WRITTEN TESTIMONY OF CLARE BUCKLEY, EXECUTIVE DIRECTOR,
VERMONT WHOLESALE BEVERAGE ASSOCIATION
REGARDING H.710, AN ACT RELATING TO BEER AND WINE FRANCHISES
February 28, 2018

Good afternoon Chair Head and members of the committee. My name is Clare Buckley and I am here today on behalf the Vermont Wholesale Beverage Association whose members include many of Vermont's beer and wine wholesalers.

Vermont distributors employ approximately 700 Vermonters. The average annual wages and benefits for an employee in Vermont at the four VWBA member distributors is $50,830 in salary, $10,920 in benefits for a total of $61,750 per employee per year. Vermont distributors are longstanding Vermont-based, family-owned businesses that are important for Vermont's economy.

Vermont has one of the highest number of breweries per capita in the country. This was achieved under the current beer franchise law. That was not a coincidence. It is very expensive to introduce, market and promote a new product in a market.

In Vermont, brewers have a choice. They can either make the investment in distribution infrastructure themselves or they can get distributors to make that investment on their behalf. Typically, craft brewers do not have the resources to make that investment. Accordingly, they get distributors to make that substantial investment. This investment ordinarily entails hundreds of thousands, if not millions, of dollars for the construction or acquisition of refrigerated warehouses, the acquisition or lease of a fleet of trucks or other vehicles, the acquisition of racking systems, the acquisition of a sophisticated computer software system and hardware, employing a sales force, employing a delivery force, and paying for the promotion, advertising, and marketing of the products. Distributors are only willing to make that substantial investment, however, if they have assurance that a brewer cannot inequitably usurp that investment by terminating without notice, without an opportunity to cure and without good cause. The Vermont beer and wine franchise law provides that assurance.

VWBA members have serious concerns that the current proposed strike-all bill will have the effect of deterring that investment and ultimately reducing the unparalleled choice and variety that Vermont consumers currently enjoy. They are also concerned that it may be vulnerable to a successful constitutional challenge. Nonetheless, VWBA members have listened and understand that truly small breweries desire to terminate a franchise without cause. At the behest of members of the legislature, we offer a proposal as a potential compromise to do the least damage possible to Vermont's family-owned beer and wine distributors and retailers. We urge the committee to amend the strike-all version of H.710, dated 2/22/18 as follows:

1. **Size of Exempt Brewery & Percent of Distributor's Portfolio**

Proposed Amendment #1: VWBA requests that the bill be amended to provide that breweries producing 775,000 Gallons (25,000 barrels) of malt beverages per year and whose sales to a distributor are one percent or less of a distributor's total annual sales of malt beverage may terminate a franchise agreement without cause.

VWBA urges the committee to look at available data to decide what truly is a "small" brewer. This strike-all draft proposes 200,000 barrels of beer.

200,000 barrels raises potential constitutional issues if implemented because every Vermont brewer (according to Brewers Association data), but not every out-of-state brewer, could terminate a franchise agreement without cause. *See Family Winemakers of California v. Jenkins*, 592 F.3d 1 (1st Cir. 2010).

But even if it were constitutional, a brewer producing 200,000 barrels of beer a year is in no way small. Different measures of "small" include:

- The federal Alcohol and Tobacco Tax and Trade Bureau (TTB) recognized in a rulemaking in 2012, "[t]here is no specific statutory or regulatory definition as to who is a 'small' brewer." As a result, they undertook a comprehensive review of the size of breweries and settled on 7,142 barrels as the threshold for small brewer tax and paperwork reduction.

- According to data the TTB published in 2016:

    - 74% of all reporting US breweries make less than 1,000 barrels.
    - 95% of all reporting US brewers make less than 15,000 barrels.

- Only four percent of brewers in the United States brew 200,000 barrels or more per year. (TTB data published in March 2016). 200,000 is not a "small" brewer.

On the flip side, VWBA's proposal of 25,000 barrels covers *96 percent* of all breweries in the United States. (Brewers Association data from 2016; TTB data published in March 2016) VWBA's proposal of 25,000 barrels is sizeable. At 31 gallons per barrel that is 775,000 gallons of beer. At 2.25 gallons per case that is 344,444 cases of beer. And at 24 bottles per case, that is 8,266,666 bottles of beer.

Colorado has many craft brewers like Vermont and uses 300,000 gallons (not barrels) which is 9,677 barrels. North Carolina uses 25,000 barrels.

New York uses 300,000 barrels AND the brewery is 3 percent or less of a distributor's annual beer sales. The 3 percent recognizes the impact a brewer leaving will have on its distributor.

VWBA proposes that the committee also adopt a provision that provides that only a brewery whose sales to a distributor is one percent or less of a distributor's total annual sales of malt beverages may terminate without cause. This standard is not about the size brewer but instead measures the level of impact on a particular distributor. It is important to all VWBA members, but particularly important to small distributors.

2. **Fair Market Value** – Fair market value is critically important to distributors in instances where a small brewer is terminating a franchise agreement with no cause. Distributors have often spent years building a brand and if a brewer leaves for no cause it is only fair the distributor be compensated for its investment. We strongly support the new definition of "fair market value" in the strike-all draft and the fact that fair market value will be an on-going requirement in Vermont law whenever a brewery chooses to terminate without cause. But who determines fair market value?

We urge the committee to adopt a process where the parties attempt to agree to a fair market value. If they are unable to agree, fair market value should be determined in arbitration, with timeframes, which would expedite the process. It avoids the courts and is often less expensive.

Proposed Amendment #2:

(a) Arbitrations under this section shall be administered by the American Arbitration Association or its successor organization. The commercial arbitration rules of the American Arbitration Association or its successor organization shall govern the arbitration. Arbitrations shall be conducted before one arbitrator. Within 15 days after the commencement of arbitration, each party shall agree to the selection of the arbitrator. If an arbitrator is not selected within 45 days after notice of the arbitration being filed, the arbitrator shall be selected by the nearest office of the American Arbitration Association or its successor organization. All arbitrators shall serve as neutral, independent and impartial arbitrators.

(2) The arbitration proceeding shall conclude not later than 90 days after the date of the notice of intent to arbitrate is transmitted to the other party, unless the parties agree to extend the time by agreement or the arbitrator extends the time. Any arbitration held pursuant to this section shall be in lieu of all other remedies and procedures. The costs of the arbitrator and any other costs of the arbitration shall be equally divided by the parties engaged in the arbitration. Each party shall bear all other expenses related to the arbitration. The arbitrator shall render a written, reasoned decision not later than 30 days after the conclusion of the arbitration proceeding, unless the parties agree to extend the time by agreement or the arbitrator extends the time.

3. No written agreement is reached by 7/1/22 – Under the strike-all version of H.710, franchise agreements must be in writing as of 7/1/22 or they are void and unenforceable. There is nothing in this draft to prevent a brewer in an existing contract at the time the act is effective from running out the clock, not reaching a written agreement by 7/1/22 with a distributor and getting out of the franchise without paying FMV. To avoid this, VWBA requests an amendment that if the parties have not reached a written agreement by July 1, 2022, that a small brewer

must pay the fair market value. The arbitration provisions proposed above can be used, if necessary, if the parties don't agree on fair market value. The provision would be effective January 1, 2019. This may also avoid a Contracts Clause issue.

AMENDMENT #3 Add a new Sec. 4a is added to the bill:

7 VSA sec. 759a, is added to read:

FAIR MARKET VALUE IF NO WRITTEN AGREEMENT IS REACHED

If the parties to a franchise agreement in existence on the effective date of the act cannot agree to a written franchise agreement by July 1, 2022, the manufacturer or certificate of approval holder shall pay the franchisee fair market value before terminating the franchise. The arbitration provisions in Section XXXX of this chapter shall apply if the parties cannot agree on fair market value.

Also amend the effective date section:

Sec. 10, EFFECTIVE DATES
(a) The section and Secs. 1, 2, ~~***and***~~ 3 ***and 4a*** shall take effect on January 1, 2019.

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4. **Transition Period** – VWBA is okay with the proposal in the draft strike-all amendment of H.740 that the no cause termination provision will apply to *prospective* contracts entered into after the effective date of the bill (1/1/19). However, we are concerned about the retroactive application of the new "no cause" termination provision for *existing* franchise agreements in effect on the effective date of the act as of 1/1/19 as proposed in the strike-all bill. "Good cause" termination for beer franchises has been the law in Vermont since 1976. For over 40 years there has been no requirement that franchise agreements be in writing in Vermont. There are hundreds of contracts that either are not in writing or do not contain termination provisions. It is critically important to VWBA members that there be a 3.5 year transition period to July 1, 2022, the date when all franchise agreements must be in writing, for *existing* franchise agreements in effect on the date of the act. This will allow time to negotiate the contracts and reduce the potential impact on businesses that have relied on Vermont law to do business. This change from "good cause" to "no cause" termination is significant for distributors and distributors need the time to adjust. Therefore, we urge the committee to adopt this proposed amendment to provide for that 3.5 year transition period.

AMENDMENT #4:

Sec. 10, EFFECTIVE DATE – add a new subsection (c)

(c) 3.5 year transition period:

(1) Prospective Contracts - Subchapter 2 (Small Manufacturers & Certificate of Approval Holders), shall apply to new franchise agreements for small manufacturers and certificate of approval holders entered into after the effective date of the act on January 1, 2019.

(2) Existing Contracts - Subchapter 1 (General Provisions) shall apply until July 1, 2022, to existing franchise agreements for small manufacturers and certificate of approval holders in effect when the act takes effect. Subchapter 2 (Small Manufacturers & Certificate of Approval Holders) shall apply on July 1, 2022, to franchise agreements for small manufacturers and certificate of approval holders that were in effect when this act takes effect.

5. **How barrels are counted** – There strike-all draft does not contain the "aggregate" language that requires a brewery to count all product made in and out of state similar to this language from H.710 as introduced. In addition, the "aggregate" language in H.710 as introduced doesn't address contract brewing. New York's law does address contract brewing and how that impacts counting the barrels. Therefore, VWBA requests that the following language from New York be added to the strike-all version of H.710. New York language can be revised, as necessary to fit H.710.

AMENDMENT #5:

(iv) For the purpose of this paragraph, the term "annual volume" shall mean: (1) the aggregate number of barrels of beer, under trademarks owned by that brewery and brewed, directly or indirectly, by or on behalf of the brewer during the measuring period, on a worldwide basis, plus (2) the aggregate number of barrels of beer brewed, during the measuring period, directly or indirectly, by or on behalf of any person or entity which, at any time during the measuring period, controlled, was controlled by or was under common control with the brewer, on a worldwide basis. Annual volume shall not include beer brewed under contract for any other brewer. There shall be no double counting of the same barrels of beer under clauses one and two of this subparagraph.

Source: New York Consolidated Laws. Alcoholic Beverage Control Law – ABC § 55-c. Agreements between brewers and beer wholesalers.

6. **Vinous beverages** – VWBA respectfully requests that vinous beverages be removed from the bill. The strike-all version of H.710 sets the threshold at 50,000 gallons. The Vermont Grape and Wine Council submitted testimony on 2/20/18 asking for a 25,000 gallon limit. VWBA does not have volume data for Vermont wineries or cider makers so we cannot determine if these limits are constitutional under the Dormant Commerce Clause. If the committee wants to move forward with vinous beverages, we urge the committee to take additional testimony from retailers and the numerous small vinous beverage distributors in the state about the impact it will have on them as well as Vermont consumers' ability to enjoy the large selection of wines and ciders they can choose from today in Vermont.

7. **Extend Notice for No Cause Terminations.** VWBA proposes that the time be extended from

30 to 120 days for no cause terminations. Thirty days is too short. Also, 120 days notice is required for "good cause" terminations so the same 120 days notice should be required in cases where it is the brewer choosing to terminate with no cause.

AMENDMENT #7 Amend Sec. 755(1) found on page 5, Line 7 as follows (changes bold and italicized):

(1) provide the franchisee with written notice of the intent to cancel or terminate the franchise at least ***120 days*** ~~***30 days***~~ before the date on which the franchise shall terminate;

We've had the draft strike-all bill for six days and these are the major issues we've identified to date.

VWBA urges the committee to adopt these amendments. Thank you for considering these amendments. We'd be happy to answer questions.

For more information please contact:
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