AMENDMENT TO H.710 – Testimony

Franchise laws were not an original feature of the post-prohibition three-tier system, but rather were written in the 1970s when large brewers began to dominate their smaller distributers. This meant that typical contract laws weren't enough to protect distributors, who were at a decided power disadvantage, and protections to level the playing field and ensure consumer choice made sense. Consequently, regulators rethought the beer market. Beer franchise laws, which are a special privilege for beer distributors above and beyond general business laws, leveled the economic playing field and allowed smaller distributors to operate without fear of larger brewers abusing their more powerful market position.

Today's beer market calls for a similar rethink on how to address market power imbalances between large beer distributors and small brewers. Although the vast majority of brewer-distributor relationships are positive, in limited cases distributors may sit on craft brewer brands, neglecting them while not allowing them to move to another distributor. In addition, the distribution needs or desires of a craft brewer may change as their business grows. In these cases, current law prohibits small brewers from fairly and adequately addressing their business's needs, offering extremely limited recourse.

The amendment that is before you is our good faith effort at a compromise -which we believe addresses a number of the concerns raised by the distributors, without compromising on the principal that we seek to achieve through franchise law reform. The VBA believes that franchise law, as it applies to small brewers, is unfair, outdated and serves no public policy.

We heard the distributors concerns that this was too much change too quickly. We reduced the amount of change (leaving in place a number of aspects of current franchise law) and extended the effective dates. Our goal remains - that small brewers and distributors should be free to negotiate enforceable contracts that govern the terms of their relationship, including and most importantly, termination of their relationship. We believe our proposal is fair and reasonable.

As introduced, H.710 proposed to exempt craft brewers from **all aspects of franchise law**. We heard the concerns of the distributors and want to address some of those concerns.

1. **PROHIBITED ACTS.** We heard the distributors concern that under H.710 As Introduced brewers would not be bound by the "prohibited acts" in current law. We propose to maintain current law with regard to prohibited acts. Under current law, a brewer is prohibited from (1) inducing or coercing a wholesaler to accept delivery of any product that was not ordered by the wholesaler; (2) inducing or coercing a wholesaler to do anything illegal by threatening to cancel or terminate the franchise agreement; or (3) failing or refusing to deliver promptly any beer that was ordered. These prohibitions stay in place under our proposal.

2. **EXCLUSIVE TERRITORIES AND SALES TO RETAILERS.** We heard the distributors (and the retailers) concerns that under H.710 As Introduced brewers would not be bound by current law with regard to exclusive territories and sales to retailers. Current law continues in these areas under our proposal.

3. **FRANCHISE AGREEMENTS WITH CRAFT BREWERS IN WRITING BY JULY 1, 2022.** Under current law, franchise agreements don't have to be in writing. Going forward, we propose that, as of July 1, 2022, to be considered valid, franchise agreements with small brewers must be in writing. Not only is this good business practice, this is a common requirement of franchise law in a number of states, including, Florida, Kansas, Ohio, Oregon.

   The main reason that many of these agreements are not in writing today is because the parties have relied on statute (which is always subject to change) for many of the key provisions of a franchise agreement. Moving toward enforceable, negotiated written franchise agreements with craft brewers will re-level the playing field by allowing the parties to decide the mutually beneficial terms of their relationship.

   We understand that there are many franchise relationships with small brewers that are currently not in writing. We believe that by postponing this requirement until July 1, 2022 - 4 years is a reasonable amount of time for the parties to move to written agreements.

4. **TERMINATION.** To address the current reality that many distribution agreements are not in writing, or if they are, may not include termination provisions, the VBA proposes a transition period from January 1, 2019 to July 1, 2022. During this time contracts that are in writing will be enforceable as written. Contracts that are not in writing or that do not contain termination provisions would rely on statute for termination with cause and without cause as well as certain other related aspects of franchise law.

   As of Effective Date, January 1, 2019, written provisions in contracts between craft brewers and distributors will be enforceable relating to termination without cause, termination with cause, sale of franchise by wholesaler, merger of franchisor. If there are no written provisions relating to these subjects, the following statutory provisions will control.

   a. <u>Termination without cause.</u> As of January 1, 2019, If there is no written contract, or if the contract does not include a termination without cause provision, a brewer can terminate without cause upon 30 days-notice and payment of reasonable costs as defined.
      i. **To address concerns of distributors about losing the value of their investment if a small brewer chooses to leave without cause, the VBA agrees to increase the definition of "reasonable costs" from 1 times average annual gross, as proposed in H.710 As Introduced, to 5 times average annual gross.** The parties will be free to agree to use a different

valuation method. If they don't agree to a different method or process, the statute will control.

b. Termination with cause. As of January 1, 2019, If there is no written contract, or if the contract does not include a termination with cause provision, a brewer can terminate with cause **as provided for in current law statute**.
c. Sale or transfer of franchise. As of January 1, 2019, If there is no written contract, or if the contract does not include a provision relating to sale of franchise by wholesaler, the wholesaler must provide at least 90 days-notice of intent to sale or transfer. If the brewer wants to resist the sale or transfer, they can do so by paying reasonable costs.
d. Merger of franchisor. As of January 1, 2019, if there is no written contract, or if the contract does not include a provision relating to merger of franchisor, **current law will apply.**

5. **DEFINE CRAFT BREWER AS BREWER PRODUCING 300,000 BARRELS OR LESS ANNUALLY.** This is not an arbitrary amount. Nationally, a craft brewer is defined as a brewer producing less than 6 million barrels annually. Large brewers, producing more than 6 m barrels annually include the various brands manufactured by, MillerCoors, Anheuser-Busch InBev., Heinekin, Pabst…These large brands constitute about 88% of the US beer market. https://www.brewersassociation.org/statistics/craft-brewer-defined/. There are many, many, brands that sell in Vermont that produce more than 300,000 barrels.

   The volume of the small brewer carve-out from franchise law cannot be separated from outdated purpose of franchise laws - which was to level the economic playing field and allow smaller distributors to operate without fear of larger brewers abusing their more powerful market position. Franchise law is intended to protect distributors from LARGE brewers. In that context, 300,000 barrels is not large, it is small.

http://www.beerandlaw.com/blog/category/distribution