REASSESSING AMERICA'S REGULATION OF THE ALCOHOL BEVERAGE INDUSTRY'S TRADE PRACTICES

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Trade associations across the American alcohol industry are asking the U.S. Alcohol and Tobacco Tax and Trade Bureau (TTB) to extend the opportunity for public comment regarding the agency's proposed review and possible amendment of trade practice regulations related to the Federal Alcohol Administration Act's exclusive outlet, tied house, commercial bribery, and consignment sales prohibitions. In a joint letter dated December 19, 2022, eight alcohol industry trade associations requested that TTB authorize a 90-day extension to the Notice & Comment period associated with the agency's Notice 216 **– "Consideration of Updates to Trade Practice Regulations**." Signators to the extension request included representatives of all three segments and all three tiers of the industry:

- **BEER**: The Beer Institute (BI) and the National Beer Wholesalers Association (NBWA);
- **WINE**: The Wine Institute, Wine America, and the Wine and Spirits Wholesalers Association (WSWA);
- **SPIRITS**: The Distilled Spirits Council of the United States (DISCUS) and The American Distilled Spirits Alliance

American Beverage Licensees, a trade association for retailers of alcohol beverages, also joined the request.[1]

Currently, comments to the proposed regulations must be received on or before **March 9, 2023**. If the trade associations' extension request is granted, an extended comment period would run to **June 7, 2023**. Whether TTB extends this comment period or not, there will be other opportunities for public comment. By law, the agency must consider all submitted comments and respond to them when proposing draft rules.

[1] Two leading trade associations representing craft producers, the Brewers Association and the American Craft Spirits Association, did not join this request for extension.

WHY DELAY?

TTB's potential revisions to existing trade practice regulations resulted from President Joe Biden's Executive Order 14036 ("***Promoting Competition in the American Economy***"). In response to that executive order, the Department of the Treasury issued a report dated February 2022 ("***Competition in the Markets for Beer, Wine, and Spirits***"), focusing on what the government found were two distinct trends in America's alcohol beverage industry:

(i) the significant growth in the number of small and "craft" producers of beer, wine, and spirits; and

(ii) consolidation, particularly at the distribution and retail levels for beer, wine, and spirits and at the production level for beer.

Subsequent public comments related to the Treasury's report and TTB's Notice 216 raised questions about whether existing trade practice regulations[2] promulgated by TTB under the FAA

[2] Section 105 of the Federal Alcohol Administration Act (FAA Act) prohibits producers, wholesalers, and importers of distilled spirits, wine, or malt beverages (*i.e.*, industry members) from engaging in certain practices (collectively referred to as "trade practices") that threaten the independence of retailers and/or give the industry members an unfair advantage over their competitors. *See* 27 U.S.C. 205. Apart from labeling and advertising (27 U.S.C. 205(e) & (f)), which are outside the scope of this document, section 105's prohibited trade practices are:
A. *Exclusive outlet*. It is unlawful for any industry member to require, by agreement or otherwise, that any retailer purchase alcohol beverages from the industry member to the exclusion, in whole or in part, of alcohol beverages sold or offered for sale by other persons. *See* 27 U.S.C. 205(a).
B. *Tied house*. It is unlawful for any industry member to induce any retailer to purchase alcohol beverages from the industry member to the exclusion, in whole or in part, of alcohol beverages sold or offered for sale by others, through any of the following means: (1) by acquiring or holding any interest in any license with respect to the premises of the retailer; (2) by acquiring any interest in the real or personal property owned, occupied, or used by the retailer in the conduct of its business; (3) by furnishing, giving, renting, lending, or selling to the retailer, any equipment, fixtures, signs, supplies, money, services or other thing of value, subject to exceptions prescribed by regulations; (4) by paying or crediting the retailer for any advertising, display, or distribution service; (5) by guaranteeing any loan or the repayment of any financial obligation of the retailer; (6) by extending to the retailer credit for a period in excess of the credit period usual and customary to the industry for the particular class of transactions as prescribed by regulations; or (7) by requiring the retailer to take and dispose of a certain quota of any alcohol beverages. *See* 27 U.S.C. 205(b).
C. *Commercial bribery*. It is unlawful for any industry member to induce any retailer or wholesaler to purchase alcohol beverages from the industry member to the exclusion, in whole or in part, of alcohol beverages sold or offered for sale by others, though the following means: (1) by commercial bribery; or (2) by offering or giving any bonus, premium, or compensation to any officer, employee, or representative of the retailer or wholesaler. *See* 27 U.S.C. 205(c).
D. *Consignment sales*. It is unlawful for any industry member to sell, offer for sale, or contract to sell alcohol beverages to any retailer or wholesaler, or for any retailer or wholesaler to purchase, offer to purchase, or contract to purchase any alcohol beverages on consignment or under conditional sale or with the privilege of return or on any basis otherwise than a bona fide sale, or where any part of such transaction involves, directly or indirectly, the acquisition by such person, from the retailer or wholesaler, of other distilled spirits, wine, or malt beverages. *See* 27 U.S.C. 205(d).

Act[3] could be improved. However, as expected, the comments received by TTB express a broad, often divergent collection of viewpoints.

TTB's review of existing trade practice regulations is attracting serious attention because several suggested proposals seek to address current industry practices that have a material impact on how alcohol beverages are distributed in the United States.

TTB is seeking input on three "broad" issues, *i.e.:*

1. *Updating* and modernizing the existing trade practice rules.
2. Exploring whether the existing rules can be relaxed without resulting in exclusion or threatening retailer independence.
3. Determining how e-commerce and digital marketing practices can be regulated in the context of the industry's current trade practice framework.

However, the great concern generated from industry trade associations and their members is primarily attributable to the specific areas of review undertaken by the agency.

More specifically, TTB's proposed regulatory revisions are focused on 16 specific areas of interest, many of which are hot topics with wide-ranging applicability to the industry today:

1. *Category management.*[4]
2. *Shelf plans.*[5]
3. *Slotting allowances (slotting fee) arrangements.*[6]

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[3] TTB has promulgated regulations at 27 CFR part 6 ("**Tied-House**") specifying the practices that are means to induce under section 105(b) of the FAA Act, criteria for determining whether a practice is a violation of section 105(b) of the FAA Act, and exceptions to section 105(b)(3) of the FAA Act. TTB has promulgated regulations at 27 CFR part 8 ("**Exclusive Outlets**") specifying arrangements which are exclusive outlets under section 105(a) of the FAA Act and criteria for determining whether a practice is a violation of section 105(a) of the FAA Act. TTB has promulgated regulations at 27 CFR part 10 ("**Commercial Bribery**") specifying practices which may result in violations of section 105(c) of the FAA Act and criteria for determining whether a practice is a violation of section 105(c) of the FAA Act. TTB has promulgated regulations at 27 CFR part 11 ("**Consignment Sales**") specifying arrangements which are consignment sales under section 105(d) of the FAA Act and containing guidelines concerning returns or exchanges of distilled spirits, wine and malt beverages from a retailer or wholesaler.

[4] The Treasury Report and comments received by TTB in response to its request for input from the public have raised concerns about the threat that category management activities pose to retailer independence. One specific concern is that industry members, acting as category managers or captains for retailers, are either making the buying decisions for retailers or strongly influencing the retailers' buying decisions in a way that threatens retailer independence.

[5] TTB is contemplating the removal of the tied-house exception which allows industry members to provide retailers with shelf plans and shelf schematics. *See* 27 CFR 6.99(b). Concerns that providing shelf plans and shelf schematics has become a practice that places or has the potential to place retailer independence at risk gave rise to the agency's issuance of TTB Ruling 2016-1 on February 11, 2016.

[6] TTB regulations provide that paying or crediting a retailer for any advertising, display, or distribution service is an inducement. Comments received by TTB have identified slotting fees as a major issue in the marketplace; however, TTB regulations do not expressly define slotting fees. Consequently, TTB is considering updating the trade practice regulations to include a definition of slotting fees, and, specifically, the extent to which such a definition should

4. *Interest in a retail license or property.*[7]
5. *Third-party companies.*[8]
6. *Consumer specialty items and point-of-sale advertising materials.*[9]
7. *Permissible credit payment terms.*[10]
8. *Consignment sales payment terms safe harbor.*[11]
9. *Definition of trade buyer.*[12]
10. *Private label arrangements.*[13]

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account for display space in the retail premises (*e.g.*, shelves, designated high-visibility areas behind the bar, tap lines, well/rail placement, prominent placement on menus, or in featured drinks) as well as virtual display space (*e.g.*, digital retail storefront, associated digital ad campaigns where products may be purchased online). TTB also is assessing whether the slotting fee definition should include free or subsidized equipment that is, by agreement or design, only able to display or dispense the furnishing industry member's products.

[7] TTB is deciding whether to amend the tied house regulations to address crowdfunding and/or minority interest in a retail license/property as being an interest that would not result in an inducement. TTB also is reviewing whether the agency should define a level of ownership interest that would not result in exclusion and, if so, what that interest should be.

[8] Although TTB's tied house regulations apply to inducements furnished directly, indirectly, or through an affiliate, there is industry confusion pertaining to inducements made through third party companies. TTB is considering whether to amend the regulations to better address such inducements and define the permissible limits of third party delivery/fulfillment services.

[9] Within certain limitations, TTB's tied house regulations allow industry members to provide retailers certain consumer specialty items and point of sale advertising. *See* 27 CFR 6.84. However, the agency has determined that some of these items, especially "alcohol beverage lists or menus," have been used to provide hidden inducements to retailers. Consequently, TTB is reviewing whether to update the list of specialty items and point of sale advertising materials allowed under the regulations to discourage their use for illicit purposes, and whether to place specific monetary caps on these items.

[10] Federal tied house regulations currently allow for a 30-day extension of credit for retailers that would not result in an inducement. *See* 27 CFR 6.65. TTB is considering whether to allow for longer payment terms for retailers, on the theory that flexible credit terms would mirror current commercial marketing and distribution practices without necessarily jeopardizing retailer independence.

[11] TTB recently issued TTB Industry Circular 2022-1, "*Payment Terms Under Consignment Sales Provisions*," announcing a safe-harbor for 30-day payment terms, which the circular deemed unlikely to result in a consignment sale arrangement. Now, TTB is considering whether it should amend the regulations to add specific safe harbor payment terms and, if so, what any such terms should be.

[12] The FAA Act defines a "trade buyer" as "any person who is a wholesaler or retailer." Similarly, TTB's commercial bribery and consignment sales regulations define a "trade buyer" as "any person who is a wholesaler or retailer of distilled spirits, wine or malt beverages." *See* 27 CFR 10.11 and 11.11. There has been some confusion about how such definitions apply to importers that wholesale (purchase for resale at wholesale) the products they import but are not required to obtain a separate wholesale basic permit pursuant to 27 U.S.C. 203(a)(2). TTB is assessing whether it should amend the regulations to clarify that trade buyers include persons engaged in wholesaling or retailing alcohol beverage products, regardless of permit status.

[13] TTB has received industry comments expressing concerns about private label arrangements and how some of those arrangements may run afoul of the TTB trade practice regulations. Private label arrangements may involve an industry member contracting with a retailer to produce products on the retailer's behalf creating the potential for exclusive outlet or tied house violations. Given the increased importance of branding and the rise of valuable trademarks and brand recognition associated with specific retailers, TTB is assessing how its tied house and/or exclusive outlet regulations should address private label arrangements.

11. *Brand sharing with retail establishments.*[14]
12. *Sponsorships.*[15]
13. *Activities which result in exclusion or place retailer independence at risk.*[16]
14. *Criteria for determining a risk to retailer independence.*[17]
15. *Third-party contracts.*[18]
16. *Sales competitions.*[19]

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[14] TTB is scrutinizing how some industry members have directly or indirectly entered into arrangements whereby retailers are permitted or required to use an industry member's brand name as part of the name of the retail establishment. TTB is considering whether it should amend the regulations to specifically address brand sharing arrangements.

[15] TTB has received comments from industry members expressing exclusionary concerns with sponsorships at ballparks, concert venues, and other events. Although many of these comments do not appear to reflect a complete understanding of the details underlying such business relationships, TTB nevertheless is considering whether to amend its regulations to clarify when the terms of a sponsorship may be exclusionary.

[16] Under existing federal tied house, exclusive outlet, and commercial bribery regulations (27 CFR parts 6, 8, and 10, respectively), an inducement or requirement to purchase an industry member's products violates the FAA Act if such activity resulted in exclusion. *See* 27 CFR 6.21, 8.21, and 10.21. TTB contends that exclusion occurs when: (i) a practice of the industry member, whether directly or indirectly, places (or has the potential to place) retailer (or trade buyer with respect to commercial bribery) independence at risk by means of a tie or link between the parties or any other means of industry member control over the retailer or trade buyer; and (ii) such practice results in the retailer or trade buyer purchasing less than it would have of a competitor's product. *See* 27 CFR 6.151, 8.51, and 10.51. The tied house and commercial bribery regulations specify certain practices deemed to place a retailer's or trade buyer's independence at risk. *See* 27 CFR 6.152 and 10.52. The exclusive outlet regulations specify certain practices that result in exclusion and other practices that do not result in exclusion. *See* 27 CFR 8.52 and 8.53. Now, TTB is considering how it might update the regulations with respect to which practices place or have the potential to place retailer independence at risk, as well as which activities would result in exclusion under these parts. TTB also is assessing whether it should clarify or alter the definition of exclusion in terms of "purchasing less" of a competitor's product, as provided in the regulations. *See, e.g.,*27 CFR 6.151(a)(2); 8.51(a)(2); 10.51(a)(2). For example, new retail establishments may have never purchased from competing industry members that did not induce or require such purchases. Should the regulations explicitly address that situation, and, if so, how? Likewise, in light of recent enforcement actions undertaken over the last two years, concerns have been raised about the need to modify existing regulations to establish and clarify levels of proof that would be deemed sufficient or insufficient to demonstrate exclusion.

[17] The federal tied house, exclusive outlet, and commercial bribery regulations provide specific criteria that indicate that trade practices other than those specifically listed in 27 CFR §§ 6.152, 8.52, 8.53, and 10.52, place retailer or trade buyer independence at risk. *See* 27 CFR 6.153, 8.54 and 10.54. As a result of recent enforcement actions, industry members are clamoring for TTB to amend its regulations to provide additional clarity as to when a trade practice jeopardizes the independence of a wholesaler or retailer.

[18] The federal exclusive outlet regulations provide that contracts between an industry member and retailer, which require the retailer to purchase products from that industry member and expressly restrict purchase of such products from another industry member, are practices which result in exclusion. *See* 27 CFR 8.52. Given the substantial increase in unlicensed third-party service providers and their relationships with licensees, especially retailers, TTB is examining the need to clarify how an industry member properly can contract with a third party, where the third party controls the retailer, and when such a relationship could result in exclusion.

[19] TTB has received numerous comments from industry members expressing concerns that larger industry members are engaging in commercial bribery activities by offering incentives, including, but not limited to, cash, airline tickets to tropical getaways, tickets to sporting events, flat screen televisions, and vacations for trade buyer sales representatives to push sales of the industry member's products. Current regulations provide that such inducements threaten trade buyer independence if provided to sales representatives in secret. TTB now is considering whether any such inducements threaten trade buyer independence regardless of whether they are provided in secret.

The scope of these specific areas of review is such that every aspect of the industry – all tiers and all segments – will be affected in some capacity should the suggested changes be implemented.

HOW TO PROCEED FORWARD

In their December 19th letter to TTB, the combined alcohol beverage industry trade associations observed that the agency's current trade practice reassessment was the "first meaningful opportunity to comment upon trade practice regulations in almost 30 years." Given the far-reaching consequences of some proposed regulatory revisions, industry members argue that an additional three months to conduct a detailed analysis were necessary to allow trade associations and their respective constituencies to collect, deliberate, and convey their collective input:

Many of the areas of interest—for example, how trade practice regulations could account for current digital marketplace realities—are complex, have developed significantly since the last trade practice regulatory update, and may require manifold responses from the Associations' respective memberships. Federal trade practice regulations can affect small, mid-size, and large producers differently. Given the importance and scope of the issues that Notice 216 addresses, the Associations will need substantial time to collect, deliberate, and convey all our members' collective input and ensure meaningful and comprehensive responses.
Trade practice isvital to every segment and every tier of America's alcohol beverage industry. In today's world, it is equally important to the growing number of unlicensed businesses that service the alcohol industry, including but not limited to those optimizing the use of e-commerce and digital marketing to expand the distribution and sale of alcohol beverages.

Given the importance of TTB's review, every interested party needs to participate in the public comment process. To make your voice heard, contact **TTB's Regulations and Rulings Division** via email using the Web form available at https://www.ttb.gov/contact-rrd or via telephone by calling **(202) 453-2265** to request copies of TTB's Notice of Proposed Rulemaking, its supporting materials, or the comments received in response. If you have any questions regarding how to comment or require more information regarding how proposed revisions to the existing federal trade practice regulations may impact your existing business, please contact **GrayRobinson's** **Nationwide Alcohol Industry Group** via telephone at **(866) 382-5132** or via email at beveragelaw@gray-robinson.com.

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