The High Cost of Cheap Alcohol

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THE HIGH COST OF CHEAP ALCOHOL—How alcohol markets are evolving to foster deregulation, offer cheap alcohol and increase social problems.

Executive Summary

Each year alcohol claims 79,000 lives. It is the third leading lifestyle-related cause of death. In 2005, 1.6 million hospitalizations and 4 million emergency room visits occurred due to alcohol. (1) To put these figures in perspective, almost 6,000 military personnel have lost their lives in the Iraq and Afghanistan wars and an estimated 3,000 people die each year due to food borne illness. (1)

Alcohol is related to crime and other social problems. Alcohol was a factor in 19-37% of violent crimes during 1997-2008 and alcohol related crimes were more likely to result in injury and involve intimates than other types of violence. (2) While underage drinking has dropped in recent years, 27% of 12 graders reported being drunk in the past 30 days (3). Youth who drink regularly are more likely to experience a host of problems including failing grades, criminal involvement, traffic crashes, unwanted sex and damage to their developing brain. (1) Problems with alcohol touch many Americans. When asked in a Gallup poll, "Has drinking ever been a cause of trouble in your family?" 31% said "Yes." (4)

Clearly the cost of alcohol misuse is very high. This suggests we need to do whatever we can to minimize the devastating impact the figures imply. A substantial body of research points to the effectiveness of restricting "affordability, availability and accessibility." [5]

The Centers for Disease Control's recommendations mirror such restrictions. Their Task Force on Community Preventive Services found that higher alcohol prices are related to fewer motor vehicle crashes; less impaired driving, violence, sexually transmitted diseases, alcohol dependence and less all-cause mortality. Recently, they recommended against further privatization of alcohol control systems because privatization increases consumption, "a well-established proxy for excessive consumption." Privatization tends to increase availability through more outlets and hours/days of sale and "may be associated with increased alcohol advertising, increases in the number of brands sold, and more lax enforcement of sales regulations, including enforcement of the minimum legal drinking age." [5]

But regulations that embody these principles are being eroded as alcohol price policies are changed, alcohol outlets are allowed to sell more types of products, hours and days of sale are increased, and the total number of alcohol outlets is increased beyond the need for population growth. Eroding these policies is often sold to the public on the basis of increasing tax revenue and improving customer convenience. However, the only way this would work is if a lot more people buy and drink a lot more alcohol.

While surveys usually find public support for alcohol policies to be high, the public doesn't always understand the impact of changes to single regulations. [6] This paper is part of the effort to educate the public about the alcohol regulatory system and how it works. It focuses on one of the most powerful tools available to control alcohol problems: price. Time and again, research has shown that when prices go up, alcohol consumption and its attendant social problems go down. [7] To be effective, pricing policies must impact the entire marketplace and be related to availability. The reason is that cheap alcohol is primarily a problem when large quantities of inexpensive products flood the marketplace; a few cheap bottles in a remote location do not lead to overall social harm.

The state-based alcohol regulatory systems in the United States are built around the need to control practices which contribute to abuse such as widespread, aggressive promotion of cheap alcohol. However, the designers of this system also knew that very high prices could foster bootlegging, smuggling, and other illegal practices. Therefore, regulations were designed to keep prices in balance.

Unfortunately, decades after the implementation of these carefully designed regulatory systems, people seem to have forgotten the bedrock principles on which they are based. This is demonstrated by the statement of US District Judge Marsha Pechman, in the case of *Costco v. Hoen*, "The court found **no persuasive evidence that the purpose of any of the challenged restraints was to promote temperance** by raising average beer and wine prices." [8, Emphasis added.]

This report spells out the basics of alcohol abuse prevention through regulation. For easy reading, just turn to the section that will answer your questions.

What did Prohibition teach us?

What Happened When Alcohol Became Legal Again?

How Did the Current Three-Tiered Regulatory System Change America's Drinking Habits?

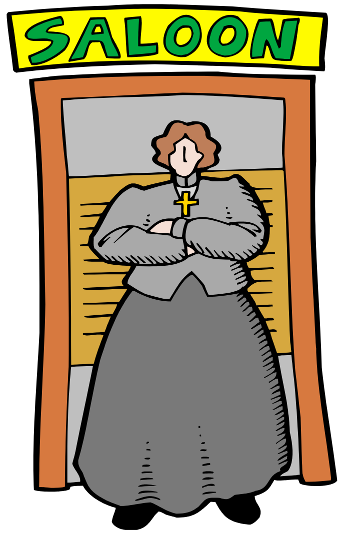
What Has the Balanced Alcohol Marketplace Accomplished So Far?

What Happens When Regulations Are Relaxed?

How Has Globalization Affected Alcohol Use?

What Dangers Lie Ahead?

To explain how regulatory systems use price as a key tool to prevent abuse, it is important to review the thinking behind state regulatory systems--how different parts of the system work together, how price affects alcohol abuse, and how global market trends can impinge upon U.S. alcohol markets.



What Did Prohibition Teach us?

Before Prohibition, alcohol was sold almost exclusively in “saloons”. According to Historian W.J. Rorabaugh, “For generation, Americans had been heavy drinkers, and by 1900 saloons were identified with political corruption, prostitution, gambling, crime, poverty and family destruction.” Beer was the preferred alcoholic beverage and, “major brewers controlled the industry, including the saloons--called ‘tied houses’-- where most beer was sold. To compete, each brewer needed to saturate a neighborhood with multiple saloons.” [9].

To maximize profits for the brewer and his saloon operators, saloons encouraged heavy consumption. They used gambling and prostitution to attract customers and were known to serve both alcoholics and children. In general, the saloon was the only place to buy alcohol—beer, wine and spirits. While most drinking took place in saloons, one could buy a bottle or a bucket of beer to consume at home.

As the years passed, poverty increased, and family paychecks evaporated because of the over-consumption of alcohol. Worker productivity was adversely affected. The severity of these problems ultimately led to the drastic step of Prohibition, which lasted from 1920 to 1933.

Prohibition did reduce alcohol consumption and some of its attendant problems, but it didn’t eliminate drinking. An illegal production and marketing system evolved which included distilleries (“stills”), other manufacturing and brewing operations, transportation, and distribution. Canada was a major source of illegal imports. Many illegal retail outlets, called speak-easies, sprang up.

During Prohibition, alcohol producers engineered a shift away from beer to spirits. Beer was perishable, hard to conceal, and heavy to transport. Spirits were easier to handle in an illegal market, and offered “more bang for the buck”.

As the years passed, it became clear that Prohibition was very unpopular. Enforcement was weak and laws against drinking were widely ignored. This climate fostered organized and violent criminal operations. Those involved had to be well-organized, with distribution systems that spanned state lines. Since the business was very profitable, the criminals involved were highly motivated and presented an overwhelming challenge to law enforcement.

What Happened When Alcohol Became Legal Again?

After Prohibition ended in 1933, a legal alcohol market had to be re-established. Since states were given the responsibility for regulating alcohol individually, each state had to design a new marketplace for itself.

With little expertise in such matters, most states relied on the recommendations of a study financed by John D. Rockefeller, a prominent entrepreneur and industrialist, who had originally favored Prohibition, but had changed his mind once he saw the unintended consequences. This study, titled Toward Liquor Control, was written by R.B. Fosdick and A.L. Scott, who had researched alcohol regulatory systems around the world. [10]

The authors focused on two major problems:

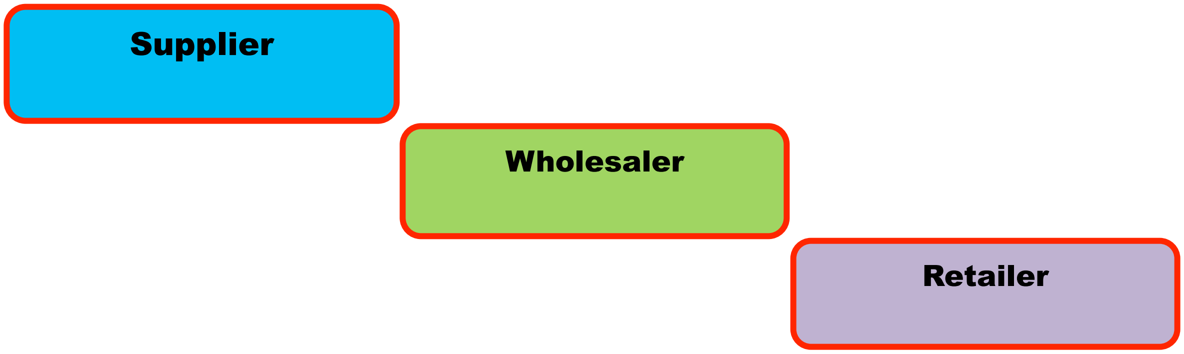
1. How could the profit motive and the consolidation of economic power be controlled in the new alcohol distribution system?

The consolidation of economic power created problems because big alcohol producers aggressively promoted excess consumption. The authors believed that the best alcohol control system was a state-run monopoly where the profit motive would be eliminated. "The possibility of increasing profits," they said, "would encourage private businesses to sell more alcohol, buy political influence and lax enforcement, and violate laws." As a secondary strategy, Fosdick and Scott also acknowledged that a "license system" could curtail some of the profit- fueled problems. [10]

Another strategy was to eliminate the "tied house" structure in which the manufacturers of alcohol products owned saloons and the distributors who supplied them. This vertically-integrated system "had all the vices of absentee ownership. The manufacturer knew nothing and cared nothing about the community. All he wanted was increased sales. He saw none of the abuses, and as a non-resident, he was beyond local influence." [10]

The solution to these problems, as suggested by Fosdick and Scott, was to create a system of licensed manufacturers, distributors and retailers that were kept separate by prohibiting ownership, financial arrangements, and favoritism among the three strata. Every state adopted some version of this "three-tiered system." In the case of Manuel v. Louisiana, there is a description of how this system works: "Without the three-tier system, the natural tendency historically has been for the supplier tier to integrate vertically. With vertical integration, the supplier takes control of the manufacture, distribution and retailing of alcohol beverages from top to bottom. The result is a push to maximize sales and stifle competition. "The three-tier system was implemented to counteract all these tendencies. Under the three-tier system, the industry is divided into three tiers, each with its own service focus. No one tier controls another. Further, individual firms do not grow so powerful in practice that they can out-muscle regulators." [11]

2. The second problem was how to gain public support for the new regulatory systems? Fosdick and Scott recognized that the new regulatory system had to be flexible to accommodate changing conditions. "We need to be on our guard against any system of control that has outlived its usefulness and that no longer represents the prevalent ideas and attitudes of the community." [10] The new systems had to reduce lawlessness and return order to the alcohol marketplace, and they would need public support to accomplish this.



How Did the Three-Tiered Regulatory System Change America's Drinking Habits?

Many said it couldn't be done. Prohibition hadn't eliminated drinking and the social problems stemming from alcohol use, so why would this new regulatory system work any better? But, indeed, it did work better. This is how scholars, Harry Levine and Craig Reinarman, describe it: "Since 1934, alcohol regulation has quietly and effectively organized and managed the production, distribution and sale of alcohol, as well as public drinking." [12] How did this come about?

Tier 1: First, curb the power of large alcohol-producing companies.

One strategy was to curtail the economic power of large, vertically-integrated companies that promoted huge quantities of cheap alcohol to vulnerable populations. This strategy involves:

***Restricting ownership to one tier*:** Federal law prohibits alcohol manufacturers from owning retailers. Most states also have ownership restrictions, and many cover all three tiers. This prohibition limits economic power, tamps down extreme competition, and moderates prices. For example, Oregon law does not permit manufacturers and wholesalers to have any financial or ownership interest in a retail establishment.

Prohibiting cross-tier financial deals: Multi-tier financial arrangements short of ownership are also generally prohibited by state and federal regulations. These are deals that link companies in different tiers through credit, loans, favorable price arrangements and fee-for-service arrangements. These measures also keep prices balanced, prevent extreme competition, and level the playing field for market participants. For example, Washington State prohibits anything of value to be given directly or indirectly from a manufacturer/distributor to a retailer and vice versa. There are exceptions for things of "nominal value" such as napkins or coasters.

Preventing favoritism and monopoly arrangements: Federal and state alcohol laws generally prohibit a manufacturer or distributor from offering an exclusive arrangement, i. e., a favorable financial deal to retailers who exclude competing brands. Again this prevents extreme price competition, affords some market transparency, and levels the playing field. For example, Minnesota law generally prohibits a manufacturer, wholesaler or out-of-state shipper from discrimination in offering price discounts. Posting of prices is also required to ensure that such discrimination does not occur.

Clearly separating the functions of each tier: When businesses found ways around the regulations, states enacted additional rules. Each state requires different licenses for retailers, distributor/wholesalers, and manufacturers. These licenses are usually only granted for performing certain business functions. For example, a retailer can be licensed to sell alcohol in a store, bar, or restaurant, but not to manufacture alcohol products. Many states also specifically prohibit one tier from doing tasks that are fundamental to another tier; for example, a retailer cannot have a central warehouse and move products from one store to another

<u>Restricting franchises and supplier contracts</u>: Many states have laws that keep suppliers from dominating the distributor tier through direct control and management. State laws may also divide the state into specific operating territories.

Tier 2: Distribute alcohol products in a fair and orderly way.

Before the three-tiered regulatory structure was put into place, the alcohol marketplace was as violent and disorderly as illegal drug gangs are today. Markets were volatile, competition extreme, there were few quality controls on products, and cheating was rampant. During Prohibition, illegal activity was everywhere and enforcement was weak.

Even after Prohibition, market disorder created problems. In New York, there were alcohol price wars in the 1930s and 1940s. Prices could change several times a day, and customers rushed to load up on large quantities of cheap product. There were such nefarious dealings in the back alleys of retail establishments that New York actually prohibited retailers from having back doors as a way to impose control on alcohol sellers. [13]

New kinds of regulations strategies were created to calm this out-of-control alcohol market. They included:

<u>Regulations to enforce fair and stable prices</u>: Many states require distributors and wholesalers to offer all of their products at the same price to all customers. Some states also require suppliers to sell at the same price to distributors. Many also require public posting of prices, as well as requirements to hold prices for a period of time. These "Post and Hold" rules use transparency as a cost-effective method of enforcing the uniform price laws. These measures were essential for stopping the price wars such as occurred in New York. Other states base tax collection enforcement and administration on these laws.

<u>Bans on promotions that encourage volume consumption</u>: States may limit volume discounts, special price reductions, and other activities that encourage the consumption of large volumes of alcohol. They may also prohibit below-cost retail sales and require a minimum mark-up. These may be imposed on suppliers, wholesalers, and retailers.

<u>Product tracking</u>: The middle tier of distributors is responsible for keeping track of all alcohol products as they move through the system. This brings order and organization to the inventory-control function, and also prevents tainted and counterfeit products from reaching the market. If spoilage is discovered, it can be quickly tracked and the contaminated products can be removed from the supply chain. Because wholesalers are in retail outlets regularly, they will notice any black or gray market products they did not supply and report that to the state liquor authorities.

<u>Tax collection</u>: The middle tier is also the tax- collection point for excise taxes on alcohol products, keeping tax-collection simple and cost-effective. By having the wholesalers/distributors collect the tax, the state saves money. Tracking and reporting of sales is done by the wholesalers/distributors and then turned over to the state such as in Texas where they report to the state Comptroller.

Licensing responsible business owners: Putting sunshine on the operators of the alcohol industry was very important after Prohibition. The alcohol business had been operated by organized crime syndicates, and once Prohibition was over, it was important to restore law, order, and accountability. All states now have license requirements to ensure that that the each licensee is an individual or company of integrity, free of criminal violations.

Tier 3: Sell alcohol products in a way that does not encourage over-consumption.

Being mindful of how market practices have previously fostered intoxication and social problems, designers of the new three-tier regulatory systems looked for ways to limit consumption. These concerns are still apparent in most states' systems. Regulations are designed to promote the consumption of products with light alcohol content, and restrict the control of products with high alcohol content.

Promotion and packaging of light alcohol products: Shortly before the 21st Amendment was ratified, Congress amended the Volstead Act to legalize beer with an alcohol content of 3.2% or less. After ratification of the 21st Amendment, most states made low- alcohol content beer more widely available than products with higher alcohol content. [12]

After Prohibition, packaging also changed. Beer was made available in single serving sizes such as bottles or cans, versus the buckets or kegs used earlier. With the new packaging, a person could gauge his or her alcohol intake by noting the number of single drinks consumed.

In many states low-alcohol wine (7-11 percent) was also sold in the same places as beer. However, few Americans drank wine, either before or immediately after, Prohibition.

Tighter control of spirits and other high-alcohol products: Most states adopted some kind of "package store" system. In 18 states, the package stores were a part of a state monopoly where products of higher alcohol content were sold in "state stores." The remaining states also developed liquor store systems which specialized in the sale of alcohol (in all forms or just spirits and fortified wines).

Such liquor or "package" stores were usually subject to tighter controls over how products were sold. Most had curtailed hours of sale and were not open on Sunday. The locations were often limited by population or by allowing local control over licensing. Many states prohibited liquor stores from selling other products, or minimized the number and types of other products sold. This allowed the stores to focus on alcohol sales within regulatory boundaries. Staff could be trained to assess age, check identification, and identify intoxicated individuals. By limiting other products for sale, it became more difficult to use inexpensive alcohol as a "loss leader" and make up the loss with other products. Thus, prices were controlled and over-consumption was discouraged.

States which limit the numbers of licenses increase the incentive to comply with regulations. The limitation increases the business value of the license and in many states such licenses are bought and sold sometimes for very high prices. Losing a license due to failure to comply with regulations would result in the loss of a valuable business asset.

Bar/restaurant design: License regulations included business and structural requirements designed to maintain public order. People were encouraged to drink at home, not just in public venues; it was thought that "home values" would restrain the consumption of alcohol. Public venues that did serve alcohol could not offer entertainment or gambling, and prostitution and "lewd behavior" were prohibited. Bars and restaurants were designed to encourage orderly behavior. The new venues offered chairs, and tables were required (as opposed to standing space only). They served food to temper the physiological impact of alcohol, and servers were trained to watch over their customers. Many states also restricted the numbers of drinks sold at any one time to a customer. Barriers were often required to separate drinkers from diners. Licenses were also categorized into wine and beer versus wine, beer, and spirits. Again, the idea was to encourage the consumption of products light in alcohol. [12]

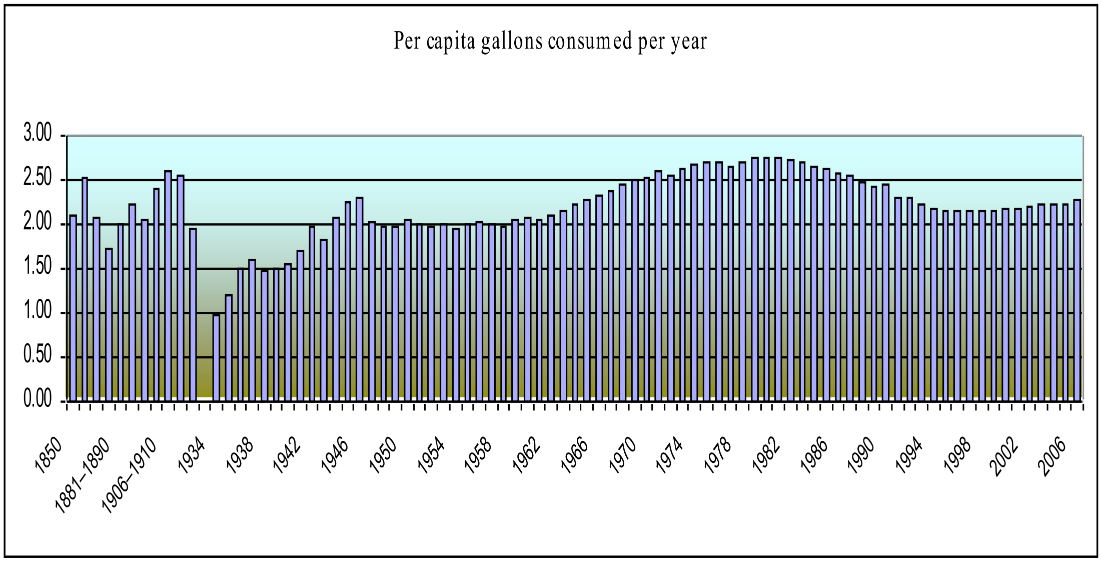
Age restrictions: Prior to Prohibition, children had ready access to alcohol and saloons were accused of selling to children. After Prohibition, all states adopted the age restriction of 21 for alcohol sales. In addition, in most states, those under 21 could not enter a liquor store or a bar where alcohol was sold.

Special customer requirements: Originally, many states imposed special requirements on people who wanted to buy alcohol. For example, some states required a special permit to buy alcohol from a liquor store, or a special identification card in order to be served alcohol in a bar or restaurant. Many states also prohibited sales to intoxicated persons and licensees could prevent specific customers from frequenting their establishment.

Local control and local presence

Two concepts found their way into regulation to avoid problems with "absentee owners" who were apt to ignore any alcohol-related problems their businesses created. The first was local control. When alcohol problems occur, they saddle local citizens with the additional costs for law enforcement, emergency room visits, health costs, loss of worker productivity, and loss of youth potential. Such problems disturb the peace and downgrade the quality of neighborhoods. States instituted local controls to avoid such problems. For example, in Illinois, one must have both a state and local license. Each local jurisdiction may set its own hours of operation and impose other requirements on licensees. In many states, the number of licenses in a local area is set at the local level.

A second concept was that small, local businesses would be the primary components in the alcohol market. Local owners could more easily be held responsible. They were more likely to know and abide by local regulations, and were more susceptible to community pressure. Applying local laws to out-of-state owners is difficult, expensive, and rarely effective. Regulations requiring small operations and local presence became the norm for distributor and retail operations. States often require distributors to be local or in-state companies, and some states prohibit corporations from owning alcohol distribution or retail businesses. For the retail sector, some states limit the number of stores a licensee can own, or may require that store owners be residents of the state.



Source: Centers for Disease Control and Prevention

What Has the Balanced Alcohol Marketplace Accomplished So Far?

Most of the early objectives set for the new alcohol marketplace have been accomplished:

Illegal activities have been eliminated: Although there may yet be a handful of illegal stills in operation, organized crime involving alcohol has been virtually eliminated. Americans were surprisingly compliant with the new system, and bootlegging and counterfeit or tainted products are now rare and swiftly prosecuted.

Saloon system abuses were stopped: The three-tier regulatory structure has eliminated the saloon as it previously operated. The new system prevents market collusion that promotes heavy consumption. License requirements discourage public intoxication, and drinking at home is now an accepted practice.

Overall consumption did not return to pre-Prohibition levels until regulations were loosened in recent years: Consumption remained at moderate levels until the late 1970s and early 1980's. From 1906-1910, Americans consumed an average of 2.6 gallons of ethanol per person; in 1934 it was 0.97. By 1940, it had reached 1.56 and by 1960, 2.07. The move toward lower-alcohol beer was also accomplished. Since 1934, American's average ethanol consumption has been primarily in the form of beer for every year except 1968 and 1969. [14]

What Happens When Regulations Are Relaxed?

Consumption stabilized in the 1950s, but began to increase in the early 1960s, rising steadily until it peaked in 1981 at 2.76 gallons per person, a level not seen even before Prohibition. All forms of alcohol consumption increased. What caused this?

Demographic and cultural changes were occurring. For example, more women began drinking. After Prohibition, a Gallup Poll found that 70 percent of men and 45 percent of women drank. By 1994, the numbers were still 70 percent for men, but a jump to 61 percent for women—this was an increase of 16 percent. [15]

However, the Baby Boomers were the big story. Beginning in 1964, the Baby Boom cohort, born between 1946 and 1969, moved into the "heavy drinking years" of ages 18-29. To understand their impact on society, consider that they represented 40 percent of the U.S. population in 1964, whereas today they constitute just 28 percent. [16]

This large body of young people put political pressure on the states to lower the drinking age. In the 1970s around the Vietnam war, many states changed their laws to allow people to drink legally at age 18 or 19. By 1979, 23 states had lowered their legal age. Retail license regulations were also changed to allow longer hours of operation and more types of licenses.

As before Prohibition, the increased consumption of alcohol once again spawned serious social problems. Now, however, people were more affluent and most people had access to a car, so driving under the influence became the biggest problem.

According to the National Institutes of Health, "In the mid-1970's, alcohol was a factor in over 60 percent of traffic fatalities. Traffic crashes were the leading cause of alcohol-related deaths and two-thirds of traffic deaths among persons aged 16 to 20 involved alcohol." (NIH Fact Sheet) Arrests for this crime increased 182 percent from 1975 to 1980.

Mothers Against Drunk Driving strikes back.

In 1980, Mothers Against Drunk Driving (MADD) was formed to combat the growing DUI problem. MADD formed chapters in every state and lobbied Congress for the National Minimum Drinking Age Act of 1984. This Act required states to increase their drinking age to 21 or lose federal highway funds. MADD also lobbied for stricter DUI laws, including a national standard of .08 Blood Alcohol Content (BAC) as a presumption of impairment for DUI. The actions of MADD and other organizations are credited with reduced deaths due to alcohol. According to MADD's website, since 1980 "alcohol-related traffic fatalities have decreased nearly 50 percent, from over 30,000 to less than 15,500 and MADD has helped save over 383,000 lives." [17]

During the 1980's, overall alcohol consumption once again declined, from a peak of 2.76 gallons per person per year in 1982, to 2.14 gallons per person in 1998. The drinking levels for youth and females also declined.

How Has Globalization Affected Alcohol Use?

In 1998 consumption started to increase again and tracked upward with the increase in prosperity associated with the 2000s. This was also a period when youth drinking increased and children started using alcohol at younger ages. By 2007, NIAAA's consumption statistics reported average per-capita consumption at 2.31 gallons of ethanol per person per year. That was the highest level since 1990 when it was 2.45.

NIAAA does not yet have data for the recent recession years, but a Gallup poll indicates that there has been little change: "The theory, at least is that the recession may give people more reasons to drink, but less money to do it with. To the extent this is true, the effect seems to be a wash. Gallup finds no major changes in the percentage of Americans who drink alcohol (which now stands at 64 percent), in how much drinkers consume, or in their preferred drink—which, by a modest margin, continues to be beer." [18]

The big story now is that major changes are taking place in alcohol markets, just as they are in other areas of the economy. According to Evan Lawson, advertising and the media are shaping public attitudes by showing drinking in a positive light, deregulation is increasing, alcohol distribution systems are becoming more efficient, and industries are consolidating at all levels. [19) All of these changes contribute to an increase in alcohol use.

Dramatic changes have occurred with alcohol advertising: Since the explosion of cable TV, alcohol advertising has increased especially for spirits. (Distilled spirits ads were not shown on network television by agreement.) According to a report by the Johns Hopkins University, cable advertising expenditures for alcohol products increased by 148.1 percent from 2001 to 2009; broadcast advertising actually declined. Spirit advertising lead the increase in ad spending with a whopping 3078%. Beer advertising continued to be the top spending category and increased by 183.3% while alcopops increased 143.6% and wine advertising decreased 40.6%. In addition to TV, alcohol ads may now be found in stores, at community festivals, and on the internet.

This explosion of advertising has impacted everyone and has resulted in "over-exposure" of alcohol advertising to youth. [20]

Increased availability of alcohol: Gone are the days when people could only buy 3.2 percent beer at a grocery store. Only five states still have that regulation. Wine, fortified wine, wine coolers, alcopops and hard cider are now common products in grocery and convenience stores. Tight controls over spirits have also relaxed, with some states allowing sales in grocery stores. Hours and days of sale have expanded so that customers can buy alcohol in many states on Sundays and holidays. Moreover, one can buy alcohol in many new outlets, including airplanes, ships, zoos, outdoor cafes, public festivals, and even some church and school events.

The alcohol content in "light alcohol content" products has also increased. The alcohol content in beer is now more likely to be 4 to 5 percent than 3.2 percent. "Flavored malt beverages" contain 5 to 6 percent, and some wines are now 13.5 to14 percent.

Alcohol is getting much cheaper: For a variety of reasons, alcohol is cheaper. Part of the reason is the failure of taxes to keep up with inflation, part may be efficiencies in production and distribution. But, merchandising methods and relaxed controls for alcohol advertising, pricing and promotion have contributed.

Globalization and consolidation in the alcohol marketplace: Most of the alcohol sold to U.S. customers comes from foreign-owned companies. This has occurred through major consolidation of alcohol companies and the formation of large, economically powerful foreign corporations. The spirits business began consolidating in the late 1990s. In 1999, the top five companies had 43 percent of the world's market share. Those companies were UDV (Diageo), Allied Domecq, Seagram, Bacardi and Pernod Ricard. In 2009, the top five had 68 percent of the global volume share of premium spirits: Diageo (28 percent), Pernod-Ricard (19 percent), Bacardi (10 percent), Brown-Forman (6 percent) and Fortune Brands (5 percent). [19]

The beer industry is highly concentrated in the U.S. to the point where it is called a "duopoly." Two companies: Anheuser-Busch/InBev and MillerCoors have 80 percent of the beer market. These two companies are now also foreign-owned. In 2008, Anheuser-Busch was purchased by InBev, a Belgian company; Miller was consolidated with South African Brewers (SAB) and this company operates in the U.S. as a joint venture with Molson-Coors. Molson is a Canadian company. [21]

The wine business is also dominated by a few top players: Gallo (26.9 percent domestic market share), The Wine Group (21.2 percent), Constellation Wines (15 percent, Foster's Wine Estates Americas (5.9 percent) and Bronco Wine Co. (5.2 percent). All together, the top eight companies hold an 82 percent share of the wine market. One difference with this segment is that these companies are all based in the U.S. except Fosters, and, five of the top eight are in California. [22]

The distribution and retail sectors have also experienced consolidation. Grocery chains, in particular, have experienced a great deal of consolidation. In 2009 Supermarketnews.com reported that the top four supermarket chains had 53 percent of the grocery market. The domination of chains is more intense in some regions than others as some of the largest chains do not have stores in every state. [23]

A large portion of alcohol companies are publically-traded. While this is no different from many commodities today, it poses some particular issues for alcohol. Public companies' primary obligation is to foster their shareholders' interests. This tends to focus corporations on short-term profits versus long term community health and safety.

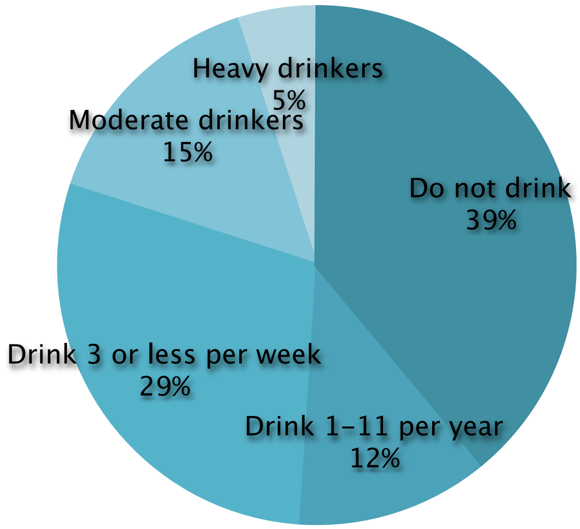
Low prices and high-volume sales spawn increased consumption: When only a few companies dominate a market, the assumption is that they will increase prices and decrease selection because they lack competition. However, this is not what happens in the alcohol marketplace. In the U.S. as well as other developed markets such as the U.K., the supermarket chains offer low prices to capture a larger share of the market. They then make their profits on a high volume of sales. [24]

Major grocery chains use mass merchandising methods to attract customers into their stores. They offer selected products as "loss leaders" to attract buyers, and then sell these customers higher-margin products once they have entered the store. Alcohol products are popular low-cost promotional items, and a good way to lure customers from a competitor's store. Both low-priced promotional offers and high-volume product sales increase alcohol consumption.

Currently, the three-tiered system and other regulations stand in the way of practices that would drop prices and promote ever-higher consumption. It helps to prevent a "race to the bottom" mentality on prices. While a global company could decide to lose money in the US to hurt a global competitor, local distributor and retailers do not share the same interest in losing money. The three separate tiers prevent vertical monopolies. However, without this effective regulation, supermarkets will use their enormous economic power to enter into contracts with suppliers. These contracts will allow rock bottom prices on high-volume purchases. Right now, regulation renders such contracts illegal in some states—instead, a distributor must offer the same price to all. This avoids most arrangements between manufacturers and supermarkets.

Clearly, many major retail players do not like the current regulatory system because it prevents them from implementing their mass merchandising techniques for alcohol products. In some states, they are actively working to deregulate the three-tier alcohol distribution and retailing systems.

American Alcohol Consumption



Source: Centers for Disease Control and Prevention

What Dangers Lie Ahead?

At present, American's consumption is still moderate. Even though overall alcohol consumption has increased in recent years, most Americans either don't drink at all, or they are infrequent or moderate drinkers. Such moderation is supported by the common-sense regulatory systems that most states have in place. [25]

The U.S. state regulatory systems are good ones. They meet the criteria of the World Health Organization which advocates for comprehensive systems that address price, availability, promotion, age restrictions and drunk-driving issues.

However, this could change as it did in the U.K. where a period of deregulation promoted increased alcohol consumption to the point of creating an alcohol epidemic with all its attendant social problems, ranging from sports hooliganism to auto accidents. [26] Similarly, in New Zealand major deregulation occurred in 1989 and consumption increased steadily, along with the usual problems. Both the United Kingdom and New Zealand are now poised to embark on a process of "re-regulation."

In the U.S., we do need to adjust our regulatory systems to meet changing times. This is something regulators have understood ever since Prohibition was lifted. However, we have learned that we can make incremental changes without causing major problems.

The take-away message is that the three-tiered regulatory system works. It is flexible and functions well in many different state environments. Updating this system may make sense, but to dismantle it would create expensive social problems the U.S. simply cannot afford.

NOTES

[1] Centers for Disease Control and Prevention website (www.cdc.gov/alcohol), "Alcohol and Public Health," estimate of deaths uses the Alcohol -Related Disease Impact (ARDI) tool from 2001-2005. Estimates of foodborne illness from website article, "Estimates of Foodborne Illness in the United States." www.cdc.gov/foodborneburden/.

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About the Author

The author of this paper is a former alcohol regulator. From 1996 to 2003, she was the executive director of the Oregon Liquor Control Commission. She left that position to work for Oregon Partnership in the non-profit field of alcohol abuse prevention, specializing in the reduction of underage drinking. As a prevention advocate, she gained an increased appreciation for the value of alcohol regulation and its effectiveness as increasingly demonstrated by research.

In 2007, she began development of the "Campaign for a Healthy Alcohol Marketplace." She became concerned that few people really understood the alcohol regulatory systems in the United States and how they work to reduce alcohol consumption and attendant problems. She realized that as a regulator she did not entirely understand many of the complex regulations that govern the alcohol market. The concern was that important regulations could be lost merely out of ignorance. Her aim with the "Campaign for a Healthy Alcohol Marketplace" is to educate all involved with alcohol issues about the important role these regulations play. This is the third major publication she has developed for this program. Others are:

"The Danger of Alcohol Deregulation: The United Kingdom Experience." 2009

"2011 Issue Briefs for States: Brief Explanations of Common Alcohol Regulatory Issues Facing State and Local Communities." 2011

In addition to these publications, she has produced numerous PowerPoint presentations and articles. All materials can be located and downloaded from the campaign website www.healthyalcoholmarket.com.

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