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Why shouldn't alcohol be sold in a free market?

It's a legal product.

By Pamela Erickson

Advocates who want to loosen or eliminate various alcohol regulations claim our laws are “antiquated, byzantine, or from the Prohibition era.” Their conclusion is that alcohol should be sold in our free market system just like any other legal product. How do we answer such claims? We need to help clarify the issue by stating that all products sold for human consumption must be regulated for public health and safety; that the US markets are highly regulated; that government interference is often needed to keep markets competitive and free of monopolistic domination. Finally we must be clear that some marketing practices can foster social problems. Here are some points that can help clarify these issues:

1. **One way or another, all food, drink, drug, and tobacco commodities are regulated for public health and safety.** Food, drugs and tobacco are all regulated by the federal Food and Drug Administration. Alcohol is regulated differently because after Prohibition, the 21 Amendment to the US Constitution gave states the responsibility to regulate alcohol. It is inconceivable that a commodity sold for human consumption would be completely unregulated. Safety of alcohol products is achieved through a three-tier system of licensing and sale. All manufacturers must be licensed and sell only to a licensed wholesaler who, in turn, can only sell to a licensed retailer. The wholesaler tracks all bottles and cans which enable them to act very quickly when there is a problem with a particular product.



2. **The United States does not have a free market in the sense that anyone can sell anything, anywhere, at any time or place.** The free market idea is a commercial system where prices are set by supply and demand, there are few barriers for new businesses to enter the market, and there is no government interference via taxes, price controls or barriers to market entry such as licensing. Clearly, our commercial markets have substantial government interference: taxes are levied by all levels of government on various products, many segments of business require some kind of license and often a government agency is designated to monitor compliance with a myriad of regulations. Just think about the banking, insurance and automobile industries. There are many regulations designed to protect the consumer from dishonest practices and to ensure safety. If alcohol were to become unregulated, it would be completely unique in our commercial environment.
3. **Non-alcoholic drink products are often sold in situations that cannot be considered “free market” operations.** Exclusive agreements are common for soft drink products. A restaurant will gain certain discounts and favors if they will exclusively sell one product over another. Often Coke products will not be sold in the same place as Pepsi products. In grocery stores, a supplier will generally pay a “slotting fee” for being on the shelf; and, the best locations cost more (i.e. the shelves at eye level). These practices impact prices and restrict market entry for new products or products from a variety of companies. Exclusive arrangements and slotting fees are illegal for alcohol products by federal law and many state laws as well.

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4. **Government interference is often required to maintain some of the elements of a “free market” system.** Our marketplaces do operate in an environment designed to allow supply and demand to set prices and to allow new businesses into a market. However, it often takes “government interference” for that to happen. For example, laws prevent price fixing arrangements. The United States has a body of market place regulations designed to prevent monopolies, fraud and unfair operations. Many of these regulations come under the heading of Anti-trust laws. They came about after the recognition that free markets often became dominated by one or more large organizations that would then have the ability to control price and access to market.
5. **Regulations governing the alcohol market are designed to prevent business practices which create social problems.** There are special problems with marketing alcohol that can create problems. Marketplace regulations help prevent these. Pricing is critical because deep discounts increase sales and consumption. While taxes keep the price reasonably high; other regulations reduce the opportunities to lower prices. These regulations include laws that prevent the sale of alcohol below cost, restrictions on coupons or other marketing devices designed to promote high volume drinking. Many states require all distributors to sell all products at the same price to all. This reduces the incentive to drastically lower prices to sell more products. It also makes it less likely that big operators can undercut small operators and eventually dominate the market.



Current Problems with Market Regulations:

1. **Illegal payments:** Despite the prohibitions against payment for things of value, shelf space and exclusive arrangements, these things do go on. Sometimes the supplier representative will find creative ways to disguise the payment. A

few years ago, Arizona had a major problem with alcohol company representatives offering large sums of money to carry their products and not others. Payments were made by giving away things of value (gift cards, furniture, free cases, etc.). After a major investigation, things changed. Currently, there is an investigation in Massachusetts. These practices seem to go on for a long time before something happens.

2. **Collapse of the three-tier system:** The dominant beer company in the US has been trying to buy up retailers and distributors in several states. This would eliminate parts of our three-tier system. Anheuser-Busch InBev makes no secret about the fact that they would like to do their own distribution and currently own several distributorships. They have been thwarted in a few states which have passed laws prohibiting such ownership. But they also are buying up craft breweries, some of which have retail operations such as brew pubs.
3. **Lack of enforcement:** Most alcohol regulatory agencies have endured budget cuts and reduced enforcement resources. The federal TTB has also had staff reductions. Thus, violations go on for some time and sometimes have to get so notorious that they cannot be ignored.
4. **Failure to understand and value market regulations:** A poor understanding of marketplace regulations and naiveté about the “free market” can lead to loss of valuable regulation. The regulations discussed in this newsletter are poorly understood and there are few good explanations in readily understood terms. It can be easy to buy into the “free market” argument.

The typical “free market” arguments just don’t add much to the debate over alcohol regulation. This is especially true because some free market advocates support government interference for other purposes such as economic development projects involving tax incentives and other benefits for a few businesses. Perhaps by noting other instances of government interference in the free market, there will be greater understanding of the need for government action when there is an important public purpose such as preventing alcohol harm.

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