September 30, 2016

BY ELECTRONIC MAIL

Peter J. Mucchetti, Esq.
Chief, Litigation I Section
Antitrust Division
United States Department of Justice
450 Fifth Street, N.W.
Suite 4100
Washington, D.C. 20530

Dear Mr. Mucchetti:

**Re:** Comments from the Brewers Association to the U.S. Department of Justice Antitrust Division Regarding the Proposed Consent Order in United States v. Anheuser-Busch InBev SA/NV and SABMiller plc

The Brewers Association[1] ("BA") appreciates the efforts of the Antitrust Division and its staff members who closely investigated the competitive implications of Anheuser-Busch InBev SA/NV's ("ABI") ABI's acquisition of SAB Miller. This was a significant undertaking by a dedicated team. BA also appreciates the relief that DOJ obtained through the Proposed Final Judgment ("PFJ"), which targets some of the ways that ABI has sought to use its dominant market position to limit distribution options for craft brewers and other beer suppliers.

BA submits this comment to assist the Antitrust Division and the Court in ensuring that the PFJ in *United States. v. Anheuser-Busch InBev SA/NV and SABMiller plc* remedies the competitive issues that the DOJ Antitrust Division has identified. As written, the PFJ leaves ambiguities or other shortcomings that create substantial risk that the PFJ does not adequately resolve the competitive concerns that the DOJ Antitrust Division determined needed to be remedied.

**Background on Beer Distribution**

As the DOJ knows, and is reflected well in the Competitive Impact Statement ("CIS"), beer brewers usually cannot sell beer directly to retailers. While limited exceptions exist, state licensing and beer franchise laws generally require brewers to sell their beer to distributors who sell the beer to licensed retailers. There are two networks of beer distributors in the United

[1] Brewers Association is a non-profit trade association supporting the interests of small and independent brewers in the United States.

States that provide efficient and effective paths for brewers to move their products through the regulated distribution system to consumers, and those two networks are formed around the two dominant U.S. brewers: ABI and MillerCoors. ABI owns distributors in ten states, including New York, California, and other large states. The ABI-owned distributors focus almost exclusively on ABI brands and a few local brands. Brewers of non-ABI brands in ABI-owned distributors face substantial costs to terminate the ABI-owned distributors because the state licensing and beer franchise laws protect ABI as a distributor. In all other U.S. locations, representing approximately 90% of ABI's total volume, ABI's products are distributed by independent distributors (each defined in the PFJ as an "Independent Distributor"). Those Independent Distributors also handle products from brewers other than ABI (each defined as a "Third-Party Brewer" in the PFJ). Third-Party Brewers, such as craft and other brewers, are reliant upon those independent distributors in the ABI and MillerCoors networks to reach the ultimate consumers.

**Background to Restrictions on ABI's Incentives to Prevent Distribution of Third Party Brewers' Beer**

ABI has used a number of tools to exert control or to influence its distributors so that they restrict their handling of beer brewed by third parties, such as BA's members. These tools seriously undermine distributor independence. They are also particularly harmful to craft brewers, as each ABI Independent Distributor is one of the two full-service distributors that serve state-mandated exclusive territories in most communities. One tactic ABI has employed is to provide strong financial incentives to a distributor if the distributor affirmatively limited its sales of beer brewed by parties other than ABI. The most recent example of this program was the Voluntary Anheuser-Busch Incentive for Performance program ("VAIP"). The VAIP provided incentive payments based upon the distributor's "alignment" with ABI's brands. The VAIP rewarded distributors financially if they limited their sales of non-ABI (i.e., third-party beer) as a group, and it penalized distributors financially if they handled more than a minor amount of third-party beer. Notably, the VAIP treated sales of third-party beer in the aggregate in determining whether the loyalty targets were met. For example, if a distributor handled five different third-party beers, each of which represented one percent of the distributor's sales, that distributor would be viewed has having five percent of its sales of non-ABI brands for calculating loyalty under the VAIP. DOJ believed these programs created competitive harm, and sought to remedy them in the PFJ.

Section V.D of the PFJ attempts to prohibit programs such as the VAIP, but it leaves significant loopholes. The DOJ and the Court should fix these issues to ensure that the anticompetitive effects DOJ found to be created by ABI's loyalty incentive program are adequately remedied by the Final Judgment, assuming it is entered in some form following the comment period.

Section V.D. of the PFJ states:

> Defendant ABI shall not unilaterally, or pursuant to the terms of any contract or agreement, provide any reward or penalty to, or in any other way condition its relationship with an Independent Distributor or any employees or agents of that Independent Distributor based upon the amount of sales the Independent Distributor makes of a Third-Party Brewer's Beer or the marketing, advertising, promotion, or retail placement of such Beer. Actions prohibited by this Sub-section include, but are not limited to: . . .
>
> 2. Conditioning the prices, services, products support, rebates, discounts, buy backs, or other terms and conditions of sale of Defendant ABI's Beer that are offered to an Independent Distributor based on any Independent Distributor's sales, marketing, advertising, promotion, or retail placement of a Third-Party Brewer's Beer . . .

PFJ V.D.2. This provision is one of several that are intended to prohibit ABI from "instituting or continuing any practices or programs that impede or disincentive ABI-Affiliated Distributors from selling, marketing, advertising, promoting, or maximizing the retail placement of the beers of Third-Party Brewers. . ." CIS p. 19. It is clear from the CIS that DOJ's intention through the PFJ is to restrict the type of conduct that ABI had engaged in through incentive programs such as the VAIP. The VAIP calculated loyalty based on a distributor's sale of non-ABI products in the aggregate rather than by each individual brewer whose products are sold by an Independent Distributor. An Independent Distributor that handled five independent craft beers that, collectively, represented five percent of the distributor's sales would be classified under the VAIP program as 95% loyal to ABI even though the VAIP did not specify any of those five competing brewers in the VAIP program. We understand based on the CIS, and ABI's elimination of the VAIP program at the time it entered into the PFJ, that the PFJ prohibits programs like the VAIP that do not specifically reference any one Third Party Brewer's Beer but instead create disincentives based on a distributor's Third Party Brewers' beer in the aggregate. Thus, BA understands that the language in several of the restrictions in V.D of the PFJ that refers to "a Third Party Brewer's Beer" are not meant to limit the applicability of the restrictions in the PFJ to ABI programs that specifically reference or relate to a single brewer's beer. Instead, any program, such as the VAIP, is prohibited if it would condition the availability of ABI's beer, or condition "the prices, services, product support, rebates, discounts, buybacks, or other terms and conditions of sale of Defendant ABI's Beer" on an Independent Distributor's sales, marketing, advertising, promotion, or retail placement of Beer brewed by other brewers as a group. BA expects that DOJ would treat a future ABI program such as the VAIP as a violation of the PFJ. If the DOJ believes that any language changes are needed to ensure that the intent reflected in the CIS, as reflected above, is accomplished, then DOJ should seek to modify the PFJ to do so.

**The carve outs at the end of V.D enable ABI to resurrect programs creating the same problems created by the VAIP, defeating the relief DOJ intended to achieve.**

Recall that the VAIP provided significant financial awards to distributors based upon their levels of "loyalty" to ABI's products and "voluntary" limitations on the sale of competing suppliers' beers to less than 10% of an Independent Distributor's total beer sales (with higher rewards at higher levels of loyalty). The VAIP measured that loyalty based upon ABI's share of the distributor's sales, created an incentive based on ABI's share of sales, and provided a strong disincentive for the distributor to sell competing brewers' beers. The carve-out paragraph at the end V.D creates room for ABI to engage in the same troublesome conduct. V.D states:

> Notwithstanding the foregoing, nothing in this Final Judgment shall prohibit Defendant ABI from entering into or enforcing an agreement with any Independent Distributor requiring the Independent Distributor to use best efforts to sell, market, advertise, or promote Defendant ABI's Beer, which may be defined as efforts designed to achieve and maintain the highest practicable sales volume and retail placement of Defendant ABI's Beer in a geographic area. Defendant ABI may condition incentives, programs, or contractual terms based on an Independent Distributor's volume of sales of Defendant ABI's Beer, the retail placement of Defendant ABI's Beer, or on Defendant ABI's percentage of Beer industry sales in a geographic area. . ."

PFJ V.D (emphasis added). BA believes that ABI should not be allowed to provide incentives to its distributors that are determined based on the distributor reducing or limiting its sales of Third-Party Brewers' Beer. The last portion of the quoted language enables ABI to provide incentives based upon ABI's percentage of sales in a geographic area. ABI Independent Distributors already control a high percentage of beer sales in all geographies, generally between approximately 45% and 60%. Given that high share of sales to retailers and the presence of only one other effective competing distributor in most markets, authorizing these incentives replicates the type of harm based on ABI's position relative to its rivals that the VAIP created. The DOJ or the Court should require this provision to be eliminated.

The harm of the VAIP was that it incentivized a distributor to reduce its sales of Third-Party Brewers' Beer because doing so increased the distributor's "loyalty" to ABI and allowed the distributor to collect significant financial benefits from ABI as a result. Allowing ABI to provide incentives based on ABI's share in a geographic area provides a similar dis-incentive for a distributor to promote Third-Party Brewers' Beer, as reducing sales of those products increases ABI's share of sales in the geographic region in which a distributor operates. This provision defeats the fundamental purpose DOJ said it was trying to achieve, which was to "ensure that Third-Party Brewers whose beer is sold by ABI-Affiliated Distributors have the opportunity to compete with ABI on a level playing field—not on a playing field in which ABI has used its influence over the distributor to favor ABI's beers at the expense of other beers in the distributor's portfolio." CIS p. 21. Allowing ABI to reward distributors based on "ABI's percentage of Beer industry sales in a geographic area," which is a figure that is influenced by the amount of Third-Party Brewers' Beer those distributors handle, allows ABI to tilt the field in its favor. This issue is particularly important because the state licensing and beer franchise laws

cited above effectively create unique geographic markets. That carve out for incentives based on ABI's percentage of beer industry sales in a geographic area is harmful to competition and should be stricken from the Final Judgment.

**The Cap On Distribution Should Prevent ABI From Acquiring Additional Distributors**

The DOJ recognized the competitive threat created by ABI's ownership of distributors, and placed a limit on that ownership. However, as drafted the ownership cap still leaves substantial room for ABI to limit competition through its ownership and shuffling of its distribution network.

The PFJ states:

> Defendant ABI shall not acquire any equity interests in, or any ownership or control of the assets of, a Distributor if (i) such acquisition would transform said Distributor into an ABI-Owned Distributor, and (ii) as measured on the day of entering into an agreement for such acquisition more than ten percent (10%), by volume, of Defendant ABI's Beer sold in the Territory would be sold through ABI-Owned Distributors after such acquisition."

PFJ V.B. This cap on distributor ownership is helpful, but it leaves significant room for ABI to continue to tilt the table in its favor because the ten percent cap leaves room for ABI to move additional distribution territories to its favored and strongly aligned distributors while remaining below the ten percent cap. ABI's past conduct shows a pattern of treating distributors as a fungible group of businesses that can be purchased and resold to achieve ABI's strategic goal of reducing the number of ABI Independent Distributors by consolidation into ABI-Owned Distributors or a select group of favored distributors with longstanding financial ties to ABI. In the third and fourth quarters of 2015 alone, ABI traded, purchased, or resold distribution rights for millions of cases of beer in four states.

ABI's purchase and subsequent sale of Colorado distributorships and its trade of ABI-owned Kentucky distributorships for Colorado distributorships illustrate the room this cap leaves for ABI to further consolidate its distribution control. To start with, by way of background, not all "independent" distributors are equally independent. Some distributors are truly independent businesses. Other ABI distributors are particularly close with, loyal to and dominated by ABI. For example, through a series of acquisitions supported by ABI, two ABI distributors owned by immediate family members the CEOs of ABI's predecessor, Anheuser-Busch, hold the majority of distribution rights to ABI products in the State of Missouri. One now also owns a Southern Illinois distributor. The other purchased some Colorado distributors in a complex transaction described below. Several similar examples exist. ABI has already used these favored distributors as a tool to work around limitations placed on its ownership of distributors. ABI owned a distributor in Kentucky and acquired an adjoining distributor in 2014. Following that acquisition in early 2015, the Kentucky legislature passed a bill that made it unlawful for a

brewer to own a distributor in the state, so ABI needed to shed its ownership of the ABI-Owned Distributors in Kentucky. To do so, ABI arranged for a swap with Standard, a distributor that is very closely aligned with ABI in three other states. Through this swap, ABI acquired Standard's distributorship in Colorado in exchange for ABI's Kentucky distributorships. As a result, ABI did not increase the number of distributors it owned, but it acquired ownership of the Colorado distributorship and moved the Kentucky territory under a very closely affiliated "independent" distributor. Simultaneously, ABI acquired other Colorado distributors and sold them to Stephen Busch, the owner of Krey Distributing, which holds ABI distribution rights in a large part of the State of Missouri.

Another example is a complex distributor transaction announced in August 2016 in Mississippi, the state where ABI has its highest market share. ABI exercised an option under its Wholesaler Equity Agreement to intervene in a negotiated sale of Rex Distributing ("Rex") to Adams Beverage ("Adams"), both existing Independent Distributors. ABI asserted its right to purchase the distribution rights at the same price (the so-called "match and snatch" right) and immediately awarded the rights to Mitchell Distributing ("Mitchell"), which already distributes ABI brands in a large portion of Mississippi and other states. This exercise of the right to meet the terms of the negotiated deal and immediately flip the rights to a friendly distributor increased ABI's control over its distribution network without increasing ABI's percentage ownership of that network, but the harm is similar.

The ten percent cap on distribution ownership leaves room for ABI to play shell games with distributors as it did in the Colorado / Kentucky swap situation and in Mississippi. ABI can further consolidate its control over its distribution network by selling some of its majority-owned distributorships to organizations that are very closely aligned with ABI, and thereby free up room under the ten percent cap for ABI to acquire additional distributorships. The net result will be an increase in ABI's distribution control even if it does not increase the percentage of its beer sold through majority-owned distributors. The PFJ should simply prevent ABI from acquiring any additional distributorships.

**The provision relating to ABI requiring marketing spend on its products should include a carve out for new craft beer products.**

The PFJ includes a provision that allows ABI to require its distributors to allocate marketing spending to ABI's products. "Defendant ABI may require an Independent Distributor to allocate to Defendant ABI's Beer a proportion of the Independent Distributor's annual spending on Beer promotions and incentives not to exceed the proportion of revenues that Defendant ABI's Beer constitutes in the Independent Distributor's overall revenue for Beer sales in the preceding year." PFJ. V.D. BA believes the measurement used in this provision creates several issues that unfairly assist ABI. First, ABI's sales of Beer have declined for several years. In a declining business, apportioning marketing spend to those declining brands based on the prior year's performance results in artificially inflated current year spending for those brands, and this will perpetuate year after year. It would be more appropriate for distributors' marketing spending in

a given year to be measured against the revenues received in that year. Second, as new craft beers enter the marketplace or enter a new geographic territory, they will require marketing spending in the current year even though no revenues were generated by the distributor from those brands in the prior year. Also, brewers and distributors traditionally provide more support for a brand in the year that it is introduced. It is therefore appropriate to allow for an exception that should exclude from any marketing spend measurement the spending on newly added products in the year in which they are added.

**DOJ should closely investigate any future acquisitions by ABI.**

The PFJ requires ABI to provide advance notice to the Antitrust Division prior to acquiring other brewers or distributors. PFJ XII. The CIS notes that "ABI has acquired multiple craft breweries over the past several years, some of which were not reportable under the HSR Act. Acquisitions of this nature, individually or collectively, have the potential to substantially lessen competition, and the proposed Final Judgment gives the United States an opportunity to evaluate such transactions in advance of their closing. . ." CIS pp. 25-26.

BA believes that ABI's past acquisitions of craft breweries have harmed competition. ABI has acquired nine craft breweries in the past five years. These serial acquisitions have enabled ABI to thwart the most likely (and perhaps only) disruptor to its entrenched market position: independent craft brewers on a pathway to scale.

In recent years, as consumer demand for craft beer has grown, many distributors who carry ABI's brands also have begun to carry competitive craft brands. This is important because access to ABI distributors is necessary for craft brewers to gain regional and national scale. Indeed, ABI recognized this and had sought to block access through earlier incarnations of programs like the VAIP. These attempts were largely unsuccessful because consumers demanded access to crafts and distributors needed to satisfy that demand.
However, the serial craft acquisitions enable ABI to eliminate craft competition, by forcing distributors to carry ABI's newly-acquired crafts brands, which leaves less room for independent crafts. ABI is using that leverage to implement programs that have resulted in distributors abandoning or pulling back support from competing craft breweries—an effect that would not have been possible if independent crafts were able to compete on the merits in response to consumer demand.

DOJ has taken steps through the PFJ to implement conduct restrictions on ABI that eliminate some of the most obvious and egregious programs that ABI put in place, such as the VAIP program. DOJ has not attempted through the PFJ to address some of the other ways in which ABI is exerting dominance in the U.S. Beer market, including its use of exclusive arrangements with key sports and entertainment venues, and BA suggests the DOJ continue to monitor ABI's conduct beyond the scope of the current complaint and PFJ. However, the history of the beer industry demonstrates that ABI is quite clever at finding loopholes around seemingly clear obligations and harming competition within the unique distribution networks mandated by the

laws of each state. Indeed, BA believes that the conduct remedies, in the long run, are unlikely to adequately preserve competition from crafts and that DOJ should instead require divestiture and/or a moratorium on future craft acquisitions.

BA does not expect ABI to stand still, but to continue to find ways to force more of its beer to the consumer level, including by taking advantage of current and future craft brands to foreclose competitors' access to ABI's independent distributors. Craft brewer acquisitions that may appear competitively innocuous at first blush can have severe ramifications on the industry at the expense of consumers and competition, and any ABI acquisition should be carefully reviewed and considered as part of an overall strategy rather than in isolation. As part of this review, DOJ should reach out to interested industry participants for their views. DOJ cannot rely on industry participants contacting DOJ because in some cases the transactions may not be publically announced because they are not material to ABI.

In addition, the prior reporting of acquisitions should include situations in which ABI exercises its right to acquire a distributor, but then transfers those rights to a third party as was the case with Rex in Mississippi. Those transfers can increase ABI's control over its distribution network in way similar to ABI's direct ownership of distributors, and they need to be evaluated before they take place.

**Monitoring of this Consent Order Will Require Significant, Ongoing Diligence by the DOJ and the Monitor Trustee**

BA appreciates the restrictions that the PFJ places on ABI's conduct moving forward. Of course, the effectiveness of the relief depends upon the ABI's compliance with its obligations under the PFJ. The PFJ allows for monitoring by the Antitrust Division as well as by a Monitor Trustee. PFJ VIII and XIV. This monitoring function must be robust. An example is the sale of Rex in Mississippi, described above. This transaction raises several basic questions, the answers to which may entail a more thorough inquiry:

> Whether the volume of Rex should be included in the ten percent cap on ABI mandated in the Consent Order, and if so, for how long?
>
> Whether ABI's action effectively granted Mitchell monopoly power in the Mississippi market?
>
> Whether the substitution of one distributor for another is related to the fact that the frustrated purchaser or the target distributor sold certain non-ABI brands?
>
> Whether ABI's decision not to purchase distribution rights for other brands harmed those brands in the Mississippi market?
>
> What incentives or assistance did ABI provide to Mitchell to accomplish that acquisition?

The brewer / distributor relationships being monitored are extremely complex. ABI has several hundred Independent Distributors in the Territory and years of experience in using its market power to manipulate the regulated distribution system. Monitoring these relationships to ensure true distributor independence and access to markets for craft brewers will be a massive undertaking, and appropriate efforts must be taken to ensure that the monitoring is effective. BA or its members can proactively raise observed compliance issues, but this is not a substitute for ongoing, active monitoring of ABI's distributor relationships and programs in the ordinary course by the DOJ and Monitor Trustee team, including monitoring of actions that may not be apparent to the BA or its members.

Again, BA appreciates that the DOJ has taken steps to reduce the potential for anticompetitive effects arising from the AB / SABMiller transaction, but the success of the relief will depend on the success of the monitoring and compliance effort.

Sincerely,

Robert D. Pease
President & CEO, Brewers Association

Cc: Michelle R. Seltzer, Esq.
David C. Kelly, Esq.