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FEDERAL TRADE COMMISSION
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COMMISSION AUTHORIZED

February 20, 1989

The Honorable Tom Alley
Michigan House of Representatives
State Capitol Building
Lansing, Michigan 48913

Dear Representative Alley:

The staff of the Federal Trade Commission's Cleveland Regional Office and Bureau of Competition are pleased to respond to your letter of November 16, 1989, requesting our comments on House Bill 5236.¹ This bill would amend existing Michigan law by allowing beer manufacturers to sell beer at retail in limited instances.² If passed, the bill would tend to provide consumers with a wider choice of specialty beers and to permit more efficient forms of distribution. For these reasons we believe that passage of the bill would enhance competition.

INTEREST AND EXPERIENCE OF THE FEDERAL TRADE COMMISSION STAFF.

Congress has charged the Federal Trade Commission with enforcing the nation's antitrust and consumer protection laws.³ The Commission is responsible for protecting consumers from unfair methods of competition and from unfair or deceptive acts or practices. In discharging this responsibility, the Commission staff has gained substantial experience in analyzing the impact of various restraints on competition. Pursuant to the Federal Trade Commission Act, the Commission staff also submits comments to other governmental bodies, upon request, to help them assess the competitive and consumer welfare implications of pending issues.

¹ These comments are the views of the staff of the Cleveland Regional Office and the Bureau of Competition. They are not necessarily the views of the Commission or any individual Commissioner.

² H.B. 5236 amends Sections 436.19, 436.24 and 436.31a of the Michigan Compiled Laws and adds Section 31b.

³ See 15 U.S.C. §§ 41 *et seq.*

The Commission staff has been specifically involved during recent years in competition issues affecting the distribution of alcoholic beverages.⁴ Recent staff comments have addressed regulation of the distribution and sale of wine coolers, liquor, beer, wine, and other alcoholic beverages.⁵

MICHIGAN'S PRESENT REGULATORY SCHEME.

The Michigan Liquor Control Act⁶ requires strict separation of the manufacture, wholesale distribution, and retail sale in the beer industry. The Act requires that beer manufacturers give wholesale distributors exclusive territories, and it prohibits them from terminating a wholesale distributor except for sufficient cause, such as loss of license, insolvency, or a felony conviction. This regulatory scheme is enforced by the Michigan Liquor Control Commission.

Under the current law the only type of license a Michigan beer manufacturer may hold is a brewery license.⁷ Brewers are prohibited by the Act from selling beer at retail and from selling directly to retailers. All cross-tier interests are strictly prohibited.

⁴ We recognize the important role played by the state in promoting the well being of its citizens and do not contend that a state should not regulate the sale of alcoholic beverages to promote temperance. Our comments are intended to address only the economic ramifications of the distribution regulations on the competitive marketplace. In this regard, we note that there may be means to promote temperance that do not limit the benefits of competition. For example, one alternative method of promoting temperance that might not have an adverse effect on competition would involve using tax revenues from the sale of alcoholic beverages for educational programs, such as alcohol abuse prevention programs.

⁵ See e.g., Comments of the Federal Trade Commission's Bureau of Competition, Consumer Protection, and Economics on the Maryland Wine Cooler Fair Dealing Act (Mar. 11, 1987); Comments of the Federal Trade Commission's Bureau of Competition, Consumer Protection, and Economics on the California Beer Distribution Bill, S.B. No. 1211 (Jul. 2, 1985); Malt Beverage Interbrand Competition Act: Hearings on S. 1215 Before the Senate Comm. on the Judiciary, 97th Cong., 2nd Sess. 266-90 (1982) (oral and written statements).

⁶ Mich. Comp. Laws Ann. § 436.19 (West 1978) *et seq.*

⁷ Mich. Comp. Laws Ann. § 436.19(1)(b) (West 1978).

THE PROPOSED LEGISLATION - HOUSE BILL 5236.

Under proposed House Bill 5236 beer manufacturers would be permitted to sell beer at retail in limited circumstances. The extent of the permissible sales would vary depending on the size of the manufacturer.

Under the proposed bill, large beer manufacturers, which produce more than 10,000 barrels annually, would continue to operate under brewery licenses. These licenses would continue to confine such firms primarily to manufacturing, but would also allow the brewer to operate a single retail establishment where its own beer may be sold. This establishment may be located on the premises of the brewery or at another location approved by the Michigan Liquor Control Commission.

The bill would also introduce a new class of "brewery public house" licenses, which could be obtained only by small brewers that produce no more than 10,000 barrels of beer annually. Holders of these licenses could manufacture and sell beer at retail on the licensed premises. In addition, the brewery public houses could act as their own wholesalers for sales to certain types of off-premises outlets.⁸

EFFECTS OF HOUSE BILL 5236 ON COMPETITION AND CONSUMER WELFARE.

Enactment of House Bill 5236 may tend to produce a wider choice of specialty beers and more efficient channels of distribution. The first and perhaps the most important effect of the proposed bill could be an increase in the number and variety of beers that are available to consumers. The current statutory plan deters the operation of small breweries that may not be able to support the administrative overhead and the transportation costs involved in conducting business through independent wholesalers and retailers. The plan contemplated by the new bill, by allowing a small integrated operation to brew beer and sell it through a pub located under the same roof, may, however, enable such a business to lower overhead costs and operate profitably. These businesses may be especially well suited to producing local or specialty beers.⁹ Faced with the new challenge from the micro-breweries, the large beer manufacturers may respond by offering new lines or specialty beers of their own. The bill, therefore, may result in a greater variety of choices in the marketplace.

⁸ The licensee may sell to "specially designated merchants," and can itself be licensed as a "specially designated merchant." A specially designated merchant may sell beer or wine for consumption off the premises only, but not at wholesale.

⁹ This effect has already become apparent in a number of areas. See "New Kinds of Beer to Tap a Flat Market," *Wall Street Journal*, April 20, 1989, at B-1.

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Another effect of House Bill 5236 may be some enhanced efficiency in beer distribution systems. In general, a distribution system is most likely to be efficient when it is designed by the participants in the distribution process. The manufacturer in particular has an interest in ensuring that its product reaches consumers as efficiently as possible, since unnecessary costs in the distribution system will have the effect of depressing consumer demand. A statutory system that constrains a manufacturer's choices may therefore produce adverse effects. The current state laws are quite rigid in excluding brewers from wholesale and retail functions. The proposed new law would loosen these restrictions to some extent, particularly in the case of "brewery public houses" that are permitted to take on wholesale as well as in-house retail functions. The proposed bill, therefore, may have at least a modest beneficial effect on industry efficiency.

CONCLUSION.

The enactment of House Bill 5236 would allow beer manufacturers to begin responding more flexibly to consumer demands. As part of the process, Michigan's brewers will become more able and inclined to offer specialty brands and to streamline their distribution systems. We believe that the bill, therefore, would enhance competition.

Sincerely,



Mark D. Kindt
Regional Director
Cleveland Regional Office