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CLIENT ALERT

On the Rocks No More: FTC Approves $1 Billion Deal Between Low-Price Liquor Rivals With Unusual Remedy

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Just before Christmas, the Federal Trade Commission cleared wine and spirits maker E. & J. Gallo's acquisition of a portfolio of low-price alcohol brands from Constellation Brands, Inc., subject to several conditions, including a rare behavioral remedy. The approval clears a deal that was first announced nearly two years ago. The FTC's decision illuminates the agency's granular approach to defining narrow product markets—here, based on customer/distribution channel, product use, and price tiers—and relies in part on a behavioral remedy requiring Constellation to hold onto and compete with certain brands it had proposed to sell to Gallo.

In April 2019, Gallo agreed to buy over 30 alcohol brands and wine-making facilities from Constellation for approximately $1.7 billion. The proposed transaction largely involved brands associated with lower-priced wines and spirits, such as Cook's sparkling wine and Paul Masson brandy. In January 2020, the parties agreed to modify their deal to remove certain of the brands to address FTC concerns, and revised the deal again in May to remove a sparkling wine production facility from the sale. Yet the as-revised $1 billion deal remained under FTC review for several more months, until approved on December 23, 2020.

The FTC alleged that the deal would result in substantial competitive harm in five product markets, distinct from other types of wine and spirits and distinct from other higher-priced versions of these same wines and spirits, in the U.S. The FTC focused on Gallo's and Constellation's number one and number two position in each of these allegedly highly concentrated markets:

1. **Entry-Level On-Premise Sparkling Wine**: The FTC alleged this market as low-priced sparkling wine often sold to restaurants, casinos, hotels, and other establishments for brunch mimosas, complimentary pours, banquets, and catering. The FTC alleged that Gallo, which owns the Wycliff brand, and Constellation, which owns the J Roget brand, are the two largest suppliers by volume of entry-level on-premise sparkling wine in the United States.
2. **Low-Priced Sparkling Wine**: The FTC described this market as wine sold primarily to end-consumers in grocery, liquor, or convenience stores. The FTC alleged that Gallo's André and Constellation's Cook's brands are the two largest low-priced sparkling wine brands in the United States.
3. **Low-Priced Brandy**: The FTC alleged that Gallo's E & J Brandy and Constellation's Paul Masson brandy are the two largest low-priced brandies in the United States, and a market distinct from other types of alcohols and high-end imported brandies such as cognacs.
4. **Low-Priced Port and Low-Priced Sherry**: The FTC alleged that the transaction would have resulted in Gallo owning 3 of the top 4 low-priced port and sherry brands in the U.S. The complaint distinguishes these cooking and consumption alcohols from others based on their price, "flavor profile, alcohol level, and use."
5. **High Color Concentrates**: This is a syrup used to enhance wines and to make jellies, juices, and other products. According to the FTC, Gallo and Constellation are the two largest producers in the United States.

To resolve concerns in three of the markets, the FTC consent order requires the parties to divest low-price brandy, low-price port and sherry, and high color concentrates products to divestiture buyers. But the consent order notably imposes a behavioral remedy in two markets, requiring Constellation, for four years, to retain and maintain the "full economic viability, marketability, and competitiveness" of both its on-premise sparkling wine brand, J Roget, and its low-priced sparkling wine, Cook's. The FTC further required that Constellation not sell or lease—and Gallo not buy—a key production facility without FTC approval.

The FTC did not explain why a divestiture remedy, which the agency repeatedly has said it prefers, was not available or workable in these two markets, but once the parties decided that Constellation would retain the two products, the FTC took the unusual step of imposing a behavioral remedy, presumably to ensure that those products remained competitive and were not simply discontinued. That would have resulted in the same effects—namely, the elimination of competition between Gallo's and Constellation's products—that the FTC was concerned would occur if Gallo acquired the products.

Notably, all five FTC commissioners voted to accept the proposed consent order, which will now be subject to public comment before the FTC issues the order on a final basis.

This matter serves as an important reminder that the antitrust agencies often define narrow product markets, based on price, quality, and distribution-channel segmentations, in consumer-products mergers. It also demonstrates the FTC's willingness, at least in some circumstances, to accept a behavioral remedy that permits deals to close if the competitive status quo is maintained post-merger.

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