Beer Distribution Law as Compared to Traditional Franchise Law

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Beer distribution laws differ from traditional franchise laws in many ways, but they do share some commonalities. Many states now regulate the relationship between those who brew or import beer into a particular state, known as brewers, and those who receive, warehouse, and distribute beer to retailers, known as distributors, through special relationship statutes that have been patterned after, and closely resemble, the relationship statutes many states have passed to protect franchisees in traditional franchise relationships.

I. Beer Distribution Relationships and Traditional Franchise Relationships

Comparing the laws enacted to regulate beer distribution relationships with those governing traditional franchise relationships requires laying out the distinguishing characteristics of each contractual arrangement. The definition of a franchise varies among jurisdictions. California law provides a clear and somewhat typical definition of a franchise by defining it as a business relationship under which (1) the franchisee's business is substantially associated with the franchisor's trademark; (2) the franchisee pays the franchisor a fee to engage in the business and use its trademark; and (3) the franchisee operates the business under a marketing plan or system prescribed in substantial part by the franchisor.[1] Some states, including New Jersey and Wisconsin,[2] define the third element more broadly, providing that a franchise exists if the franchisor and franchisee have a "community

1. Cal. Corp. Code § 31005(a) (West 2013).
2. W. Michael Garner, Franchise and Distribution Law and Practice, § 5:4 (2013).

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of interest" in the marketing of goods or services.[3] Under California's marketing plan standard, franchisees must be required to utilize the franchisor's system, marketing plan, or both for a franchise to exist, but a franchise may exist in states following the broader community of interest standard once some degree of interdependence and financial interest exists between the parties.[4] In some states, including Arkansas, Connecticut, Missouri, New Jersey, Rhode Island, and Wisconsin, a franchise exists regardless of whether the franchisee pays or agrees to pay a fee.[5]

In a traditional franchise relationship, the balance of power tips heavily in favor of franchisors. It is a widely held belief that, because franchise agreements are typically drafted by the franchisor's attorneys, franchisees have little power to negotiate favorable terms. As a result, franchising is heavily regulated at both the federal and state levels. Franchising is regulated at the federal level by the Federal Trade Commission (FTC), which imposes very specific presale disclosure requirements on franchisors selling franchises in any state through the amended Federal Trade Commission Rule on Franchising, known as the FTC Rule.[6] The inherent one-sided nature of franchise agreements has caused many states to provide prospective franchise buyers with additional protections through tough presale registration and disclosure statutes and other states to pass franchise relationship laws to benefit franchisees during the term, upon renewal and transfer, and even after expiration of their franchise agreements. For example, thirteen states, referred to as registration states, require franchisors to register their franchise offering documents before offering or selling franchises within their borders,[7] and eighteen states have franchise relationship acts in one form or another aimed at protecting franchisees from unfair treatment after they sign a franchise agreement.[8]

In a growing trend, states are passing new franchise specific legislation to provide additional protections for in-state franchisees. For example, Ohio recently amended its Business Opportunity Law to provide Ohio franchisees a

3. FUNDAMENTALS OF FRANCHISING 190 (Rupert M. Barkoff & Andrew C. Selden eds., 3d ed. 2008).

4. *Id.* at 191.

5. *Id.*

6. 16 C.F.R. § 436.

7. Federal Trade Commission, *State Offices Administering Franchise Disclosure Laws*, http://corporate.findlaw.com/business-operations/state-offices-administering-franchise-disclosure-laws.html (last visited Dec. 4, 2013).

8. Mario, Herman, *Protection After the Purchase, State Franchise Relationship Laws*, BLUE MAUMAU (May 23, 2011, 1:16 PM), http://www.bluemaumau.org/protection_after_purchase_state_franchise_relationship_laws; *See also* FUNDAMENTALS OF FRANCHISING 190 (Rupert M. Barkoff & Andrew C. Selden eds., 3rd ed. 2008) (stating twenty-one states and territories have laws governing the franchise relationship, including Arkansas, California, Connecticut, Delaware, Hawaii, Illinois, Indiana, Iowa, Michigan, Minnesota, Mississippi, Missouri, Nebraska, New Jersey, Puerto Rico, Rhode Island, South Dakota, U.S. Virgin Islands, Virginia, Washington, and Wisconsin. Ohio should now be included as the twenty-second state after its passage of additional franchise protection laws in February 2013, as discussed in footnote 10).

private right of action for fraud for certain disclosure violations; it also voids any choice of law provision that designates any law other than Ohio law to govern a franchise agreement made with an Ohio franchisee.[9] However, many states have no franchise specific laws and rely on the FTC Rule and on state remedies for fraud and breach of contract to address franchise-related problems.[10]

In a typical distributorship arrangement, the distributor operates an independent business under its own trade name and purchases and resells the supplier's products according to its own procedures, not according to the supplier's system or prescribed marketing plan. Customers generally do not associate a supplier's trademark with the distributor's business, and it is unlikely that the distributor pays a fee to sell the supplier's products.

Like franchising, however, power in beer distribution relationships tends to be unbalanced, tipping heavily in favor of brewers. Large, powerful brewers tend to dominate the beer distribution industry. For example, as of late 2012, Anheuser-Busch, the world's largest brewer, controlled approximately 46 percent of the beer marketed in the United States.[11] After finalizing a deal to buy Mexico's Grupo Modelo in June 2013, Anheuser-Busch is believed to control, directly or indirectly, over 50 percent of all beer sold in this country.[12] Another major brewer, MillerCoors, controls about 30 percent.[13] Size equals power and thus control, which is why most will stipulate that brewers generally tend to dominate the beer distribution relationship.

Unlike franchising, and as further discussed below, states take the primary role in regulating beer distribution. All fifty states regulate the sale and distribution of beer within their borders. Because of the dramatic brand consolidation in the beer industry, many states address the distribution of beer separately from that of wine and liquor, making the beer distribution industry one of the most highly regulated industries in the United States. To complicate matters, the differences among states in terms of statutes, regulations, licensing schemes, taxes, and control processes result in a legal minefield that can be difficult to navigate for brewers, distributors, retailers, and the attorneys who advise them.

9. Stanley Dub, *Recent Revision of Ohio Business Opportunity Law Provides New Protections for Franchisees*, AAFD (Feb. 6, 2013), http://www.aafd.org/blog/recent-revision-of-ohio-business-opportunity-law-provides-new-protections-for-franchisees/.

10. Johnathan Klick, Bruce Kobayashi & Larry Ribstein, *The Effect of Contract Regulation: The Case of Franchising* (Jan. 16, 2008), http://econfaculty.gmu.edu/pboettke/workshop/spring08/FranJLErev1-15.pdf (stating that Washington D.C.'s franchise termination law was repealed in 1998 by the U.S. Congress).

11. Steve Hindy, *Don't Let Big Brewers Win Beer Wars*, CNN (Dec. 12, 2012, 10:52 AM), http://www.cnn.com/2012/12/12/opinion/hindy-beer-wars/.

12. *Grupo Modelo Deal Finalized, Completing Anheuser-Busch's Purchase Of Mexican Brewer*, HUFFINGTON POST (June 4, 2013, 2:35 PM), http://www.huffingtonpost.com/2013/06/04/grupo-modelo-deal-anheuser-busch_n_3385566.html.

13. Hindy, *supra* note 12.

II. Beer Distribution Law: An Introduction to the Three-Tier System

Before examining the specifics of beer distribution law and delving deeper into the similarities between beer distribution law and franchise law, it is necessary to understand the process, known as the three-tier system, by which American consumers get their beer.

Before 1919 and the passage of the Eighteenth Amendment, brewers and producers of alcoholic beverages sold their products directly to retailers and often held unfettered ownership interests in taverns (known as tied houses), often leading to anticompetitive business practices and unscrupulous marketing tactics aimed at encouraging excessive consumption. To combat that problem, the states ratified the Eighteenth Amendment ushering in the Prohibition Era and outlawing the manufacture, distribution, and sale of alcoholic beverages. The Twenty-First Amendment repealed the Eighteenth Amendment in 1933 and gave states the primary authority to regulate the distribution of alcoholic beverages, including beer, within their borders. The three-tier system of alcohol production, distribution, and sale was born.

The three-tier system is designed to prevent pre-Prohibition style marketing tactics, generate revenues for the states, facilitate state and local control over alcoholic beverages, and encourage temperance. Its three tiers consist of brewers (top tier), distributors (central tier), and retailers (bottom tier). Brewers produce the product and sell it to distributors, also called wholesalers, who then sell the product to retailers (retail stores, taverns, etc.). In turn, retailers sell the product to consumers. In many states, importers are treated as brewers, placing them in the top tier of distribution. In less-populated states, however, large retailers may act as distributors by distributing beer products to smaller retailers, thus creating a four-tier distribution system.[14] In May 2005, the U.S. Supreme Court in *Granholm v. Heald*[15] found the three-tier distribution system to be "unquestionably legitimate."

III. Licensing Versus Control

Although state statutory and regulatory schemes establishing the three-tier system vary widely, states generally fall into one of two categories: license states and control states. License states, also known as open states,

14. Charlie Papazian, *The Future of Beer Distribution in America*, http://www.globalbeeralliance.com/craftbrewing/pdf/Future_of_beer_distribution.pdf (Humorously, the U.S. beer distribution scheme is sometimes referred to as the "four-tier system of beer distribution" of brewers, distributors, retailers, and beer drinkers).

15. 544 U.S. 460, 476 (2005) (holding that New York and Michigan laws that permitted in-state wineries to ship wine directly to consumers, but prohibited out-of-state wineries from doing the same, unconstitutionally violated the Commerce Clause).

are the most prevalent and regulate alcohol distribution using a hierarchical licensing system under which they approve and sell different licenses to businesses in each tier. There are thirty-two license states,[16] including Alaska, Arkansas, California, and Colorado, to name a few.

Although licensing systems in the license states provide accountability and an additional source of revenue for those states, they are often convoluted; determining which licenses are needed is no easy task. It is common for states to require brewers, distributors, and retailers to hold multiple licenses. Under a typical licensing scheme, brewers that brew beer in another state, but want to sell it in the license state, must obtain a manufacture's license[17] or register with a regulatory body before signing a distribution agreement with a distributor to sell its beer.[18] Beer distributors/wholesalers are required to purchase a beer wholesaler's license,[19] which allows for the distribution of beer only, but must purchase an additional license to distribute distilled spirits or wine.[20] There are usually numerous types of retail licenses, as well as separate licenses for craft brewers[21] and special events. Licenses may be required by statute, while others may be required by rule or regulation, a fact that makes ensuring compliance even more difficult. Nebraska's Liquor Control Act, for example, provides for fifteen different types of licenses[22] as well as state regulations covering the distribution of beer.

Eighteen states,[23] including Alabama, Idaho, Iowa, and Maine, and fourteen others, operate as control states. Although control states also have licensing requirements, what distinguishes them from license states is that at some point in the distribution process, they obtain a direct interest in the revenues obtained through distribution by taking an ownership stake as distributors or retailers of the product. These states are also known to exert greater control over the conditions of sale and promotion of alcohol within their borders. Pennsylvania and Utah, for example, are sometimes referred to as sole importers and require their citizens to purchase alcoholic beverages through state stores.[24]

16. Alaska, Arizona, Arkansas, California, Colorado, Connecticut, Delaware, Florida, Georgia, Hawaii, Illinois, Indiana, Kansas, Kentucky, Louisiana, Maryland, Massachusetts, Minnesota, Missouri, Nebraska, Nevada, New Jersey, New Mexico, New York, North Dakota, Oklahoma, Rhode Island, South Carolina, South Dakota, Tennessee, Texas, and Wisconsin.

17. Neb. Rev. Stat. § 53-123.01 (West 2013).

18. Taxes, South Dakota Department of Revenue, http://dor.sd.gov/taxes/ (last visited Dec. 4, 2013).

19. Neb. Rev. Stat. § 53-123.03 (West 2013).

20. Neb. Rev. Stat. § 53-123.02 (West 2013).

21. Neb. Rev. Stat. § 53-123.14 (West 2013).

22. Neb. Rev. Stat. § 53-123 (West 2013).

23. Alabama, Idaho, Iowa, Maine, Michigan, Mississippi, Montana, New Hampshire, North Carolina, Ohio, Oregon, Pennsylvania, Utah, Vermont, Virginia, Washington, West Virginia, and Wyoming.

24. *State Shipping Laws Background Information*, Wine Institute, http://www.wineinstitute.org/initiatives/stateshippinglaws/backgrounder (last visited Dec. 4, 2013).

IV. Relationship Laws: Specific Protections for Beer Distributors that Mirror Franchisee Protections

As previously discussed, an inherent imbalance of power exists between the contracting parties in both beer distribution and franchising. To address this problem in the beer distribution context, many states have passed legislation aimed at balancing power in favor of distributors by requiring good faith dealings between the parties to distribution agreements. For example, Texas has passed the Beer Industry Fair Dealing Law.[25] In Illinois, the Beer Industry Fair Dealing Act regulates relationships between brewers and distributors.[26] Utah relies on the Utah Beer Industry Distribution Act to protect distributors in that state.[27]

Not unlike franchising, which requires franchisees to make a substantial initial investment, beer distribution requires a substantial investment in infrastructure by beer distributors, which is one of many reasons why most states have an array of statutes, rules, and regulations aimed at balancing power in favor of distributors. These balancing protections may, in general, be boiled down to four categories: territorial protections, transfer protections, protections relating to termination, and dispute resolution protections/remedies.

A. *Territorial Protections*

All states protect distributors by allowing brewers to grant distributors an exclusive sales territory for their brands. In fact, most states require brewers to grant distributors an exclusive sales territory for their brands. As an example, Subsection 401(1) of Michigan's Beer Franchise Code requires that "[a supplier] shall grant to each of its [distributors] an exclusive territory, as agreed upon by the [distributor and supplier], within which the [distributor] shall be the exclusive distributor of the specified brand or brands of the [supplier]."[28] Although this practice raises some monopolistic concerns,[29] the requirement strengthens distributors and makes it easier for states to regulate the movement and sale of beer within their borders and to collect taxes.

25. Tex. Alcoholic Bev. Code Ann. § 102.71 (West 2013).

26. 815 Ill. Comp. Stat. Ann. 720/1 (West 2013).

27. Utah Code Ann. §§ 32B-13-101–302 (West 2013).

28. Mich. Comp. Laws Ann. § 436.1401 (West 2013).

29. A monopoly occurs when one company or group controls all of a market for a given product and is characterized by a lack of competition, which generally results in higher prices and inferior products. Providing a particular beer distributor an exclusive territory means that retailers do not have the ability to shop around to obtain a better price. Combining exclusive territory protections with the termination protections (virtually perpetual terms) that most states provide beer distributors may also result in fewer choices for consumers. Once a distributor has contracted to distribute the product, it can set its price for the product as high as it chooses to maximize it margins or can selectively market brands based on profit margins without running the risk that any brewer will terminate its distribution rights. Some states passed legislation providing for exclusive territories intending this consequence (higher prices) in an effort to promote temperance.

This differs substantially from franchising, however, in that franchisors may grant exclusive territories to their franchisees but rarely do so. Franchisors are required to disclose in Item 12 of the Franchise Disclosure Document (FDD) provided to potential franchisees any territorial rights the franchisee will receive upon purchasing the franchise and whether the franchisee will be granted an exclusive territory where the franchisor will not compete or license others to compete against the franchisee.[30] Franchisors generally agree not to allow another franchised outlet of the same type to operate within the franchisee's protected territory, but reserve the right to open competing outlets at nontraditional venues, such as airports, sports arenas and stadiums, hospitals, hotels, shopping malls, military bases, national parks, schools, and theme parks[31] within the franchisee's territory. The fact that states generally require brewers to provide distributors with an exclusive territory, but that franchisors are not required to provide exclusive territories to their franchisees, and typically do not do so, demonstrates the degree to which beer distributors enjoy even greater legal protections than do franchisees.

B. *Transfer Protections*

Most states also limit brewers' ability to prevent distributors from transferring their distribution rights under distribution agreements. Typically, states allow brewers to require distributors to provide them with written notice and obtain their prior approval before transferring any substantial portion of the distribution rights licensed under the distribution agreement to another distributor or before a change of ownership or control of the distributor.[32] However, in Oregon and most states, brewers may not withhold consent or unreasonably delay a distributor transfer if ". . . the transferee meets reasonable standards and qualifications required by [the brewer] which are nondiscriminatory and are applied uniformly to all [distributors] similarly situated."[33] In addition, most state beer distribution statutes allow distributors and their owners to transfer, bequeath, or devise their interest in the distribution business and the distribution agreement without obtaining the brewer's consent and sometimes without notice.[34]

30. 16 C.F.R. § 436.5(l).

31. On October 16, 2012, the Federal Trade Commission opined in its Frequently Asked Question #37 that a franchisor may not claim to provide an exclusive territory unless it "promises not to establish either a company-owned or franchised outlet selling the same or similar goods or services under the same or similar trademarks or service marks within the geographic area or territory granted to a franchisee" including outlets at nontraditional venues. Federal Trade Commission, *Amended Franchise Rules FAQs*, http://www.ftc.gov/bcp/franchise/amended-rule-faqs.shtml (last visited Dec. 4, 2013).

32. Ala. Code § 28-9-5(3) (providing that a distributor is prohibited from transferring control of its distribution business without providing the supplier a notice of intent to transfer and receiving the supplier's prior approval).

33. Or. Rev. Stat. § 474.045 (West 2013).

34. Mich. Comp. Laws Ann. § 436.1403(16) (providing that suppliers shall not interfere with, or prevent, the transfer of the distributor's business or interest to a designated member, the inheriting spouse, child, grandchild, parent, brother, or sister of a deceased individual who owned

Although the transfer-related protections provided to beer distributors tend to exceed those afforded to franchisees in most jurisdictions, a few states do extend transfer protections to franchisees by statutory provisions that resemble those commonly provided to beer distributors.[35] Interestingly, franchise transfers tend to be less contentious, and franchisee transfers are less worrisome to franchisors. This is true because the franchisor continues to receive royalties after the transfer, and the franchisee may typically only transfer the remaining term of its existing franchise agreement, which allows the franchisor to evaluate the transferee at renewal. Therefore, franchisors are usually willing to consent to franchise agreement transfers to qualified buyers, provided the franchisor receives payment of a transfer fee and the buyer signs the franchisor's then-current form of franchise agreement for the remainder of the term under the seller's franchise agreement.

Iowa is an example of a state that provides franchisee transfer protections by statute. Iowa law affords franchisees the right to transfer their franchise agreements to transferees that reasonably satisfy the franchisor's current qualifications for new franchisees and provides that refusal to provide consent to a franchisee transfer by the franchisor may not be arbitrary or capricious.[36] Hawaii and Michigan franchisors must have good cause to refuse to permit a transfer; good cause exists in these states if monies remain unpaid to the franchisor or the transferee does not meet the franchisor's reasonable qualifications, competes with the franchisor, or refuses to agree to comply with all franchise obligations.[37] California prohibits franchisors from denying consent to a transfer of a franchise to the surviving spouse, heirs, estate, or majority shareholder of a deceased franchisee but permits franchisors to exercise a right of first refusal and purchase the franchisee's franchise if the franchisee has received a bona fide purchase offer and has requested the franchisor's consent to a transfer.[38]

C. *Protections Relating to Termination*

Protecting distributors against having their distribution agreements terminated or not renewed without good cause is perhaps the most significant protection states provide beer distributors. Oregon law provides that good cause exists for a brewer to terminate a beer distribution agreement when the distributor fails to comply with a provision of the written agreement

an interest in the distributor); *see also* ARK. CODE ANN. § 3-5-1110(a)(1)(A) (providing "consent or approval of the supplier shall not be required of any transfer of the wholesaler's business to a designated member, the spouse, child, parent, brother, or sister of a deceased individual who owned an interest, including a controlling interest, in wholesaler.").

35. Arkansas, California, Hawaii, Iowa, Michigan, Minnesota, Nebraska, New Jersey, and Washington.

36. IOWA CODE § 523H.5.1.

37. FUNDAMENTALS OF FRANCHISING 215 (Rupert M. Barkoff & Andrew C. Selden eds., 3d ed. 2008).

38. CAL. BUS. & PROF. CODE § 20027 (a-b).

that is both reasonable and material to the business relationship.[39] Other states, such as Wisconsin, limit the definition of good cause—and thus the right of the brewer to terminate the agreement—to instances in which the distributer has committed fraud, been convicted of a felony, filed for bankruptcy, or knowingly distributed the brewer's products outside of its exclusive territory.[40] Statutes in most states, including Iowa, bar brewers from modifying, not renewing, or terminating any beer distribution agreement unless the brewer acts in good faith and provide that "the supplier shall have the burden of proving that it acted in good faith, [in any proceeding related to the wrongful amendment, modification, termination, cancellation, discontinuance, or non-renewal of the distribution agreement.]"[41] Termination and nonrenewal restrictions are interpreted broadly, and good cause is universally interpreted narrowly in the beer distribution context. As a result, beer distribution agreements take on a perpetual duration, more or less, in many states.

In addition to limiting the grounds for terminating a distribution agreement, states usually demand that brewers comply with stringent procedural requirements before terminating or not renewing distributors. In order to terminate distribution agreements, brewers usually must provide distributors with notice they are in default under the distribution agreement and an opportunity to cure the default. The average required cure period is ninety days, although some states, such as Virginia and Delaware, also require brewers either to notify or obtain permission from a regulating commission before they terminate the distribution agreement,[42] even though the distributor has failed to cure its defaults.

Even though seventeen states have franchise relationship laws, not all of those states specifically protect franchisees against termination or nonrenewal of franchise agreements without good cause. Delaware, Hawaii, Iowa, New Jersey, Rhode Island, and Wisconsin require that franchisors have good cause for not renewing franchise agreements,[43] but other states place other, less onerous restrictions on the franchisor's right to not renew. In general, the definition of good cause for nonrenewal in the franchise context tends to be rather broad. In good cause states, as well as others addressing the nonrenewal issue, franchisors may usually refuse to renew a franchise agreement if the franchisee fails to satisfy certain notification obligations regarding its intent to renew, the agreement specifies it is not renewable upon expiration, or the franchisor provides the franchisee with some advance notice it will not renew.

Of the four balancing protections discussed in this section, we note that the protections provided by the states to beer distributors and franchisees,

39. Or. Rev. Stat. § 474.011 (West 2013).
40. Wis. Stat. Ann. § 125.33(10)(b-c).
41. Idaho Code Ann. § 23-1107(2).
42. 4 Del. Admin. Code § 46 (West 2013).
43. Fundamentals of Franchising, *supra* note 38, at 203.

if applicable, against arbitrary early termination of their agreements most closely resemble each other. Again, only seventeen states have specific franchise relationship laws, and only twenty-three states have laws addressing the franchise relationship. Nevertheless, most of these states require the franchisor have good cause to terminate a franchise agreement before its expiration, although the definitions of good cause used by the states vary somewhat. For example, the laws of Minnesota, Nebraska, New Jersey, Rhode Island, and Wisconsin provide that good cause exists for a franchisor to terminate the franchise agreement any time the franchisee fails to substantially comply with the franchisor's reasonable requirements.[44] Other states, such as New Jersey, extend the protection against termination without good cause by imposing good faith requirements. As most franchise attorneys will attest, however, California was the first state to pass a franchise relationship law and provides the standard definition of good cause relating to the termination of a franchise: "Good cause shall include, but not be limited to, the failure of the franchisee to comply with any lawful requirement of the franchise agreement after being given notice thereof and a reasonable opportunity, which in no event shall be more than 30 days, to cure the failure."[45] In general, filing for bankruptcy, failing to comply with the franchisor's system in a way that damages the franchisor's reputation, underreporting sales, or selling unauthorized products are just a few examples of acts that may constitute good cause for a franchisor to terminate a franchise agreement in any of the states with laws addressing the franchise relationship. Although less than a majority of the states provide specific statutory protections against the early termination of a franchise agreement by the franchisor, those that do require the franchisor to have good cause to terminate the franchise agreement before its expiration. This closely resembles the protections most states provide to beer distributors.

D. *Dispute Resolution Protections/Remedies*

Finally, many states have statutes providing distributors with the right to recover damages, typically treble damages,[46] from brewers that have terminated, not renewed, or refused to consent to the transfer of a distribution agreement without good cause. In addition, states generally impose mandatory venue requirements, requiring that any disputes between a brewer and a distributor be brought in the jurisdiction where the distributor has its primary place of business, and most void all choice of law provisions in distribution agreements that specify that any law other than that state's laws govern the beer distribution agreement.

The remedy that primarily differentiates beer distribution law from franchise law is the legal right beer distributors have to reasonable compensation

44. *Id.* at 194.
45. CAL. BUS. & PROF. CODE § 20020.
46. N.M. STAT. ANN. § 60-8A-9 (E).

upon termination of the distribution agreement by the brewer, for any reason. Idaho law requires:

> In the event that an agreement is terminated, canceled or not renewed by a [brewer], the distributor shall be entitled to reasonable compensation for the laid-in cost to the distributor of the inventory of the [brewer's] products, including any taxes paid on the inventory by the distributor, together with a reasonable charge for handling of the products.[47]

In general, reasonable compensation payments must also include payment of to one to three years' worth of the beer distributor's profits, calculated as 100 percent of the beer distributor's gross margins on each case of the brewer's products sold to customers, multiplied by the number of cases of product actually sold by the beer distributor to customers during the twelve months prior to the termination. If the brewer terminates a beer distribution agreement in bad faith or for any reason other than good cause, the brewer must also pay the distributor the fair market value of "all assets, including ancillary businesses, relating to the transporting, storing and marketing of [brewer's] products" and the goodwill of the distributor's business.[48] Clearly, these protections go a long way toward shifting the balance of power back toward distributors in the beer distribution relationship.

In franchising, the remedies available to wrongfully terminated franchisees vary widely from state to state. Wrongfully terminated franchisees may recover damages, such as lost profits and unrecouped expenses, but may also recover payments for goodwill, attorney fees, and punitive damages according to the facts and the laws governing the franchise agreement. In some states, franchisors may be required to repurchase inventory if they wrongfully terminate a franchisee.[49] Although all states have antiwaiver provisions covering choice of law and choice of venue for beer distribution agreements, only some states provide antiwaiver and venue protections relating to franchise agreements to franchisees.[50] Therefore, the level of protection (and recourse) from any wrongful acts committed by franchisors that is available to franchisees depends entirely upon the state where the franchisee is located and which state's laws govern the injured franchisee's agreement. In states without any franchise relationship laws, however, franchisees must rely on injunctive relief, common law fraud, and breach of contract remedies to address the franchisor's wrongful acts. Accordingly, beer distributors are substantially better protected with regard to dispute resolution protections and remedies for wrongful acts.

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47. Idaho Code Ann. § 23-1110(1).
48. Idaho Code Ann. § 23-1110(2).
49. Cal. Bus. & Prof. Code § 20035.
50. Md. Code Ann. Bus. Reg. § 14-226 (providing that franchisors may not require prospective franchisees to release the franchisor from liability under Maryland law); *see also* Minn. Stat. § 80C.21 (providing that any condition or provision purporting to bind the franchisee to waive compliance or has the effect of waiving compliance with the Minnesota franchise laws or any rule or order thereunder is void).

V. Size Matters: Alternate Methods of Distribution for Craft Brewers

Although franchise laws apply to all traditional franchise relationships, beer distribution relationship statutes, which interestingly enough are sometimes referred to as franchise laws or acts,[51] generally do not apply to craft brewers producing small amounts of beer annually. States recognize that craft brewers are simply too small to exert much control over the marketplace. Most states exempt craft brewers, or microbreweries, from complying with the three-tier system of distribution altogether and often allow them to self-distribute beer in the state where their brewery facilities are based until they produce a certain volume of beer each year. In Washington, in-state brewers producing less than 200,000 barrels of malt liquor[52] annually are excluded from the definition of a supplier[53] and thus are not required to distribute their products in the state through distributors. Indiana allows brewers that produce less than 30,000 gallons in the state to self-distribute.[54]

Because of their size, however, craft brewers struggle to find distributors willing to distribute their products, particularly outside of their home states. However, in light of the prevalence of beer in American culture, it is no surprise that hundreds of new craft breweries, all of which are looking to level the playing field with larger brewers and distributors, have opened throughout the country within the past decade.[55]

An alternative channel of distribution for craft breweries' products is the Internet. However, the direct shipment of beer is an area of beer distribution law that is in flux. Vermont, for example, just passed Senate Bill 61 in June 2013 and now permits licensed in-state brewers and out-of-state brewers holding a valid manufacturer's license in another state to obtain a consumer shipping license permitting them to ship "no more than 12 cases of malt beverages containing no more than 36 gallons of malt beverages to any one Vermont resident in any calendar year."[56] However, sixteen states[57] for-

51. Virginia's Beer Franchise Act, VA. CODE ANN. §§ 4.1-500–17; *see* N.M. STAT. ANN. §§ 60-8A-7–11 (distributors are sometimes referred to as franchisees).

52. The definition of beer varies somewhat among the states. Many states, including Washington, utilize the broader, more inclusive term "malt liquor" or "malt beverage" instead of beer to capture the colloquial terms for beer products. Washington law defines "malt liquor" to mean "any beverage such as beer, ale, lager beer, stout, and porter obtained by the alcoholic fermentation of an infusion or decoction of pure hops, or pure extract of hops and pure barley malt or other wholesome grain or cereal in pure water containing not more than eight percent of alcohol by weight, and not less than one-half of one percent of alcohol by volume." WASH. REV. CODE ANN. § 66.04.010(26) (West 2013).

53. WASH. REV. CODE ANN. § 19.126.020(26).

54. IND. CODE ANN. § 7.1-3-2-7 (West 2013).

55. Billy Broas, *The Ins and Outs of Shipping Beer*, billybrew.com, http://billybrew.com/the-ins-and-outs-of-shipping-beer (last visited Dec. 4, 2013).

56. Act Relating to Alcoholic Beverages, Vt. S.B. No. 61, Vt. 2013-2014 Legis. Sess. (to be codified at VT. STAT. ANN. tit. 7, § 66(d)(2)).

57. Alaska, Arkansas, Delaware, Hawaii, Kentucky, Massachusetts, Maine, Maryland, Montana, Mississippi, Oklahoma, Pennsylvania, South Dakota, Texas, Utah, and West Virginia.

bid the direct shipment of beer to their residents. Those that do permit direct shipment typically require the shipper to be licensed as a brewer, distributor, or retailer in its state of origin and to obtain a direct shipper permit in each state where it wants to ship its products before shipping into their states.[58] Further complicating matters, shipping beer through the U.S. Postal Service is illegal; DHL refuses to ship beer per company policy; and Federal Express and United Parcel Service typically only ship for properly licensed shippers (those holding a valid brewer, wholesaler, retailer license, etc.) on a contract basis. In addition, some states have alcohol content restrictions or limit the amount of beer each resident may purchase on a monthly or annual basis. Not surprisingly, large brewers and distributors tend to oppose direct shipping because it poses a threat to the protections they enjoy under the three-tier system of distribution. They do, however make several valid points and spotlight the concern that direct shipping makes it much more difficult to police the illegal sale of alcohol to minors. Although the direct shipment of beer represents a potential sea-change for the beer distribution industry, this area of beer distribution law needs to develop a bit more to catch up with the times.

VI. Conclusion

Although beer distributorship arrangements are distinctly different from traditional franchise arrangements, it is clear there are certain commonalities. Clearly the three-tier system of beer distribution can trace its origins to the Prohibition Era and the Twenty-First Amendment, but modern beer laws governing beer distribution relationships between brewers and distributors have been patterned after franchise relationships laws. After all, brewers resemble franchisors in that they tend to hold a lion's share of the power in the beer distribution business relationship. Accordingly, we can expect more and more states to pass relationship laws aimed at further balancing power in favor of distributors, as we continue to see in franchising, and to require good faith dealings between the parties in each of these contractual arrangements. Considering that trend and the complexity of and differences among these statutes, it is easy to see why expert legal advice from an attorney specializing in this area of the law is essential at every step for those doing business in the beer distribution industry or in franchising.

58. *Direct Ship Permit*, New Hampshire Liquor Commission, http://www.nh.gov/liquor/direct_ship_permit.shtml (effective Jan. 11, 2012).