying is concerned. The excise tax deficit would instead have to be accounted for through increased sales and income taxes on new employees employed by a burgeoning craft beer industry.

V. CONCLUSION

The craft beer industry has made great strides in the last few decades. The beer industry as a whole makes substantial contributions to the economy in the form of tax revenues and jobs, with craft beer's market share having grown exponentially in recent years. While the industry has sustained its impressive growth so far, defects in the regulatory structure of beer have left future development uncertain. By easing the financial burden on smaller breweries, as well as giving them greater freedom to market and distribute their products, the industry can continue to grow and flourish, leading to greater economic gains.

Changes to the industry are difficult; Big Beer companies, as well distributors both big and small, have leverage and bargaining power much greater than

239. For example, take a brewer who produces 350,000 barrels annually. Taking this as his previous year's production, the brewer would take \$7.25 (the difference between \$10.75 and \$3.50) and multiply that by the percentage that 350,000 bears to 500,000 ($7.25 \times (350/500) = 5.075$). The resulting number, after being rounded, would then be added to \$3.50 to arrive at the brewer's excise tax rate per barrel for the new year ($3.50 + 5.08 = \$8.58$).

240. See *supra* notes 228–32.

241. Lydia DePillis, *Tax Bill Does the Booze Industry a Solid*, CNN MONEY (Dec. 22, 2017, 7:24 AM), <http://money.cnn.com/2017/12/21/news/economy/booze-taxes/index.html> (“In order to get meaningful tax relief for the breweries that I represent, it was necessary for small brewers and big brewers to come together,” says Bob Pease, CEO of the Boulder, Colorado based Brewers Association . . .”).

that of craft breweries. In some states, lobbying efforts have prevented any extensive changes to law. In other states, laws have changed for the better, but there is room for improvement if small breweries will ever have hope to compete on a larger scale. For there to be any substantial change, reforms that occur will need to be compatible with the interests of distributors or large brewers. While there is no easy answer, the proposals herein may ease the burden that craft brewers face.