

Responses to Questions for the Record for Bob Pease

Chief Executive Officer of the Brewers Association

Senate Committee on the Judiciary

Subcommittee on Antitrust, Competition Policy and Consumer Rights

Submitted December 28, 2015

- 1. News outlets have reported a new incentive program launched by AB InBev that will offer independent distributors in the U.S. annual reimbursements of as much as \$1.5 million if 98 percent of the beers they sell are AB InBev brands. I am concerned that this will negatively impact the ability of craft brewers to access the market. Do you have concerns about the impact of this type of incentive program on the ability of craft brewers to compete?**

The recently announced ABI incentive program is a new, more aggressive, and better-funded effort to discourage “independent ABI wholesalers” from selling competing brands. The incentives are based primarily on the proportion of *competing brands* sold by a wholesaler, not on increases in sales of *ABI brands*. In mid-December, ABI announced changes in its incentive program, although full details are not public. From information provided to industry trade publications, the modified incentives appear to be designed to accommodate small local breweries whose products are distributed by independent ABI distributors. The incentives still appear to be intended to slow or disrupt the growth of regional or national brands produced by successful craft brewers.

These tactics are especially effective in the heavily regulated beer industry. As discussed at length in the Brewers Association (BA) written testimony, the state-by-state regulatory structure of the beer industry was designed to ensure that truly independent and competitive wholesalers provide market access to all brewers. Consolidation of the largest brewers and the fact that only two full-service wholesalers now serve most communities have severely undermined the goals of state lawmakers.

The ABI incentive program is likely to lead to two outcomes:

ABI company-owned and independent wholesalers can simply reduce efforts to sell competing brands to meet the eligibility criteria for ABI’s financial incentives. Under beer franchise laws in 48 states, failure to make best efforts on behalf of brands requires a brewer to terminate a wholesaler for cause. Those special protections conferred by state law on beer wholesalers force brewers to spend months or even years and huge sums to regain control of the distribution rights to their brands in each market. (*See*, Exhibit A of BA written testimony.) During the prolonged period that a brewer must fight to regain its distribution rights, that brewer’s brands get no attention in the market from the wholesaler that the brewer is trying to terminate.

Alternatively, ABI wholesalers can sell the competing brands to another wholesaler, often the sole remaining full-service wholesaler in that market. A brewer is forced to

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spend enormous time and effort to establish a relationship with a new wholesaler that already sells dozens of competing brands. ABI understands that competition in the wholesale tier no longer exists in many U.S. beer markets. ABI is uniquely positioned to take advantage of that fact and to slow and disrupt progress of competing brewers. Again, most state beer franchise laws play a role in this scenario. Most beer franchise laws protect a wholesaler's ability to sell distribution rights to a competing wholesaler unless a brewer has a reasonable objection to withhold consent to the sale. In a market served by two full-service wholesalers, no alternative wholesaler exists. If a viable third option does exist, the franchise law is significant. A brewer that objects to the sale of the distribution rights to its brands to a particular wholesaler is often forced into protracted negotiations and settlement payments to select its preferred wholesaler or to self-distribute its brands.

Both scenarios cause immediate harm to competing brewers whose brands are distributed by independent ABI wholesalers. We have directed the Subcommittee to very recent examples of these tactics in California, Missouri, and Vermont.

These are not imaginary business scenarios. In the late 1990s, ABI's predecessor company adopted similar incentives that significantly disrupted the growth of leading craft brewers. While some of those brewers recovered, they lost the benefits of innumerable commercial relationships and were forced to "start over" in many markets with new wholesalers. Today, that type of competitive dynamic would be far more difficult for craft brewers because the number of competitive wholesalers is far lower than it was in 1995.

When given the choice about which beer to purchase, American consumers are increasingly choosing the beer produced by America's craft brewers. In fact, the evidence of this is demonstrable. Sales of hundreds of small brands produced by craft brewers are increasing year over year while ABI's sales are decreasing. ABI knows that it cannot control the decisions made by individual American consumers who purchase beer, but ABI can utilize its market power and the industry regulatory structure to control the choices available to those consumers through its acquisition of craft breweries, influence on the wholesaler tier, and sophisticated understanding of the beer industry regulatory structure. We believe ABI's influence on and power over the wholesaler tier is intimately connected to its larger strategy to limit the development of competitive regional and national craft brands.

The BA reiterates its request that the Subcommittee urge the Department of Justice to take an aggressive stand against the existing ABI incentive program and any similar future initiative.

- 2. Much of the hearing focused on issues surrounding distribution, yet several participants noted that those issues may not relate directly to the proposed merger. In your view, what is the justification for considering distribution issues in connection with the antitrust authorities' review of the proposed merger of AB InBev and SAB Miller?**

The Brewers Association (BA) testimony urged the Subcommittee to review the proposed Anheuser-Busch InBev (ABI) acquisition of SAB Miller in tandem with the dynamics of the

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current U.S. beer market. The written and oral hearing testimony of ABI Chief Executive Officer Carlos Brito repeatedly indicated that ABI is paying well over \$100 billion for enhanced opportunities to do business in Africa, Asia, and Latin America, three areas of the world with great potential for growth and enormous economic and political risks. Senators were assured several times that the deal would have no effect on the U.S. market.

A venture of this magnitude and risk will certainly affect all of ABI's strategies in the United States, which is a highly profitable national market. The BA is not surprised by ABI's aggressive stance in the market. Prior to the public announcement of ABI's intent to acquire SAB-Miller, ABI's management aggressively utilized its dominant market power to achieve greater consolidation of the wholesale tier of the beer industry. Again, the state-mandated wholesale tier is the primary and only effective means of access to retailers and consumers in the beer industry. ABI's tactics diminish competition within the wholesale tier and create many opportunities for ABI to expand its dominant market share to pay down its debt and reduce risk. With an estimated 57 percent of the global profit pool for beer and \$64 billion in annual revenues, ABI will have ample resources to continue its path toward monopolization of the U.S. beer industry.

The BA testimony laid out the fact that the regulatory structure for the beer industry reasons that distribution effectively creates fifty separate heavily-regulated markets in the United States. Each market is subject to economic pressure that Anheuser-Busch InBev (ABI) is uniquely able to exert through its direct ownership of wholesalers in several of the largest states and effective control of most of its "independent wholesalers" throughout the nation. All ABI wholesalers possess enormous market power in their respective exclusive territories as most have well over a 50 percent market share. In states where ABI is both the brewer and the wholesaler, ABI's market power is significantly magnified and will grow if unchecked by antitrust enforcement. Many subtle strategies can be utilized to disrupt or diminish competition. For example, ABI's acquisition of local craft breweries in several states over the last two years gives ABI wholesalers the opportunity to focus solely on the brands acquired by ABI at the expense of the non-ABI brands. For the ABI-owned wholesalers, that step is easy. For the independent wholesalers, the incentives to reduce sales of non-ABI brands are substantial. The decisions to focus exclusively on ABI brands at the expense of competing brands are generally protected by state beer franchise laws.

Four of the five craft brewers purchased by ABI over the last two years are in states where ABI is also a substantial wholesaler, and the fifth is in Arizona, a state where one ABI wholesaler has consolidated an exclusive territory that includes most of the state's population:

Blue Point Brewing Co. (New York), February 2014;
10 Barrel Brewing (Oregon), November 2014;
Elysian Brewing (Washington), January 2015;
Four Peaks (Arizona), December 2015;
Breckenridge (Colorado), December 2015.

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The BA supplemented the hearing record with additional background to challenge ABI's assertions about the level of competition in the wholesale tier of the 50-state markets. Significant concentration has occurred in the wholesale tier over time. By far, the largest wholesaler is ABI itself. (*See*, Exhibit C of BA written testimony.) ABI should not be permitted to operate its own wholesale operations. Wholesaler decisions to sit on brands or to sell them are immunized by beer franchise laws in all nine of the states where ABI is a major wholesaler. The acquisition of SAB Miller will heighten the pressure on ABI to use its market power and all available levers to reduce competition in those states. We believe economic pressures generated by the SAB Miller acquisition will lead ABI to accelerate its efforts to dominate the wholesale tier of the U.S. beer industry and to limit opportunities for competing brewers to effectively access retailers and consumers in the United States. Again, the Department of Justice should look at the adverse impact on competition in the United States if ABI's strategic and tactical moves continue in the absence of intervention based on federal antitrust laws.