Regulating the Alcohol Marketplace in an era of Globalization

By Pamela S. Erickson

Today we are faced with major attempts to tear down alcohol regulations that govern marketplace activities. To a great degree this is driven by our general business environment which has become national and international in scope. Because the US Constitution allows the states to have the primary role in alcohol regulation, every state has a different set of rules. And, to complicate matters the federal government has its set of regulations. As alcohol businesses move from local and state markets to the national and international level, they often find these regulations impede their ability to easily do business. They must master each state’s unique rules and get the required licenses. Some practices that are legal in one state are prohibited in another. For many states, direct sales of alcohol products to customers from out of state are not allowed.

With these kinds of obstacles, many businesses have called for elimination of the state-by-state regulations, branding the rules as “antiquated” designed for an era before Prohibition that no longer exists. But, before jumping on the deregulation bandwagon, it would be wise to look at the European experience as well as our own recent experience with “unbridled capitalism.”

Impact of Alcohol Deregulation in Europe

Contrary to popular belief, Europe has greater problems with alcohol than we do, particularly when it comes to youth consumption. (Note 1) In fact, Europe is the heaviest drinking region in the world and does suffer the consequences. For example, France, which we consider to be a model of moderation, has one of the highest rates of cirrhosis of the liver in the world over twice that of the US. (Note 2) The Scandinavian countries have a tradition of heavy drinking of high proof liquor. Those countries have had regulations which keep prices high. However, Finland’s alcohol industry found itself competing with cheap alcohol from neighboring Estonia. Under pressure, the government reduced prices. The results are tragic: “Alcohol
abuse has since 2005 been the leading cause of death among Finns aged 15 to 64. The number of deaths from cirrhosis of the liver has increased 100-fold since the 1960s. Consumption has risen from the equivalent of 2.6 litres of pure alcohol per person per year in 1967 to 11 liters in 2006, according to the Finnish temperance league.” (Notes 3 and 4)

Great Britain is currently in the throes of alcohol problems where 13 children a day are hospitalized as a result of alcohol misuse and alcoholic liver cirrhosis has increased by 95 since 2000. The elimination of bar closing hours has resulted in round the clock binge drinking. “The Christina Science Monitor reported in Aug. 24 that British officials say that cheap drink promotions and a trend among supermarkets toward selling alcohol below cost are contributed to crime, assaults, and antisocial behavior. “(Note 5) A recent report found that the 4 largest grocery chains engaged in heavy promotion of alcohol (beer, wine and spirits) at levels below cost during the month of the national football championship. This report sparked calls for price controls including elimination of specials below cost and various kinds of advertising. (Note 5)

**U.S. Experience with Deregulation**

In the US, we are just beginning to see some of the problems with globalization and deregulation. Most recently, we are reeling from the excesses of a poorly regulated mortgage marketplace. As the demand for greater housing and investment grew, the mortgage and banking industry created new loan products to finance exceptionally risky ventures. And, now we are learning about fraudulent practices such as inflating income and home values. Prospective homeowners were enticed with adjustable rates which they could not afford once they adjust upward. In a market environment with no restraint, publically owned companies are pressured by stockholders to make as much money as possible. In an era of globalization, we are finding that companies trying to constantly improve the bottom line will farm work out to foreign countries where there are poor quality control standards or where abuse of employees occurs. These are some of the results of a market free from boundaries or restraints.

These examples caution us to take a close look at our regulations, think about what purpose they serve and decide how best to accommodate new market realities without endangering our population with serious alcohol problems.

**Purposes for Alcohol Marketplace Regulations**

1. **Create and maintain a system with rules that ensure alcohol is sold with restrain and caution.** Each state has a set of rules designed to ensure that alcohol is sold in a way that does not create problems. All businesses are required to
structure their operations to abide by these rules. In many cases, this results additional labor for businesses to do reporting and paperwork and they are restricted in how they make their money. However, in exchange, businesses are protected from many unfair practices such as cutthroat competition, fraud and other abuses.

2. **Promote moderate alcohol consumption**: Research has shown that policies which impact the entire population and operate to reduce overall consumption are the most effective in controlling problems. (Note 6) While somewhat counter-intuitive, these policies prevent moderate drinkers from moving into the heavy drinking category and actually reduce the amount consumed by heavy drinkers.

3. **Prevent problems with specific populations**: Research also shows that attention to specific populations with alcohol problems can be effective. Such populations include underage youth, alcoholics and heavy drinkers and drunk drivers. Marketplace regulations generally prohibit or curtail advertising and promotions targeted at youth and heavy drinkers. Experts usually call for a balance of policies which impact the whole population and those that impact problem areas.

4. **Provide a system which can effectively deal with problems when they arise**: Our license and enforcement systems are designed to provide a state and local level response to problems when they occur. It is important to recognize that alcohol problems are local in nature and can severely impact public health and safety. This is the reason for state and local—versus federal—regulation. Federal agencies are large, cumbersome and react slowly to local issues. Traditionally, enforcement (police powers) is retained by the states and their subdivisions.

5. **Prevent unscrupulous businesses and business practices**: Unethical operators can have devastating impacts on public health and safety by heavy promotion of alcohol to vulnerable populations. Therefore, regulations are designed to reduce the number of bad operators in a marketplace.

**Methods Used to Accomplish Purposes**

States use a large variety of methods to accomplish the above purposes. Some relate to a specific state’s experience. For example, if businesses find a way around a regulation, the state may institute something else to prevent the harmful action. Regulations have grown almost organically working in tandem with one another. Some of the common approaches are:

1. **Prevention of marketplace domination**: Marketplace domination creates problems for alcohol. As businesses attempt to gain market share they often
engage in cutthroat competition driving prices ever lower and increasing consumption. Those businesses that are on the losing end of competition may be tempted to engage in unethical or illegal practices such as promoting heavy drinking and selling to underage customers. As companies become more powerful, they may also attempt to dominate the marketplace by advocating the reduction of regulation. Before Prohibition, large manufacturing companies owned strings of bars and engaged in practices which encouraged very heavy consummation. Therefore, regulations—both federal and state—have created a “three-tiered” system where the retail, wholesale and manufacture sectors are completely or somewhat independent.

- **Tied House Prohibitions prevent or curtail ownership between sectors.** The primary method of combating alcohol marketplace domination throughout the US is our Tied House prohibition. A variety of federal and state laws attempt to limit or prohibit ownership between the retail, wholesale and manufacturing sectors. The concept is designed to keep each sector independent so there is less chance that one or two companies will engage in monopolistic or dominant practices that create social harm. In practice, laws vary. Federal law is designed to keep retailers independent and does allow some ties between manufacturers and wholesalers. Some states require each sector to be independent. As retailers have become large and economically powerful, domination has been an issue with retailers.

- **Financial Assistance or Money’s Worth Regulations.** While Tied House Prohibitions prevent or curtail ownership, marketplace domination can occur in other ways. As a result, many states have laws against the provision of financial assistance or things of value that tie one sector to another. For example, a manufacturer or wholesaler could buy equipment, bar supplies, furniture if the bar owner will agree to exclusively pour a particular manufacturer’s brand, charge prices the manufacturer demands and participate in various promotional campaigns. Retailers could demand payment for labor to service shelves, liberal credit terms for product payment, payment for furniture and equipment as a cost of doing business with a given wholesaler.

It should be noted that Tied House and “Financial Assistance/ Money’s worth” regulations also keep the marketplace relatively vital and competitive. By curtailing marketplace domination by large companies, small wineries, brewers and distillers have been able to enter the market. However, despite these regulations, there has been considerable consolidation of companies in all
sectors. Thus, the threat of marketplace domination and its consequences remain very real.

2. **Price regulation prevents major availability of cheap alcohol.** Throughout the world there are many examples of cheap alcohol devastating whole populations. Cheap alcohol in Finland and Great Britain were mentioned earlier. Brazil is another example where an unregulated market has produced very cheap alcohol and the problems which accompany it. (Note 6) Research has shown that price is a powerful tool in preventing excess consumption. It is particularly powerful in controlling underage consumption as youth are more price sensitive. (Note 7) Price control is not a simple matter because large companies can manipulate pricing in many different ways to retain their market share. Often they can keep prices low in one market even though it is not very profitable, but make it up in another market. Over time they expect it to work in their favor. They can drive others out of business by selling at or below cost. Once the competition is reduced, they can raise their price and reap the profits.

3. *Price supports.* Because price is an effective way of controlling consumption, these laws attempt to prevent large amounts of cheap alcohol. Some states have price supports that prohibit selling below cost.

   *Prohibition of Volume Discounts and other Promotions.* Some states prohibit volume discounts, coupons, or other methods of buying larger quantities at a lower price. Others allow discounts, but prohibit their advertising or promotion.

   It is important to have a variety of ways to control price as one method doesn’t always work.

4. **Curbs on marketing especially to youth and heavy consumers.** Many states have regulations which prohibit marketing to underage consumers or which would appeal to underage consumers. Increasingly, it is difficult to enforce these prohibitions as advertising is interstate in nature. And, it is difficult to prove that an ad was specifically aimed at youth when we live in a youth-oriented culture. Other regulations prohibit promotions which encourage over consumption such as volume discounts.
Other Regulatory Considerations

**Protection for local businesses:** Some states (including Oregon) have laws that require regulations to promote local or small business. Such laws are often subject to challenge as impeding interstate commerce. However, when the objective and method are designed to prevent monopoly and/or marketplace domination, protection of small businesses can be legitimate and valuable to a state’s business vitality. Policy makers need to be concerned about possible impacts of globalization. As we have seen, cheap imports can be problematic. When the cost is low because of “sweatshop labor” or use of impurities or unfair subsidies, our marketplace is adversely impacted. When imports cause local businesses to fail, we lose the capacity to produce that product. As cheap imports experience transportation and labor cost increases, these products will also increase in price. If we have lost our local businesses, we have no choice but to pay higher prices.

**Tax collection:** The regulatory systems in most states have provided for collection of excise taxes through the system in a cost-effective manner. Any changes to regulations need to consider this issue and the cost of tax collection.

**Product safety:** The current regulatory system provides a tracking system that can be used to quickly identify and eliminate tainted products. This has not been a problem in recent years, but could become one with increased imports. Any change in regulation should consider this issue.

**Where to go from here?**

To maintain healthy alcohol business markets, it will be necessary to refine regulations from time to time. Such refinement should be done with caution and restraint given the magnitude of the consequences.

Because there is widespread confusion about the purpose and operations of these regulations, an educational effort is needed within states and across the nation. In addition to education, a national level effort is needed to recommend careful refinements that can accommodate business needs that will no damaging our system that promotes alcohol moderation. The alcohol regulatory system should be viewed as a compact. A structure has been created by law that allows businesses to make a good living but not great wealth through cut-throat, bottom-line oriented practices. Businesses get certain protections from price-gouging, but in exchange they can’t engage in unbridled promotion to vulnerable populations. The rules represent a fine balance that must be maintained no matter how difficult.

**Notes**

2. According to the World Health Organization (WHO), the French drink one and a half times the US per capita and their death rate from liver cirrhosis is more than one and a half times the US rate.


   This is London, January 18, 2008, stated, “Figures hidden away in a Competition Commission paper reveal that the country’s four biggest supermarkets sold 112.7 million pounds of beer, wine and spirits below cost during one month in 2006 when the football World Cup was taking place.


   “The relationship between alcohol price, consumption and related harms is one of the most researched areas of alcohol policy. What the evidence consistently shows I that alcohol prices do have an effect on the level of alcohol consumption. All things being equal, if the price of alcohol goes down, consumption will rise as will the level of harm.”

P. 31