Case Nos. 22-2979, 22-3067

UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

MAJOR BRANDS, INC.,

Appellee/Cross-Appellant,

v.

MAST-JÄGERMEISTER US, LLC,

Appellant/Cross-Appellee, and

SOUTHERN GLAZER'S WINE & SPIRITS OF MISSOURI, LLC

Appellant/Cross-Appellee.

BRIEF OF *AMICI CURIAE* AMERICAN CRAFT SPIRITS ASSOCIATION; BREWERS ASSOCIATION; DISTILLED SPIRITS COUNCIL OF THE UNITED STATES; WINE INSTITUTE; AND MISSOURI CRAFT BREWERS GUILD IN SUPPORT OF APPELLANTS

Appeal from the United States District Court
for the Eastern District of Missouri, No. 4:18-cv-00423
Hon. Henry E. Autrey, United States District Judge

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IDENTITIES AND INTERESTS OF *AMICI*

Amici curiae are the American Craft Spirits Association; the Brewers Association; the Distilled Spirits Council of the United States; the Wine Institute; and the Missouri Craft Brewers Guild.[1] As the leading national trade associations for producers of distilled spirits, beer, and wine, *Amici* represent a broad spectrum of beverage alcohol producers, ranging from start-up craft producers to some of the largest food and beverage companies in the world. *Amici* and their members have a substantial interest in fostering robust competition that delivers lower prices and more diverse product offerings to American consumers. As described below, an unnecessarily expansive application of Missouri's franchise statute and similar laws in other States threatens the competitive marketplace that has made the American beverage alcohol industry the most dynamic in the world.

BACKGROUND

This case involves an alleged violation of Missouri's franchise statute. The franchise statute imposes a variety of regulations on the relationships between franchisors and franchisees. *See generally* Mo. Rev. Stat. §§ 407.400-407.420. Under the statute, a franchisor-franchisee relationship exists if two conditions are

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[1] Pursuant to Federal Rule of Appellate Procedure 29(4)(E), *Amici* certify that no party's counsel authored this brief in whole or in part, nor did any party or party's counsel contribute any money that was intended to fund preparing or submitting this brief.

satisfied: first, the franchisor must have granted a license to use its trade name or trademark to the franchisee; and second, there must be a "community of interest in the marketing of goods or services" between the franchisor and the franchisee. Mo. Rev. Stat. § 407.400(1). These threshold conditions apply regardless of the nature of the goods or services involved. *See id.*; *High Life Sales Co. v. Brown-Forman Corp.*, 823 S.W.2d 493, 500 (Mo. 1992) (explaining that the "general definition of 'franchise' appli[es] generally to all types of businesses").

If those two conditions are satisfied, then Missouri law imposes two sets of regulations on the franchise relationship, neither of which can be waived or modified by contract. *See* Mo. Rev. Stat. § 407.410.1; *High Life*, 823 S.W.2d at 499. The first of those applies to franchise relationships regardless of the industry involved. That generally applicable provision requires that a franchisor provide at least 90 days' notice before terminating or declining to renew a franchise agreement. Mo. Rev. Stat. § 407.405. The statute provides a private right of action for franchisees to seek compensatory damages in the event of a failure to provide the requisite notice. Mo. Rev. Stat. § 407.410.2.

Missouri law also imposes a second, more stringent set of regulations on the relationship between franchisors (*i.e.*, suppliers) and wholesale franchisees (*i.e.*, wholesalers) in the beverage alcohol industry. *See* Mo. Rev. Stat. § 407.413. The statute prohibits a supplier from terminating, declining to renew, or substantially altering a franchise agreement unless it acts for "good cause" and "in good faith." *Id.* Mo. Rev. Stat. § 407.413.2, 407.413.4. The statute defines "good cause" to include only three expressly enumerated reasons. Mo. Rev. Stat. § 407.413.5. In any litigation resulting from an alleged violation of the statute, the supplier bears the burden of establishing the existence of "good cause." Mo. Rev. Stat. § 407.413.2. The statute defines "good faith" to mean "the duty of each party to any franchise and all officers, employees or agents thereof to act in a fair and equitable manner towards each other." Mo. Rev. Stat. § 407.413.5. The statute provides a private right of action for wholesaler franchisees to seek compensatory damages for violations of the statute, as well as attorneys' fees. Mo. Rev. Stat. § 407.413.3.

Missouri's franchise laws are not unique. A number of other States have enacted a variety of franchise-termination statutes. *See generally* Tracey A. Nicastro, Note, *How the Cookie Crumbles: The Good Cause Requirement for Terminating a Franchise Agreement*, 28 VAL. U. L. REV. 785 (1994) (collecting and discussing state franchise statutes). While these franchise-termination statutes vary between jurisdictions, their stated justifications all generally rest on the perception "that there is a disparity in size between the franchisee and franchisor that gives the franchisor an unfair bargaining position." James A. Brickley, Frederick H. Dark, & Michael S. Weisbach, *The Economic Effects of Franchise Termination Laws*, 34 J. L. & ECON. 101, 115 n.24 (1991); *see also, e.g.*, Wis. Stat. § 135.025(2)(b) (explaining that a similar Wisconsin statute was enacted "[t]o protect [franchisees] against unfair treatment by [franchisors], who inherently have superior economic power and superior bargaining power in the negotiation[s]").[2]

Both empirical research and economic theory provide substantial reason to doubt this premise. For example, a large-scale analysis of the duration of franchise contracts found that the available data were inconsistent with the view that franchisors wield undue bargaining power in their relationships with franchisees. James A. Brickley, Sanjog Misra, & R. Lawrence Van Horn, *Contract Duration: Evidence from Franchising*, 49 J. L. & ECON. 173 (2006). In addition, economic theory indicates that opportunistic or exploitative conduct by franchisors would frequently *harm* their own businesses. *See id.* at 178; Richard A. Epstein, *Unconscionability: A Critical Reappraisal*, 18 J. L. & ECON. 293, 314-15 (1975); Paul H. Rubin, *The Theory of the Firm and the Structure of the Franchise Contract*, 21 J. L. & ECON. 224, 231-32 (1978).

Moreover, changing market conditions over the decades since the franchise statutes were enacted has further eroded any merit that the justifications underlying

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[2] Looking at these regulations from a public choice theory perspective, there is substantial reason to believe that many franchise statutes "were enacted to benefit [franchisees] rather than serve the public interest." Francine Lafontaine & Fiona Scott Morton, *State Franchise Laws, Dealer Terminations, and the Auto Crisis*, 24 J. ECON. PERSPECTIVES 233, 243 (2010) (noting that franchise statutes may act as "a wealth transfer that benefits [franchisees] at the expense of consumers").

the statutes may once have had, particularly in the beverage alcohol industry. When Missouri first enacted its franchise statutes in the mid-1970s, there were far fewer suppliers than wholesalers, and many wholesalers were small, regional, family-owned businesses. *See* Steve Hindy, *Free Craft Beer!*, N.Y. TIMES (Mar. 30, 2014) (noting that "there were fewer than 50 brewing companies in America and 5,000 distributors" in the 1970s, compared to "more than 2,700 breweries, and fewer than 1,000 viable distributors" today).[3] However, the past several decades have seen a notable trend toward consolidation among wholesalers. *See, e.g.*, GLEN WHITMAN, STRANGE BREW: GOVERNMENT AND ALCOHOL MONOPOLY 19-20 (2003) (noting that "nationwide, the wholesaler sector has experienced substantial consolidation over the last two decades").[4] Alongside this consolidation, there has also been a shift in wholesalers "from small family-owned operations to much larger corporations." Andrew Tamayo, *What's Brewing in the Old North State: An Analysis of the Beer Distribution Laws Regulating North Carolina's Craft Breweries*, 88 N.C. L. REV. 2198, 2218 (2010).

As wholesalers have amassed greater economic power through consolidation, suppliers have been proliferating, particularly small suppliers and new market

[3] Available online at https://www.nytimes.com/2014/03/30/opinion/sunday/free-craft-beer.html.

[4] Indeed, shortly after the trial in this case, Major Brands announced that it had been acquired by Breakthru Beverage Group, one of the largest alcohol wholesalers in North America.

entrants. *See, e.g.*, Steve Hindy, *Free Craft Beer!*, *supra*; RICHARD MENDELSON, FROM DEMON TO DARLING: A LEGAL HISTORY OF WINE IN AMERICA 177 (2009) (describing how "[t]he number of small wineries has increased dramatically"). These parallel trends—consolidation among wholesalers and proliferating competition among suppliers—further undermine the notion that suppliers systematically possess undue bargaining power over wholesalers. Indeed, in many cases, wholesalers wield far greater economic power than the suppliers whose products they distribute.

Franchise termination laws do not merely rest on dubious assumptions. As described in the brief below, if expansively applied, those laws also substantially undermine competition, thereby harming consumers and the economy as a whole. For this reason, for more than 35 years, the Federal Trade Commission ("FTC") has aggressively and consistently opposed the expansion of franchise regulation at the state level, particularly in the beverage alcohol industry. *See, e.g.*, Joint Submission of FTC and U.S. Department of Justice to Hon. Jim Wood (Mar. 20, 2020) ("2020 Joint Submission") (opposing the enactment of a proposed California statute similar to Missouri's liquor franchise statute);[5] FTC Submission to Hon. Alice H. Peisch

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[5] Available online at https://www.ftc.gov/system/files/documents/advocacy_documents/joint-comment-ftc-staff-doj-antitrust-division-staff-california-state-assembly-concerning-california/v200008_california_beer_distribution_advocacy_2020.pdf.

(May 16, 2011) (opposing the enactment of a malt beverage franchise statute in Massachusetts); FTC Submission to Hon. Bill Seitz (Dec. 12, 2005) (opposing the enactment of a wine franchise statute in Ohio); FTC Submission to Hon. Wesley Chesbro (Aug. 24, 2005) (opposing the enactment of a beer franchise statute in California); FTC Submission to Hon. Dan Cronin (Mar. 31, 1999) (opposing enactment of franchise protection provisions in wine and spirits industries in Illinois); FTC Submission to Hon. Juanita Miller (Mar. 11, 1987) (opposing the enactment of a wine cooler franchise statute in Maryland); FTC Submission to the Council of the District of Columbia (Aug. 29, 1986) (opposing the enactment of a beverage alcohol franchise statute in the District of Columbia); *see also* James C. Cooper & Joshua D. Wright, *State Regulation of Alcohol Distribution: The Effects of Post and Hold Laws on Consumption and Social Harm*, FTC Working Paper No. 304 (Sept. 2010).

The FTC is not alone among federal agencies that have opposed the expansion of franchise regulations based on their anticompetitive effects. The Antitrust Division of the U.S. Department of Justice ("DOJ") joined the FTC in its 2020 opposition to a proposed California law that would have regulated the beer industry much as Missouri's franchise statute regulates the entire beverage alcohol industry. *See* 2020 Joint Submission.

In addition, in February 2022, the U.S. Department of the Treasury issued a report addressing barriers to competition in the beverage alcohol industry. *See* U.S. Department of Treasury, *Competition in the Markets for Beer, Wine, and Spirits* (Feb. 2022) ("2022 Treasury Report").[6] In that report, the Treasury Department found that state franchise laws—particularly those that limit franchise termination—substantially hinder competition in the beverage alcohol industry. *See id.* at 12-14. The Treasury Department issued its report pursuant to Executive Order 14036, which called for a whole-of-government approach to enhancing market competition in the U.S. economy. *See generally* Executive Order 14036, *Executive Order on Promoting Competition in the American Economy* (July 9, 2021). That Executive Order specifically prioritized "protect[ing] the vibrancy of the American markets for beer, wine, and spirits, and . . . improv[ing] market access for smaller, independent, and new operations." *Id.*, § 5(j).

ARGUMENT

The conclusion that Major Brands constitutes a franchisee impermissibly stretches the Missouri franchise statute far beyond what either the statutory text or the underlying statutory purpose permits. The district court's construction of the statute conflicts with the plain statutory text by rendering the "community of

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[6] Available online at https://home.treasury.gov/system/files/136/Competition-Report.pdf.

interest" requirement effectively superfluous, transforming almost every wholesaler into a franchisee. Moreover, this result fails to advance the purpose of the statute, which was intended to apply only to situations in which a franchisor could exercise undue bargaining power in its relationship with its franchisee. The district court's approach is also out of step with cases from other jurisdictions, which have generally rejected franchise claims in situations where a supplier's products constitute a small portion of the wholesaler's business.

The Court should be especially reluctant to endorse an expansive, atextual interpretation of the franchise statute in light of the anticompetitive effects of franchise-termination laws. "[O]ur national policy favoring competition" constitutes a deeply rooted legal principle that is part of the backdrop against which all legislation is enacted. *FTC v. Phoebe Putney Health Sys., Inc.*, 568 U.S. 216, 234 (2013). Pro-competition policy does not override clear statutory text that dictates an anticompetitive result; however, it *does* counsel against interpreting a statute broadly in a way that conflicts with our nation's fundamental commitment to competition in the private sector. *See id.* (construing a state statute narrowly to avoid an outcome that would restrict market competition). Particularly when applied beyond the narrow scope reflected in the statutory text, Missouri's franchise statute and similar laws from other jurisdictions pose a substantial risk to competition.

Under a proper interpretation of the Missouri franchise statute, Major Brands does not constitute a franchisee.

I. The District Court's Holding Eviscerates the Franchise Statute's "Community of Interest" Requirement and Fails to Advance the Statute's Underlying Purpose.

Franchise laws like Missouri's rest principally on the premise "that there is a disparity in size between the franchisee and franchisor that gives the franchisor an unfair bargaining position." Brickley, Dark, & Weisbach, *The Economic Effects of Franchise Termination Laws*, 34 J. L. & ECON. at 115 n.24; *see also High Life*, 823 S.W.2d at 498 (noting that the statute was "designed to regulate the marketplace to the advantage of those traditionally thought to have unequal bargaining power" (quotation omitted)). The Missouri franchise statute incorporates this rationale into the statutory definition of "franchise," which requires that there be "a community of interest in the marketing of goods or services" between the franchisor and the franchisee. Mo. Rev. Stat. § 407.400(1). In interpreting the Missouri franchise statute, courts have looked to case law interpreting New Jersey's substantially similar statute. *See Missouri Beverage Co. v. Shelton Bros., Inc.*, 669 F.3d 873, 878-79 (8th Cir. 2012). As the Third Circuit recently explained in the context of the New Jersey statute, "[t]he lynchpin of the community of interest element—and the [franchise statute] more generally—is the vulnerability of the purported franchisee."

Golden Fortune Import & Export Corp. v. Mei-Xin Ltd., Nos. 22-1710 & 22-1885, 2022 WL 3536494, at *3 (3d Cir. Aug. 5, 2022).

The factors that support the existence of a community of interest reflect this focus on the potential disparity in power that gives rise to a franchisee's vulnerability. Courts generally look to whether the purported franchisee is "subject to the whim, direction and control of a more powerful entity whose withdrawal from the relationship would shock a court's sense of equity." *Colt Indus. Inc. v. Fidelco Pump & Compressor Corp.*, 844 F.2d 117, 120-21 (3d Cir. 1988). Courts also consider the purported franchisee's "economic dependence on" the franchisor, any "disparity in bargaining power," and the risk that the termination of the relationship may deprive the franchisee of "franchise-specific investment[s]." *Cassidy Podell Lynch, Inc. v. SnyderGeneral Corp.*, 944 F.2d 1131, 1140 (3d Cir. 1991); *see also Shelton Bros.*, 669 F.3d at 879-80. Each of these considerations points back to the fundamental concern regarding a disparity in economic power between the franchisor and the franchisee.

Here, the evidence presented at trial did not establish that Major Brands was a vulnerable franchisee subject to the opportunistic conduct of a much larger franchisor. Among other things, Jägermeister products never accounted for more than 2% of Major Brands' sales and that Major Brands made only minimal "franchise-specific investments," including the salary of a single employee who focused on selling Jägermeister products, and who continues to work at Major Brands even after the termination selling other products.

Treating Major Brands as a franchisee eviscerates the statutory requirement that a franchisor and franchisee share "a community of interest in the marketing of goods or services." Mo. Rev. Stat. § 407.400(1). The district court's holding creates a situation in which almost *any* sales of a supplier's product by a reseller potentially establish a franchise relationship, even if those sales account for an extremely small portion of the reseller's revenues and the reseller would not lose substantial investments if the relationship were terminated. Almost any resale relationship would potentially constitute a "franchise" under such a rule. A small local supplier like a craft brewery could constitute the "franchisor" of a large wholesaler whose revenues and economic power far outstrip the purported franchisor's. Similarly, under the district court's approach, many grocery stores and convenience stores could argue persuasively that they constitute franchisees of suppliers like Pepsi (whose portfolio includes a wide range of food and beverage products).[7]

The Missouri General Assembly plainly did not intend that result. Instead, the Missouri franchise statute imposes the "community of interest" standard in order to distinguish between run-of-the-mill resale relationships and situations in which a franchisee is genuinely economically dependent on a franchisor. Mo. Rev. Stat.

[7] *See* https://www.pepsico.com/our-brands/creating-smiles/our-products.

§ 407.400(1). The district court's interpretation effectively renders this statutory requirement superfluous. "This result would defy the norm of statutory construction that every word, clause, and provision of a statute must have effect." *St. Louis Effort for AIDS v. Huff*, 782 F.3d 1016, 1025 (8th Cir. 2015) (quoting *Civil Serv. Comm'n of St. Louis v. Members of Bd. of Aldermen of St. Louis*, 92 S.W.3d 785, 788 (Mo. 2003)).

Treating Major Brands as a franchisee also goes far beyond the narrow purposes underlying the Missouri franchise law and conflicts with common-sense understandings of what constitutes a "franchise." As noted above, Jägermeister products accounted for an extremely small portion of Major Brands' sales. *Compare Golden Fortune*, 2022 WL 3536494, at *4 (finding no community of interest where supplier's products accounted for 8.6% of distributor's revenues); *Kenosha Liquor Co. v. Heublein, Inc.*, 895 F.2d 418, 419 (7th Cir. 1990) (cited approvingly in *Shelton Bros.*) (holding that no franchise relationship existed where supplier's products accounted for 5.8% of wholesaler's revenues). The remaining 98% of Major Brands' revenues came from other products, many of which *compete directly against* Jägermeister products. There is no "community of interest" between a supplier and a wholesaler when that wholesaler is actively selling products that directly take sales away from the supplier.[8] This is a far cry from situations that ordinarily would be viewed as franchises, such as a McDonald's franchise that operates exclusively under the McDonald's trade name; sells exclusively McDonald's products; and is subject to pervasive control by its franchisor.

This dynamic is particularly pronounced in the case of Major Brands. In a series of lawsuits over the past several years, Major Brands has contended that it is a franchisee of a number of beverage alcohol suppliers, all of whom compete with Jägermeister. *See, e.g.*, *Bacardi U.S.A., Inc. v. Major Brands, Inc.*, No. 13-cv-20791 (S.D. Fla.) (Major Brands asserting counterclaim contending that it was a franchisee of Bacardi); *Pernod Ricard USA, LLC v. Major Brands, Inc.*, No. 4:13-cv-64 (E.D. Mo.) (Major Brands asserting counterclaim contending that it was a franchisee of Pernod Ricard); *Major Brands, Inc. v. Luxco, Inc.*, No. 1322-CC00538 (Circuit Court of St. Louis City, Missouri) (Major Brands contending that it was a franchisee of Luxco); *Major Brands, Inc. v. Diageo North Am., Inc.*, No. 1322-CC00534) (Circuit Court of St. Louis City, Missouri) (Major Brands contending that it was a franchisee of Diageo); *Major Brands, Inc. v. Moet Hennessy USA, Inc.*, No. 4:06-cv-582 (E.D. Mo.) (Major Brands contending that it was a franchisee of Moet

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[8] In some cases, this dynamic may be even more extreme. Wholesale distribution contracts often contain requirements that a wholesaler provide preferential treatment to a particular supplier. It would be especially implausible to contend that a wholesaler constitutes a franchisee of a supplier when the wholesaler is contractually bound to provide preferential treatment to products that compete with the supplier's.

Hennessy). It is difficult to understand how Major Brands could simultaneously be economically dependent upon and subject to the whims of all of these suppliers. And given the direct competition among these suppliers, it is also difficult to understand how Major Brands could simultaneously share a "community of interest" with all of them. Only an interpretation of the franchise statute that is unmoored from both the statutory text and the underlying statutory purpose could yield such a result.

As described below, the adverse consequences of the district court's atextual, outlier interpretation of the franchise statute do not stop with suppliers like Jägermeister. Instead, an impermissibly expansive application of the franchise statute imposes substantial anticompetitive effects that harm consumers and the wider economy. Moreover, because the "community of interest" standard applies regardless of the industry involved, these anticompetitive effects could apply in every sector of the economy, increasing consumer prices, reducing output, and suppressing innovation. Neither the text nor the legislative purposes of the Missouri franchise statute dictate these unreasonable and economically harmful results. The Court should decline to adopt the district court's expansive application of the Missouri franchise law.

II. In Light of the Anticompetitive Effects of the Missouri Franchise Law, the Court Should Not Apply the Statute Expansively.

As described below, a broad application of Missouri's franchise statute substantially undermines competition. Thus, the Court should not stretch the statute's "community of interest" requirement in a manner that unnecessarily imposes those substantial anticompetitive effects. *See Phoebe Putney*, 568 U.S. at 234.

A. Franchise termination regulations stifle competition among wholesalers.

Franchise termination regulations—particularly those requiring "good cause" to terminate a franchise relationship—substantially reduce competition among actual and potential wholesalers. As the FTC and DOJ explained in connection with a substantially similar proposal in California, such regulatory provisions "make it difficult—if not impossible—for a [supplier] to terminate a wholesale contract in order to switch to a competing wholesaler." 2020 Joint Submission, at 8-9; *see also* 2022 Treasury Report at 13 ("Requiring proof of 'good cause' reduces this competitive pressure by making it very challenging for suppliers to leave their current distributors."). For one thing, "good cause" only encompasses certain specific forms of misconduct by a wholesaler. *See* Mo. Rev. Stat. § 407.413.5. A franchisor cannot move to a new wholesaler simply because the new wholesaler would charge lower prices or provide better services than the incumbent. *Id.* "Those constraints reduce competitive dynamism, leading to higher consumer prices." 2022 Treasury Report at 13.

Moreover, the good-cause requirement often deters contract termination or non-renewal even when good cause exists. A supplier bears the burden of establishing that good cause exists. Mo. Rev. Stat. § 407.413.2. Moreover, the standards for establishing good cause are relatively amorphous. For example, it generally is not enough that the wholesaler has breached a material provision of a franchise agreement. Instead, a supplier must establish that the wholesaler failed "to comply substantially" with a contractual provision that is "both essential and reasonable." Mo. Rev. Stat. § 407.413.5(1). Similarly, a supplier cannot terminate a wholesaler merely because the latter engages in conduct that harms the reputation of the supplier. Instead, the franchisor must establish that the wholesaler "[u]se[d] bad faith or fail[ed] to observe reasonable commercial standards of fair dealing in the trade." Mo. Rev. Stat. § 407.413.5(2). In addition to establishing "good cause," a supplier must also prove that it acted "in good faith," which involves a vague requirement that the supplier "act in a fair and equitable manner." Mo. Rev. Stat. § 407.413.5.

Thus, even where a wholesaler has clearly failed to meet its contractual obligations or has engaged in conduct that clearly harms the supplier, a supplier may face both substantial litigation uncertainty and the prospect of significant legal fees if it terminates the relationship. These factors frequently deter suppliers from switching franchisees, even where good cause likely exists. *See* 2020 Joint Submission at 12; Epstein, *Unconscionability: A Critical Reappraisal*, 18 J. L. & ECON. at 314 ("If the franchise could be terminated only 'with cause,' [the franchisor's] settlement costs on termination are apt to be high no matter what the circumstances, for the franchisee could always litigate the matter. If those costs deter the franchisor from termination, he loses the benefits of a substitute franchisee, while being forced to suffer from the continued erosion of his good will.").

In a wholesaler market characterized by robust competition, current and potential wholesalers "would vie with each other to secure and maintain [suppliers'] business, competing on price, the range of services they offer, and the quality and consistency of their services." 2022 Treasury Report at 12. Key among these services, "[w]holesalers are responsible for storing and delivering [beverages] in a manner that maintains the [beverage's] quality." 2020 Joint Submission at 5. Competition based on price and service quality directly advance consumer welfare. *See, e.g.*, *Pool Water Products v. Olin Corp.*, 258 F.3d 1024, 1034 (9th Cir. 2001) ("Consumer welfare is maximized . . . when consumers are assured competitive price and quality." (quotation omitted)).

The barriers to switching wholesalers imposed by franchise-termination laws effectively eliminate the incentive to engage in such competition. With the knowledge that a supplier cannot readily terminate its existing franchise relationships, "new and existing wholesalers would have little incentive to compete to distribute [the supplier's] brands." 2020 Joint Submission at 9; *see also* 2022 Treasury Report at 14 (noting that franchise-termination laws make it "very difficult to recruit new producers from incumbent distributors, further diminishing competition among distributors"). By eliminating this incentive, franchise laws deprive consumers of the reduced prices and enhanced product quality that robust competition among wholesalers would offer. *See* 2022 Treasury Report at 13.

B. Franchise termination regulations distort competition among suppliers.

Franchise termination regulations do not merely disadvantage all suppliers in their ability to partner with the wholesaler of their choosing; they also harm competition at the supplier level. As reflected in the Treasury Report, "much of the producer-level competition concerns in the alcohol marketplace could in fact be viewed as a *distributor*-level problem." 2022 Treasury Report at 24 (quoting an industry respondent to a request for public comment). These laws shield wholesalers from the otherwise natural competitive pressures to provide the best service to launch and promote new brands. As a result, wholesale service efforts are often focused on high volume, incumbent brands, at the expense of new product lines, smaller suppliers, and new market entrants. *See* 2020 Joint Submission at 9. As described above, to terminate an existing franchise relationship, a supplier often faces either substantial litigation costs, substantial settlement costs, or both. Larger, more well-established suppliers generally can bear these legal and regulatory costs more easily than smaller competitors. 2022 Treasury Report at 14. For this reason, although franchise termination regulations place great cost and burden on all suppliers, they will be disproportionately felt by smaller and newer entrants.

Moreover, large suppliers also often possess greater ability to bear and mitigate the adverse effects of underperforming franchisees. With greater resources at their disposal, large suppliers generally are better positioned to engage in their own marketing efforts directly to customers. *See* 2020 Joint Submission at 9. These efforts blunt some of the adverse effects of a wholesaler that does not invest substantially in marketing the supplier's products, albeit at a substantial cost. Similarly, a well-resourced supplier with strong brand recognition may retain significant demand even if a franchisee does not actively market the products. In contrast, "smaller producers' ability to succeed may rely more heavily on [their franchisees'] marketing efforts than larger producers that may handle more of their own marketing and advertising." 2022 Treasury Report at 14.

These competitive distortions make it difficult for new suppliers and new products to enter the market. Those competitive harms are not merely theoretical. A recent study by an economist at DOJ found that, absent beer franchise laws, "there would have been approximately 3000 more breweries in the US in 2016—43% higher than observed—and craft beer production would have been 24% higher." Jacob Burgdorf, *Franchise Termination Laws, Craft Brewery Entry and Growth*, U.S. Dep't of Justice Antitrust Division Economic Analysis Group Working Paper 21-3 (Nov. 2021), at 2.[9]

Reducing competition from new products and supplier entrants does not merely undermine consumer welfare. It also directly conflicts with the policies underlying the franchise laws. As described above, the stated purpose of the franchise laws is to protect franchisees from what is perceived as the unfair economic power of franchisors. But reducing competition among suppliers *increases* the power of franchisors vis-à-vis franchisees. The Court should be especially hesitant to attribute an expansive interpretation to the franchise laws that undermines the stated purpose of the statute. *Cf. Feesers, Inc. v. Michael Foods, Inc.*, 591 F.3d 191, 198 (3d Cir. 2010) (collecting cases construing the Robinson-Patman Act to avoid results that conflict with the underlying policies of the antitrust laws).

C. Franchise termination regulations stifle innovation in suppliers' products and operations.

Franchise termination regulations may also deter suppliers from adopting innovative new products and business models. New products—particularly those that mark a major departure from existing options—often require particularly robust marketing, promotion, and consumer-education efforts. These efforts often must

[9] Available online at https://www.justice.gov/atr/page/file/1454331/download.

also be sustained; consumers will not necessarily understand the benefits of a new product and shift their preferences from existing products overnight.

For the reasons described above, however, franchise-termination laws substantially limit a supplier's ability to persuade wholesalers to aggressively promote new, innovative products. "[P]roducers—both well-established and new—may be less willing to invest in brand extensions or product developments that their distributors may not promote." 2022 Treasury Report at 14. Moreover, franchise-termination laws have the practical effect of tethering any size of supplier to the first wholesaler to carry its products. If an innovative new product takes off in popularity, outstripping its original wholesaler's ability to promote and distribute the product, the supplier nevertheless cannot replace the wholesaler with another option that is more up to the task or willing to offer better terms and service.

Franchise-termination laws also impair suppliers' ability to adjust their business operations and practices to account for evolving economic realities. For example, one study of franchise relationships in the automotive industry found that franchise-termination limitations contributed to the crisis faced by the "Big Three" U.S. auto manufacturers, ultimately leading to an unprecedented taxpayer bailout of the companies. *See generally* Francine Lafontaine & Fiona Scott Morton, *State Franchise Laws, Dealer Terminations, and the Auto Crisis*, 24 J. ECON. PERSPECTIVES 233 (2010). Among other things, limitations on franchise termination prevented auto manufacturers from adjusting their franchise networks "to shifts in population, market share, and technology," which in turn "create[d] dynamic inefficiency in U.S. auto retailing." *Id.* at 244.

CONCLUSION

If allowed to stand, the district court's construction of the Missouri franchise statute threatens to impose wide-ranging anticompetitive effects. Suppliers are likely to be locked into a "franchise" relationship with the first wholesaler to distribute their brand—even if that wholesaler makes minimal investments in the brand, even if the wholesaler lacks the capacity to effectively distribute the brand, even if the brand makes up only a minimal portion of the wholesaler's business, even if the wholesaler carries and is contractually required to promote competing brands, and even if the wholesaler is larger and more economically powerful than the supplier. As a direct and foreseeable consequence, consumers will face higher prices and reduced choice. This result has no basis in the statutory text or the legislative purpose. To the contrary, it directly undermines the policies underlying franchise statute by forcing unwilling parties into a business relationship with a more powerful counterparty with the opportunity to exploit its unfair advantage. The Court should reverse the judgment with respect to Major Brands' franchise statute claim.

Respectfully submitted,

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RULE 32(g) CERTIFICATION

I hereby certify that based on the word-count function of Microsoft Word, this brief contains 5,128 words, in compliance with the applicable type-volume limitations under the Federal Rules of Appellate Procedure.

In addition, this brief has been scanned for viruses and is virus free.

/s/ Michael Martinich-Sauter