ECONOMIC AND REGULATORY ASPECTS OF LIQUOR LICENSING *

HARVEY J. LEVIN †

One frequent justification for governmental control of entry into an industry is that free, unfettered competition may jeopardize the industry's economic and social performance. By stabilizing industry revenues, and thereby increasing the funds available for reliable service, entry control is alleged to further the public interest and convenience. Yet, the social consequences of regulation are often less predictable than its economic effects. Licensees derive great economic benefits from the privilege of operating in controlled markets with supported price floors; but it is uncertain whether the public gets anything commensurate in return.

Inasmuch as most scholarly inquiry has focused on federal regulatory experience, there is sufficient reason to undertake a case study of state regulation of retail liquor licensing. There are, however, additional reasons. Alcoholic beverage control is an excellent example of regulatory inertia. The theory behind restrictive liquor licensing has remained untested for thirty years despite its doubtful economic

*This article is based on research initiated when I was Co-Director of Economic Studies for the New York Moreland Commission on the Alcoholic Beverage Control Law during the Summer of 1963. I am particularly indebted to Donald J. Dewey of Columbia University for comments on the whole study. Special thanks are due also to Elliott Zupnick (City University) and William K. Jones (Columbia Law School) for valuable advice on key portions of the argument, and to Robert G. Rice (University of Chicago), Harold L. Wattel (Hofstra University), and the Commission's staff economists and lawyers for assistance at the outset. Most of the statistical work was executed this Winter with the help of Lowry L. McKee of the Hofstra Computer Center. I am grateful, finally, for the chance to discuss some of the ideas with Clark Byse, Lon L. Fuller, and Louis L. Jaffe of the Harvard Law School where the Article was completed during my tenure as Carnegie Fellow in Law and Economics, 1963-1964. The views expressed are my own and not necessarily shared by any of these individuals or organizations.

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### TABLE 1

Alcoholic Beverage Control Laws in the United States, 1960

<table>
<thead>
<tr>
<th>States with</th>
<th>Number of States (incl. D.C.)</th>
<th>Status of New York</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Private License System</td>
<td>33</td>
<td>X</td>
</tr>
<tr>
<td>2. Monopoly System</td>
<td>17</td>
<td></td>
</tr>
<tr>
<td>3. Statutory Objectives:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Exercise of Police Power</td>
<td>14</td>
<td></td>
</tr>
<tr>
<td>Welfare</td>
<td>17</td>
<td>X</td>
</tr>
<tr>
<td>Health</td>
<td>20</td>
<td></td>
</tr>
<tr>
<td>Peace</td>
<td>14</td>
<td></td>
</tr>
<tr>
<td>Morals</td>
<td>14</td>
<td></td>
</tr>
<tr>
<td>Protection</td>
<td>16</td>
<td>X</td>
</tr>
<tr>
<td>Safety</td>
<td>15</td>
<td>X</td>
</tr>
<tr>
<td>Promote Temperance</td>
<td>14</td>
<td>X</td>
</tr>
<tr>
<td>Prohibit Saloon</td>
<td>10</td>
<td>X</td>
</tr>
<tr>
<td>Obedience to Law, Good Order, End Bootlegging</td>
<td>9</td>
<td>X</td>
</tr>
<tr>
<td>4. Statutory Licensing Criteria:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Citizenship</td>
<td>43</td>
<td>X</td>
</tr>
<tr>
<td>No Conviction of Felony</td>
<td>33</td>
<td>X</td>
</tr>
<tr>
<td>Character</td>
<td>27</td>
<td></td>
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<tr>
<td>No Violations of ABC Laws</td>
<td>38</td>
<td>X</td>
</tr>
<tr>
<td>Age</td>
<td>30</td>
<td>X</td>
</tr>
<tr>
<td>Bona-Fide Owner</td>
<td>20</td>
<td></td>
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<tr>
<td>Interlocking Interests</td>
<td>34</td>
<td>X</td>
</tr>
<tr>
<td>Residence</td>
<td>32</td>
<td></td>
</tr>
<tr>
<td>Financial Responsibility</td>
<td>9</td>
<td></td>
</tr>
<tr>
<td>5. License Limitation:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>No Limitation by Statute</td>
<td>13 (10)*</td>
<td></td>
</tr>
<tr>
<td>Discretion Vested in State Agency</td>
<td>11 (8)</td>
<td>X</td>
</tr>
<tr>
<td>Discretion Vested in Local Authorities</td>
<td>5 (4)</td>
<td></td>
</tr>
<tr>
<td>Statutory Numerical Limitation</td>
<td>21 (12)</td>
<td></td>
</tr>
<tr>
<td>6. Resale Price Maintenance in License States:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Compulsory Resale Price Maintenance</td>
<td>17</td>
<td>X</td>
</tr>
<tr>
<td>Voluntary Fair Trade:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>With Nonsigner Clause</td>
<td>7</td>
<td></td>
</tr>
<tr>
<td>Without Nonsigner Clause</td>
<td>4</td>
<td></td>
</tr>
<tr>
<td>No Fair Trade</td>
<td>5</td>
<td></td>
</tr>
<tr>
<td>7. Types of Establishments Eligible to Sell Liquor by the Bottle in License States:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Exclusive Liquor Stores Only</td>
<td>10</td>
<td>X</td>
</tr>
<tr>
<td>Grocery Stores</td>
<td>17</td>
<td></td>
</tr>
<tr>
<td>Drugstores</td>
<td>22</td>
<td></td>
</tr>
<tr>
<td>Other</td>
<td>10</td>
<td></td>
</tr>
<tr>
<td>8. Commodities other than Wine and Liquor Sold in Package Stores in License States:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Wine and Liquor Only</td>
<td>3</td>
<td>X</td>
</tr>
<tr>
<td>Wine, Liquor, Food</td>
<td>20</td>
<td></td>
</tr>
<tr>
<td>Wine, Liquor, Beer</td>
<td>30</td>
<td></td>
</tr>
<tr>
<td>Wine, Liquor, Nonalcoholic Beverages</td>
<td>29</td>
<td></td>
</tr>
<tr>
<td>Wine, Liquor, Bar Accessories &amp; Glassware</td>
<td>22</td>
<td></td>
</tr>
</tbody>
</table>

* () denotes number of private license states.
(See opposite page for footnotes 1 to 4).
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premises. Until recently there has not even been adequate analysis of its effects on the economic status of the licensees.

This Article focuses on liquor licensing in New York State. But, as Table 1 indicates, the findings also are relevant to many other states.

Identical problems do not necessarily arise in every license state. Restrictive licensing and price maintenance, however, can be expected to have similar economic-regulatory effects wherever they operate under comparable conditions. New York's licensing system presents an excellent example since it has long had nationwide prestige and the recent licensing scandals there⁵ may be viewed as a danger signal for other localities.

Today, more than thirty years after the twenty-first amendment, the main question is how well license limitation and price control have furthered temperance or related goals, and whether other techniques might not achieve those goals more efficiently. Answers to these questions will not only help in appraising the performance of New York's liquor laws, but may also provide insights into forces at work elsewhere; if a satisfactory alternative could be found for New York it might stimulate reform in other states.

I. THE PHILOSOPHY OF ALCOHOLIC BEVERAGE CONTROL

The philosophy of control purports to strike a balance between the close-fisted paternalism of prohibition and complete reliance on consumer preferences as the arbiter of production and consumption. With a few important exceptions, today the consumer is free to consume, but the conditions under which he does so are controlled by a licensing authority.

A. A Statement of Policy

The regulatory philosophy is exemplified by section 2 of New York's Alcoholic Beverage Control Law:

[T]o regulate and control the manufacture, sale and distribution . . . of alcohol beverages for the purpose of fostering . . . temperance in their consumption and respect for and

¹ The figures for items 1-5 were derived from JOINT COMM. OF THE STATES TO STUDY ALCOHOLIC BEVERAGE LAWS, ALCOHOLIC BEVERAGE CONTROL (rev. ed. 1960) [hereinafter cited as ALCOHOLIC BEVERAGE CONTROL].
³ DISTILLED SPIRITS INSTITUTE, SUMMARY OF STATE LAWS AND REGULATIONS RELATING TO DISTILLED SPIRITS (1961).
obedience to the law . . . [This can] best be carried out by empowering the liquor authority of the state to determine whether public convenience and advantage will be promoted by the issuance of licenses to traffic in alcoholic beverages, the increase or decrease in the number thereof and the location of premises licensed thereby, subject only to the right of judicial review . . . . The restrictions, regulations and provisions . . . [prescribed aim to promote] the protection, health, welfare and safety of the people of the state. [A proscription against “saloons” concludes this preamble.]

Further elaboration of the philosophy appears in subsections 4 and 5 of section 63 which provide that liquor is to be distributed by stores: (a) which specialize in that alone and conduct no other business on the premises; (b) only one of which is owned by any single licensee; (c) that are not interlocked directly or indirectly with any manufacturer or wholesaler of alcoholic beverages.

Before examining the theory behind restrictive licensing, a brief discussion is in order on the magnitude of New York’s liquor trade and on the character of its regulatory framework.

B. Economic Organization and Regulatory Technique

About one-third of retail liquor distribution in New York is “by the drink,” handled largely by restaurants, bars, and taverns—places for so-called “on-premise consumption.” The remaining two-thirds is “by the bottle,” handled by package stores licensed exclusively to sell for “off-premise consumption.” Retail licenses for off-premise sales have always been distributed much more freely for beer than for liquor. On January 1, 1962, New York had some 24,000 outlets for canned

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6 N.Y. ALCO. BEV. CONTROL LAW §2.
7 N.Y. ALCO. BEV. CONTROL LAW §63(4). The exclusion of grocers and drugstores is sometimes justified as facilitating tighter controls over the number of off-premise outlets and the enforcement of minimum consumer resale prices. Of the 33 states and the District of Columbia which have private license systems today, New York is one of only ten which limit off-premise liquor sales exclusively to specialized liquor stores. This contrasts with twenty-two states which permit drugstores or groceries to distribute liquor, thirteen of which actually have no specialized package stores. See DISTILLED SPIRITS INSTITUTE, SUMMARY OF STATE LAWS AND REGULATIONS RELATING TO DISTILLED SPIRITS (1961).

8 N.Y. ALCO. BEV. CONTROL LAW §63(5). The one-to-a-customer rule, aimed at preventing excessive control by any single entity, is also tied in with the statutory provision that retail prices should be maintained to preserve “the statutory plan for location of off-premise liquor and wine stores in neighborhood communities.” N.Y. ALCO. BEV. CONTROL LAW §101(c).

9 A policy in favor of local residents is allegedly based on a belief that greater licensee responsibility will result when licensees are well known in the community. The prohibition of interlocking interests aims further at precluding irresponsible absentee ownership. But its original target was the “tied house”—those chains of taverns controlled by big distillers or brewers who subjected them to financial pressures to push beverage sales vigorously.
or bottled beer (mainly grocery stores and supermarkets), but only 4,236 licensed liquor stores.

Relevant statistics for New York are contained in Table 2. New York placed first among all states in 1958 in aggregate on-premise liquor business, and seventh in gross sales per drinking place. New York also ranked second in aggregate off-premise liquor sales in that year. Among license states, New York ranked ninth in liquor consumption per adult, but only thirteenth when the data are limited to residents of “wet” areas. Finally, New York ranks thirteenth among the license states in the volume of state revenues per capita derived from alcoholic beverage taxation.

In marked contrast with the above figures is New York’s relative showing in the ratio of off-premise liquor licenses to population. In the on-premise field, the state ranks fourth among nineteen license states studied, but only twenty-fifth among thirty-two such states in off-premise outlets. Even including the sixteen monopoly states which restrict off-premise outlets, New York still ranks only twenty-ninth of forty-eight states studied.

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10 New York actually ranked only twenty-first in gross sales per package store. But this rank reflects the policies of monopoly states which handle the bulk of their off-premise sales in relatively few state stores. Thus, New York had annual sales of $108,750 per store compared to an average of $203,220 per store for all monopoly states, and of $96,990 for all license states. She actually ranked ninth in sales per store among the license states. See 1 U.S. BUREAU OF THE CENSUS, DEPT OF COMMERCE, 1958 CENSUS OF BUSINESS 59 (1961).

11 Specifically, New York’s consumption per adult in 1960 was 2.79 gallons compared to an average of 2.37 for all license states and of 1.83 for the monopoly states. However, when we exclude dry areas from the study, New York’s figure remains the same but contrasts with 2.68 gallons for all license states and 2.04 for the monopoly states. In 1962, only .5% of New York’s population resided in dry areas, compared to a national average of 12.3% and to Georgia, 59.1%; Tennessee, 54.3%; North Carolina, 51.3%; Arkansas, 44.3%; and Alabama, 40.1%. See DISTILLED SPIRITS INSTITUTE, 1962 ANNUAL STATISTICAL REVIEW OF THE DISTILLED SPIRITS INDUSTRY 49 (1963).

12 DISTILLED SPIRITS INSTITUTE, PUBLIC REVENUES FROM ALCOHOLIC BEVERAGES (1961). Because alcoholic beverage tax revenues in monopoly and license states are not fully comparable, New York is most appropriately compared to other license states. In 1960 such revenues amounted to $6.27 per capita in New York compared to an average of $6.08 for all license states, of $9.05 for the monopoly states, and of $6.98 for all states. Some license states with comparable industrial-economic characteristics raised more tax revenue per capita [California ($8.10), Illinois ($7.16)], and others raised less [Connecticut ($5.18) and New Jersey ($4.52)].

13 In this paragraph, variations in the number of states studied are due partly to gaps in the data, and partly to the fact that some states permit sales of liquor by the drink and by the bottle in the same establishment. In 1960 there was one on-premise outlet in New York for every 485 adults residing in “wet” areas, compared to one package store for every 2,611 persons. This situation contrasts with comparable averages for all license states of 1,043 persons per on-premise outlet and 1,694 per off-premise outlet; and for the monopoly states of 684 and 5,933 persons, respectively. As regards comparable license states, California served an average of 1,031 and 1,181 persons respectively, with each of its on-premise and off-premise outlets; the District of Columbia served 892 and 1,306; Massachusetts, 654 and 1,559; and New Jersey 9,600 and 1,900.
<table>
<thead>
<tr>
<th>State</th>
<th>On-Premise*</th>
<th>Off-Premise</th>
</tr>
</thead>
<tbody>
<tr>
<td>New York</td>
<td>45.96</td>
<td>108.75</td>
</tr>
<tr>
<td>Connecticut</td>
<td>35.75</td>
<td>129.49</td>
</tr>
<tr>
<td>Massachusetts</td>
<td>44.94</td>
<td>99.10</td>
</tr>
<tr>
<td>New Jersey</td>
<td>38.33</td>
<td>121.20</td>
</tr>
<tr>
<td>Pennsylvania</td>
<td>40.69</td>
<td>120.64</td>
</tr>
<tr>
<td>Ohio</td>
<td>36.33</td>
<td>73.18</td>
</tr>
<tr>
<td>Illinois</td>
<td>41.91</td>
<td>111.96</td>
</tr>
<tr>
<td>California</td>
<td>46.84</td>
<td>108.83</td>
</tr>
<tr>
<td>All License States</td>
<td>36.63</td>
<td>96.99</td>
</tr>
<tr>
<td>All Monopoly States</td>
<td>35.31</td>
<td>203.22</td>
</tr>
<tr>
<td>All States</td>
<td>36.23</td>
<td>205.38</td>
</tr>
</tbody>
</table>

**Note:**
- * refers to total sales of 'drinking places' as defined by U.S. Bureau of the Census, including non-liquor sales.
- ** monopsony state.
- *** licenses serve liquor for on- and off-premise consumption jointly.

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15 Distilled Spirits Institute, Apparent Consumption of Distilled Spirits, 1953-1962 (1960 data).
16 Distilled Spirits Institute, 1960 Annual Statistical Review Table 55.
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The State Liquor Authority (SLA) is empowered to employ a comprehensive licensing system at all three levels of the alcoholic beverage industry—production, wholesaling, and retailing. Virtually no one may enter or operate without a license or permit, and there has been little serious talk of complete deregulation, even of low alcoholic content beer and wine. Violation of the SLA’s detailed rules and regulations may mean loss of operating rights through revocation, cancellation, or nonrenewal of a license, subject to judicial review.

The entry control power includes the power to impose limits on the number of licensees in any and all markets. In this respect, New York’s discretionary control technique probably has potentially greater flexibility—and is therefore subject to more attempts at manipulation—than those in twenty-one states with explicit statutory numerical limitations. New York contrasts also with thirteen states which have no statutory limits whatever, and five in which limits are set locally.

Related to entry control is the SLA’s power to enforce compliance with the standards of conduct by which licensees must abide. Conduct standards include prescriptions respecting the physical character of the premises—rules on “visibility” for package stores and seating arrangements for bar-grill licensees—and minimal standards of decorum—rules on gambling, the serving of minors, solicitation, and disorderliness. The SLA also has the responsibility to enforce minimum resale prices.

Regulatory standards purport to promote the “public convenience and advantage,” a broad administrative standard that confers considerable latitude on the SLA to override strict competitive norms. The ultimate viewpoint from which the SLA’s control of entry and other conduct must be appraised is not simply that of economic efficiency and progressiveness, but of alcohol consumption control.

In short, the SLA theoretically has the power to alter the industry’s structure, by limiting the number of sellers in each relevant market, and the industry’s behavior, by prescribing and proscribing specific dimensions of business conduct. Within broad statutory bounds, the SLA possesses considerable discretion in formulating criteria and policies to further the ultimate goals of the law. Although most of the aforementioned regulatory powers formally apply to each

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18 New York actually authorized their production and distribution a year before legalizing liquor sales in 1934. From the outset it has also issued off-premise beer licenses far more freely, and at lower license fees, than licenses to sell liquor by the bottle. See N.Y. State Comm’n on Alcoholic Beverage Control Legislation, First Report 11 (mimeo. 1933). In 1961, 23,531 grocery stores were licensed to sell beer, compared to a total of 4,236 liquor stores.

19 See ALCOHOLIC BEVERAGE CONTROL 104-05 (Table 15).

level of industry, regulation at the retail level is of greatest concern today and will be scrutinized most intensively in this Article.21

C. The Theory of Restrictive Licensing

Restrictive licensing is based first on general assumptions about the relation between the number and character of licensees and the volume of alcohol consumption. The theory is that:

(a) availability is a factor in consumption;

(b) drinking conditions are a factor in consumption;

(c) the responsibility of retail licensees especially with regard to minors and habitual alcoholics is best maintained by encouraging local neighborhood location, by prohibiting interlocking ties with absentee producer interests, by careful initial screening of licensees to weed out undesirables, and by creating a franchise sufficiently valuable to give the licensee a stake to safeguard it;

(d) short of absolute prohibition, some control over consumption is needed to preserve law and order, health, safety, and community welfare—sumptuary taxation can help to a point, but is not an adequate alternative to restrictive licensing because the tax level needed might well precipitate further illicit production with less rather than more tax collections than under lower tax levels with restrictive licensing.22

The theory of restrictive licensing is also built on specific assumptions regarding the relation between unlimited retail licensing and particular price and nonprice inducements to excessive consumption:

1. Off-Premise Licensees

(a) resale price-maintenance notwithstanding, unlimited new entry would subject off-premise licensees to serious pressures to stimulate liquor sales by price competition in the form


of secret discounts, rebates, and "deals" for their customers, and to pressures for comparable secret concessions from their suppliers;

(b) if price-control efforts are effective, attempts to increase consumption will simply take nonprice forms, ranging from free delivery and excessive advertising (which must therefore also be closely regulated), to illicit incidental activities like the provision of bookie facilities;

(c) if even the illicit kind of competition just cited does not eventually sustain revenues, licensees may become "fronts" for underworld-type elements who, despite their own inability to qualify, and the one-to-a-customer rule, may assume de facto control of a sizable empire.24

2. On-Premise Licensees

(a) unregulated multiplication of bar-grills would create comparable competitive pressures to bring the customer in at any cost (even by using hostesses, gambling, and prostitution);

(b) although offenses in drinking places are punishable under the criminal code, competition would aggravate enforcement problems and add unnecessarily to the load of other governmental agencies;

(c) these dangers of "excessive competition" largely disappear once one limits the on-premise outlet to "bona-fide" restaurants, a requirement which not only improves the character of drinking conditions but also provides a sane, convenient rule of thumb to restrict the number of on-premise licenses.25

So much for the theory. For purposes of analysis and testing, the key question is whether restrictive licensing is really a significant factor in restraining liquor consumption, or whether unrestricted licensing would necessarily stimulate consumption excessively. Much of New York's present licensing system rests on hitherto untested answers to these questions.

24 On the alleged relations between entry control, resale price maintenance, and alcoholic consumption control see 1947 SLA ANN. REP. 16-18; 1950 SLA ANN. REP. 22-25; 1954 SLA ANN. REP. 18-20. On the danger that licensees may become "fronts" for criminal elements and on the need to maintain vigilance against undesirables of bootleg days see 1954 SLA ANN. REP. 6; 1958 SLA ANN. REP. 12-13, 16-18; 1961 SLA ANN. REP. 6.

D. Effects of Restrictive Licensing on Alcohol Consumption

1. Theoretical Aspects

There are good reasons for doubting that a restrictive licensing policy, by itself, has had any important restraining effect on off-premise liquor consumption. Economists generally agree that with given incomes the quantity demanded of any commodity depends on individual tastes and the cost of the commodity to the consumer. Restrictive licensing can affect the quantity of liquor demanded only by affecting one or another of these variables.

The cost of liquor to the consumer actually consists of three components—the price of liquor, the delivery costs or personal transportation expense incurred in buying liquor, and the value to the consumer of the time he must spend in purchasing liquor. The only way that restrictive licensing can affect the demand for liquor is by raising its price, making it less convenient to buy, or changing the consumer's tastes. The policy has probably not affected consumer tastes significantly. In regard to price, the enforcement of minimum resale prices may conceivably have been more difficult without restrictive off-premise licensing. But price maintenance is often used without entry controls. Lacking evidence on the amount of price shading that would have occurred without restrictive licensing, it is difficult to argue that the latter has raised off-premise retail prices higher than they would have been under price maintenance alone.

This leaves the policy's effects on public convenience in buying liquor by the bottle. Given the price of liquor, the amount demanded will vary inversely with the amount of time and money the consumer is forced to spend in seeking out a package store, or in the cost of having liquor delivered to his home. The significance of this effect of restrictive licensing, however, is open to question. Despite restrictive licensing of retailers, few, if any, residents of major population centers in New York State are very far from a package store. In addition, package stores in many areas provide free delivery service as a com-

26 The specialized liquor store provides tighter control over sales to minors than widespread grocery store distribution. Hence it would seem to prevent undue "exposure" and thus to deter the development of drinking habits over time. Yet it is not clear that restrictive licensing is needed. Nonrestrictive licensing (and possibly even controlled distribution by drugstores) might achieve the same purpose.

27 To say that off-premise licensing is necessary because resale prices of packaged liquor are set administratively at a level above that which would prevail in a free market is not to say that this licensing policy per se acts to raise price. In the absence of resale price control, it is not clear that the present licensing policy by itself would keep off-premise retail prices above their free market level unless it facilitated price collusion.
petitive tactic in the face of price control. This suggests that for all
practical purposes the license limitation policy in these areas has
raised the total cost of liquor by no more than the price of a telephone
call.

These considerations would limit the impact of the restrictive off-
premise licensing policy to those residents who live outside the major
population centers, and who, for one or another reason, are deprived
of free delivery service or are unaware of its existence. A regu-
lation that affects so few people is not likely to be a significant deterrent.
The conclusion that emerges is not that restrictive off-premise licensing
cannot restrain the demand for liquor, but rather that it can be
effective only if it acts to raise the total cost of liquor to the consumer
by more than it presently does in New York State.

The effects of license limitation on on-premise consumption are
less readily apparent. The distinction that Table 3 draws between
restaurants where food sales completely dominate the business and
taverns where liquor sales dominate is important. All qualified bona-
fide restaurants are normally granted liquor licenses for the asking.
License limitation and refusal of permission to remove premises have
been applied almost exclusively to taverns and bar-grills. The effec-
tiveness of this restrictive policy is subject to question. Clearly, non-
committed drinkers will be less likely to seek out a tavern, the fewer
the taverns per capita in a county, the less convenient they are to
locate or reach, the higher the cost of drinks, and the less compelling
the incidental attractions. With no legal control of price minima,

\[28\] One would also have to assume that the potential consumers were only "border-
line" drinkers. It is hard to see how restrictive licensing per se could ever deter a
heavy drinker from planning his purchases far enough in advance to maintain any
desired rate of consumption. Finally, one would want to rule out any significant
substitution of on-premise for off-premise consumption in those areas.

\[29\] Derived from unpublished SLA survey. "Gross Sales" include all receipts
from sales of food and liquor. Zone 1 includes New York, Kings, Bronx, Queens,
Richmond, Nassau, Suffolk, West Chester, and Orange Counties.

TABLE 3 \[29\]
Gross Sales of On-Premise Licensees in New York State—Zone 1, Spring 1961
(all sales in thousands of dollars)

<table>
<thead>
<tr>
<th>Licensees With Food Sales of</th>
<th>Percentage</th>
<th>Gross Sales</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Licensees</td>
<td>Total</td>
<td>($$)</td>
</tr>
<tr>
<td>I.</td>
<td>75% or More</td>
<td>1,051</td>
<td>11.6</td>
</tr>
<tr>
<td>II.</td>
<td>50%-75%</td>
<td>1,154</td>
<td>12.8</td>
</tr>
<tr>
<td>III.</td>
<td>25%-50%</td>
<td>2,359</td>
<td>26.1</td>
</tr>
<tr>
<td>IV.</td>
<td>Below 25%</td>
<td>4,473</td>
<td>49.5</td>
</tr>
<tr>
<td>TOTAL</td>
<td>9,037</td>
<td>100.0</td>
<td>1,061,235</td>
</tr>
</tbody>
</table>
moreover, the price of drinks would vary inversely with the number of taverns in the market. It follows that license limitation may in fact reduce the pressure for price competition and even for those illicit varieties of nonprice behavior already mentioned.

In theory, tight control over the number of licensed taverns, and any resulting reduction of price or nonprice competition, might simply divert alcohol consumption from taverns to restaurants or package stores. There is, however, no conclusive evidence on the actual degree of substitutability. The most that can be said is that the limitation of tavern licensees seems somewhat more likely than the limitation of package stores to deter alcohol consumption. A more definite statement must wait on further empirical work.

2. Empirical Aspects

In the absence of sufficiently refined or even separate data for taverns and restaurants, my inquiry is limited to off-premise consumption. I have utilized multiple regression techniques to test the theory that restrictive off-premise licensing has had significant restraining effects on alcohol consumption in New York State. This analysis permits estimation of the relative importance of several factors which appear to influence the level of gross per capita liquor store sales in sixty-two New York counties. The four factors that seem most relevant for this purpose are income, population density, flow of traffic and transients across county lines, and off-premise licenses per capita.

Because general knowledge of the determinants of liquor consumption leads to the conclusion that income exerts a strong positive influence, each county's median family income was taken into consideration. It is obvious, however, that liquor store sales are by no means limited to any county's own residents; they are also affected by the flow of transients or regular buyers from outside the county. To assess the influence of the transient, a second factor was introduced—per capita sales of eating and drinking places in each county.


This variable also reflects consumer preferences for eating and drinking outside the home. To the extent that it does (and consumers substitute on-premise for off-premise consumption), its power to explain differences in gross liquor store sales per capita may actually be understated in our results because the variable represents a net effect of transients and tastes. Finally, the introduction of traffic-transient flow
LIQUOR LICENSING

The use of population per square mile is based on the known differences in drinking habits in urban and rural areas. The assumption is that the percentage of different counties' populations consisting of drinkers and nondrinkers varies and these variations are related positively to population density. Adult population per package store was introduced as a final variable on the assumption that, if restrictive licensing did exert any significant restraining effect on consumption, then, holding constant income, tastes, and transient-traffic flows, per capita liquor store sales should be lower where population per package store was higher. 32

The major conclusions were: 33

Per capita liquor consumption in New York, as reflected in gross liquor store sales per capita in sixty-two counties, is significantly associated with the flow of transients and regular consumers into, as well as within, a county (as reflected in per capita sales of the county's eating and drinking places); differences in tastes and degrees of urbanization (as reflected in population density); the average number of persons served by each package store; and the county's median family income.

The best estimate available is that, for any 1% rise in per capita sales of eating and drinking places, gross per capita sales of liquor stores rise .55%, holding constant median family income, population density, and population per liquor store. The relation between changes in liquor store sales and changes in each of the remaining variables (holding constant three others in each case) is +.09% for every 1% increase in population density; +.63% for every 1% increase in median income; and −.45% for every 1% increase in population per package store.

The major factors which explain variations in liquor store sales among the sixty-two counties are population density and the flow of traffic and transients as reflected in sales per eating and drinking places. Together they account for 77% of the total variations in liquor store sales. Indeed, the explanatory power of sales per eating and drinking place may actually understate the im-

may help to compensate for the inadequacy of counties as a proxy for the package store's true market. Counties seemed to be considerably better basic units here than states, especially in view of differences between license and monopoly states, but counties also have limitations of the sort just mentioned.

32 It was not assumed, however, that a statistically significant negative association between population per license and per capita consumption would necessarily demonstrate a causal relationship. Many other factors must be weighed to establish license limitation as a "cause" of lower liquor consumption.

importance of traffic flows and transients insofar as some people undoubtedly substitute on-premise for off-premise liquor consumption. The effects revealed in the regression might be larger if we could exclude such substitution.

Because changes in population per liquor store and liquor store sales per capita are inversely associated with changes in liquor store sales per capita, it might seem reasonable to conclude that restrictive licensing restrains consumption. However, there are great hazards in inferring any such causal relationship. For example, assuming economic rationality one would expect that businessmen would have flocked to the high income, densely populated centers before 1948 when licensing was less restrictive; i.e., to the centers where large liquor sales could be anticipated. Likewise the fact that areas with relatively few licenses per population today are the very ones where income and population density are relatively low, nondrinkers numerous, and liquor sales small, may simply reflect the rationality of the original package store owners and their ability to predict subsequent patterns of economic growth.\textsuperscript{34} Insofar as the above is true, one can clearly infer that variations in licenses per county population reflect rather than "cause" variations in per capita liquor store sales.

The last point can be stated in another way. Stores locate close to customers because "nearness to stores" or "convenience" are factors that affect the quantity of a commodity demanded. The less time and money consumers must spend in buying liquor by the bottle, the more likely it is that they will buy. For this reason it is rational for package stores to flow to the areas of greatest potential consumption. Hence, the negative association in the regression between population per package store and liquor store sales per capita. What this really shows is not the measure of the effect of license limitation on consumption, but rather an "index" of the state's potential power to curtail consumption by depriving consumers of their neighborhood stores. What remains unclear is the extent to which the number of licenses must be reduced to reduce consumption by any desired percentage. In contrast, income, population, and transient-traffic flows emerge as unmistakable determinants of per capita liquor store sales.

Strikingly similar results appear in additional analyses of all states. For every 1% rise in median family income, population per licensee, in per capita sales of eating and drinking places, and

\textsuperscript{34} Also relevant is the fact that licenses per county population are more numerous in those areas where per capita sales of eating and drinking places are higher. That is, package stores go to the places where people spend a good deal on eating and drinking out—because these are in turn the places where the flow of traffic and transients supports high liquor store sales.
in population density, respectively, apparent consumption varies, other things equal, by .82%, -.06%, .20%, and .07%. These coefficients are not identical with those for New York alone, but the relative importance of each variable is roughly the same in both tests.\(^3\) The main difference is the weaker evidence for all states that population density has any significant effect at all. Looking at thirty-two license states only, we find roughly similar relationships. Here the aforementioned coefficients are now .17%, -.14%, .66%, and .09%. (The main difference from the analysis of all states is simply in the relative importance of income and sales of eating and drinking places.) In sum, the findings are consistent with the thesis that New York's experience is broadly representative of the situation elsewhere.

**E. Conclusion**

The substance of these findings can be restated succinctly. For thirty years the advocates of restrictive off-premise licensing, both in government and industry, have defended the policy's widely acknowledged economic advantages to industry by citing its social value in the control of alcohol consumption. A fairly elaborate theory regarding the danger of unlimited licensing is based largely on an alleged relation between the number of package stores in a market, their price policies and nonprice behavior, and the volume of liquor consumption. Defenders of the present system, however, have never presented systematic or comprehensive evidence in support of this theory.

The preceding analysis, however, provides no conclusive support for the theory behind restrictive off-premise licensing. Even the most liberal interpretation of the data for New York indicates, at most, possible restraining effects in some sparsely populated upstate areas. The absence of significant restraining effects is corroborated further by separate analyses of other multistate data.\(^3\)\(^6\)

It is doubtful whether restraints for which so little can be claimed justify the package store moratorium in New York or the stringent policy on removals of premises. It is not even clear that the policy is needed for effective maintenance of retail prices and, if it were, it is arguable that retail prices could be kept at about their present level without compulsory resale price maintenance or restrictive licensing.

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35 See Appendix B, Tests I and III.

36 Additional evidence in Entine, *op. cit. supra* note 30, also suggests the absence of any significant association between the number of on-premise outlets per adult population and on-premise consumption per adult. This is clear both for New York and for selected states with which New York is compared. However, this material must be interpreted with caution because separate figures for taverns and restaurants are not available.
by an excise tax. It can also be shown that the restriction of alcohol consumption by taxation would be less likely to create certain unwanted economic side-effects which in turn disrupt the whole regulatory system.

II. SOME ECONOMIC CONSEQUENCES OF THE PRESENT LICENSING SYSTEM

One way to clarify the economic effects of liquor licensing is to analyze the determinants of franchise value. The economics of franchise value should interest students of regulatory reform because it is the arbitrary creation and maintenance of artificially high franchise values which is widely believed to induce the corruption that breaks out periodically in the pursuit of these valuable license privileges.

A. Analytical Aspects

The economic value of liquor licenses is largely a function of supply and demand. The demand for licenses is related to the consumer’s demand for liquor; the supply depends largely on policies of the SLA. The value of liquor licenses can best be determined when licensed premises are sold and when licensees seek rights to remove premises to preferred markets. Because licenses extend to particular premises the locations of which cannot be changed without explicit approval, the value of the removal rights really reflects the anticipated value of the licensed premises after relocation.

Franchise value can probably be studied best by analyzing package store sale prices. Incorporated in these prices is the capitalized value of the income-earning opportunities conferred by the license. Franchise value is easier to segregate out here, when the licensee’s whole business is liquor, than for restaurants or bar-grills. Even so, it is not easy to determine what precise portion of the spread between sale price and the replacement value of physical assets is properly allocable to the license itself.

1. Package Stores

The scarcity value of package store licenses and removal rights appears to have emerged as follows:

No new license has been issued since 1948, after a doubling of licensees just after World War II. Incumbent licensees have

37 Aside from their precise value under varying conditions there seems to be no question that these licenses often have considerable value where their number is limited. See ALCOHOLIC BEVERAGE CONTROL 30; 1951 SLA ANN. REP. 13.

38 SLA Rule 17. [The SLA Rules are included in the volume of McKinney’s N.Y. Statutes which contains N.Y. ALCO. BEV. CONTROL LAW.]
therefore enjoyed growing opportunities for gain in the context of state-wide growth in population and markets.

Unable to secure new licenses, newcomers have had to buy existing premises at substantial premiums if they seek entry into the most profitable markets. However, few licensees will sell since most package store owners are generally small businessmen in the business "for keeps." They seem to sell out only for the most pressing reasons—moving away, bankruptcy, pending slum clearance.

As a consequence, the newcomer may have to buy poorer premises in less profitable markets and apply to remove to the more profitable sites. Existing licensees who are dissatisfied with their present location have also vied for privileges to remove to the more profitable sites.

Removals are now the sole mechanism for adjustment to changing market conditions. The SLA has modified a permissive policy by denying removal requests that would subvert other regulatory objectives such as preventing the clustering of package stores in a few very profitable centers. It thereby also seeks to forestall competitive pressures on price, and temptations to attract customers by illicit auxiliary services. Although removal applicants are probably more familiar with market conditions than a complete newcomer would be, the SLA apparently fears that the applicants may make errors in business judgment which would result in an oversaturation of the market; that the clustering of licensees even when warranted by high demand may still produce pressures for secret price breaks and illicit competitive tactics that stimulate consumption; and that the applicant's present community may be left "under-served."

In short, the removal policy theoretically imposes a principle of qualified profit maximization on package store licensees. To establish the "public convenience and advantage" of any move, it will not suffice to argue that one's income expectations are greater at the new site than at the old. Relative public need for a store in the two communities is determined ostensibly by additional factors such as the character of the two neighborhoods, their existing social problems, and their present ratios of package stores to population.

The value of removal rights seems to vary inversely with the ease with which the SLA grants them, or directly with the weight the SLA gives to evidence regarding deficient market support for more stores at the new location, a high ratio of stores to population in the new area, and a low ratio in the neighborhood to be vacated.
These estimates, however, may be colored by the fact that the four package stores closest to the proposed new site are virtually invited to contest the removal application.

So much for the value of removal rights under the present moratorium. Should the moratorium be lifted, the probable result would be that:

New licenses would have economic value to the extent they were not readily available for the asking by any and all applicants. Franchise value might still be substantial if the SLA were the sole supplier of licenses; if the licenses were issued in numbers limited by a formal mathematical rule, or limited less formally below the number which any neighborhood could support without restrictive licensing; if transfer applications were readily approved by the SLA; if the service standards imposed on licensees were vague; or if the risks of nonrenewal or revocation of licenses were slight.

The premiums offered for removal rights would depend on the number of new licenses, on their cost to applicants in legal fees, "pay-offs," and the current value of income foregone during any protracted processing-negotiation period, and, finally, on the degree to which older licenses might subject licensees to less stringent rules of conduct than new ones.

Thus, applicants would prefer a new license to a removal grant when the current discounted value of income expected from the former exceeds the current value of the income expected from the latter.

2. On-Premise Outlets

Removal rights also appear to have scarcity value in the restaurant field, though to a lesser extent. The moratorium imposed on new licenses during the years 1956-1960 undoubtedly raises issues similar to those just reviewed in the package store field. However, frequent waivers and exceptions for bona-fide restaurants probably mean that the restrictive effect of the moratorium was far smaller. Still another


40 SLA Rule 45.

41 On August 1, 1955 the SLA promulgated Rule 34-A which instituted a moratorium on all applications for on-premise licenses and removals. See 1955 SLA ANN. REP. 16-17. Then, on March 11, 1956, it instituted Rule 45 which redefined this statewide moratorium and prevailed until the courts invalidated it on April 1, 1960. See 1960 SLA ANN. REP. 10.
factor may have acted to create franchise value in the restaurant field. An SLA rule instituted in 1951 required that all prospective licensees establish their status as bona-fide restaurants by operating without a liquor license for 90 days.\textsuperscript{42} To avoid costly delay, restaurant owners have sometimes preferred to pay a premium and buy out premises that already have licenses, and then request permission to relocate.\textsuperscript{43}

One other factor may help to explain why franchise value is smaller in the on-premise than the off-premise field. Holders of on-premise licenses run greater risks of losing a license permanently should they fail to meet far more detailed rules of acceptable conduct. Statistics on the frequency of suspensions, revocations, and non-renewals for various categories of violations point up the different risks that confront licensees in the two fields.\textsuperscript{44}

A distinguishing feature of the on-premises policy is its progressive upgrading of the standards imposed on licensees. At present, no more than one-half of the business of any new restaurant, hotel, or bar-grill licensee is supposed to be derived from liquor sales. If imposed retroactively, this rule might well deprive many bar-grill owners of their licenses.\textsuperscript{45}

The process by which on-premise licenses acquire scarcity value can be summarized as follows:

The bona-fide restaurant provision, and the policy of upgrading standards, have made the acquisition of new liquor licenses increasingly difficult.

These restrictions, combined with the SLA's reluctance to impose its new, and more rigorous, standards retroactively have created a preference among bar-grill owners for old rather than new liquor licenses.\textsuperscript{46} Newcomers prefer to pay a premium for an old license, with its less stringent requirements, rather than apply for a new one, subject to more stringent rules. Old licensees will apply to remove premises rather than to sell out old premises and apply for a new license to enter a new market. The above

\textsuperscript{42}SLA Rule 34.
\textsuperscript{43}1955 SLA ANN. REP. 16-17.
\textsuperscript{44}See 1943 SLA ANN. REP. 34-37; 1942 SLA ANN. REP. 42-45; 1941 SLA ANN. REP. 42-43; 1939 SLA ANN. REP. 58-59. In more recent years the data were not sufficiently detailed.
\textsuperscript{46}The creation of at least two rather different classes of tavern licenses was apparent in talks with regulatory officials. See also 1960 SLA ANN. REP. 9-13; New York Retailer's Guide to the Law, Beverage Media Blue Book, April 1963, pp. 159-63 What appears to have happened is that newcomers will prefer to pay premiums for old licenses, with their less stringent food requirements, rather than apply for new ones subject to more stringent requirements. Likewise, old licensees apparently prefer to retain their old license and merely to request permission to change location rather than sell out and apply for a new license in a new market.
process is facilitated by the SLA’s practice of permitting a buyer to enjoy a licensee’s rights for the duration of his license term, and then renewing the license indefinitely, provided only that he complies with the less rigorous standards in force at the time of his initial purchase.

B. Empirical Aspects

Empirical study, limited mainly to the off-premise field, has revealed several predictable results of the package store moratorium. Briefly, the evidence indicates that a restrictive licensing policy has raised the gross sales of almost all licensees, but it has benefited some licensees far more than others.\(^\text{47}\)

1. Creation of Franchise Value

Franchise value is the present discounted value of future income expected to be earned by licensees and which is attributable to possession of a license. Expected earnings will be greater the fewer the number of licensees in the market and the harder it is to remove premises to better locations or to secure new licenses from the SLA. Two kinds of data cast light on the franchise value of licenses—statistics on gross sales of all package stores and aggregate purchase prices of package stores sold in selected markets. Neither approach to franchise value is definitive, nor does either make it possible to put a price tag on any particular package store license. Nonetheless, the results will at least show whether the analysis thus far is consistent with the available statistical evidence.

a. Gross Sales per Licensee

By holding constant the number of package stores during the past 15 years in the face of rising incomes and population, New York’s restrictive licensing policy has virtually guaranteed more business for almost all licensees. The data do not reveal precisely how liquor store sales per licensee have responded to changes in income, population, and traffic flow since 1948, but the probability seems high that incumbent licensees in many markets have enjoyed substantial economic gains.

In this regard, regression analysis shows that, for any number of off-premise licenses, a rise in median income, in population per square mile, or in per capita sales of eating and drinking places, will

\(^{47}\) The analytical-empirical techniques used in this section are adapted from Levin, *Economic Effects of Broadcast Licensing*, 72 J. of Political Economics (April 1964).
be associated with a rise in gross liquor store sales per licensee. Specifically, the analysis shows that in 1958, other things being equal, sales per store rose .77%, .58%, .55%, and .10%, respectively, for every 1% increase in income, population per license, traffic-transient flows, and population density. Because the regressions were conducted for a cross section of data in a single year, broad conclusions about their relevance to changes in liquor sales per store over time cannot be drawn. The most that can be safely predicted is the direction—not the magnitude—of changes in sales induced by changes in income, population, and traffic flow. But the evidence is incontrovertible that, by issuing no new package store licenses since 1948, notwithstanding New York's general economic expansion, the SLA's licensing policy has bolstered the gross sales of almost all licensees.48

The results of studies of all states, and of thirty-two license states, are statistically less significant.49 The relative importance of each independent variable is also noticeably different from its relative strength when computed for New York only. To be sure, the explanatory power of income is greater than that of any other factor in both multistate tests, as is true in New York. But the power of sales of eating and drinking places is much smaller than in the New York study; and the coefficient for population density is actually negative rather than positive. Also, liquor store sales per licensee in the license states vary, other things being equal, only +.08% for every 1% increase in population per licensee, compared to +.58% in New York. Nonetheless, this coefficient is still consistent with the thesis that license limitation bolsters the revenues of liquor licensees. Even more to the point, finally, is the fact that sales per licensee in all forty-nine states studied vary +.33% for every 1% increase in population per licensee.

b. Package Store Purchase Prices in New York City, Long Island, and Westchester

Table 4 shows the sale prices of all package stores sold in New York City, Long Island, and Westchester in 1950 and 1958. For

48 This conclusion is established somewhat differently in Entine, op. cit. supra note 30. Of interest finally is the very pronounced gross relation between the level of adult population in 1958 and the level of gross liquor store sales in sixty-two counties (r = .97908). The experience of particular licensees will naturally depend on the distribution of gains in income and population as between the several counties. Given the distribution of licenses, a pattern of differential changes in income and population will over time necessarily produce differential economic advantages and disadvantages for package stores located in different markets.

49 See Appendix B, Tests V and VI. The smaller values of the multiple correlation coefficient (.65 and .39, respectively, compared to .85 for New York) may simply reflect in part the fact that states are poorer "proxies" for retail liquor markets than counties are. By the term "proxy" I refer to the use of some statistical variable "to represent" some true economic force for which statistics cannot be directly obtained.
**TABLE 4**

Analysis of Package Store Purchase Price in New York State—
Zone 1, 1950 and 1958 60

1958 Transfers
Aggregate Purchase Prices as Percentage 61 of Aggregate Gross

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<td>45.2</td>
<td>39.2</td>
<td>30.6</td>
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<tr>
<td>Queens</td>
<td>47.6</td>
<td>47.8</td>
<td>42.2</td>
<td>35.0</td>
<td>22</td>
<td>11</td>
<td>(1)</td>
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<td>38.1</td>
<td>43.2</td>
<td>37.8</td>
<td>2</td>
<td>4</td>
<td>(—)</td>
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<td>5</td>
<td>8</td>
<td>(8)</td>
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<td>33.5</td>
<td>23.8</td>
<td>1</td>
<td>5</td>
<td>(5)</td>
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<td>43.3</td>
<td>34.4</td>
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<td>7</td>
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<td>47.9</td>
<td>46.6</td>
<td>38.8</td>
<td>1</td>
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**Median**       | 53.6 | 47.8 | 42.2 | 34.4 | 29.8 | 20.1 | 18.0 | 16.5 | 13.7

1950 Transfers
Aggregate Purchase Prices as Percentage of Aggregate Gross Sales in

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<tr>
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<td>48.6</td>
<td>47.9</td>
<td>46.6</td>
<td>38.8</td>
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No Transfers in 1950

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60 Derived from the files of the SLA. Purchase prices include all payments for furniture, fixtures, and goodwill, but excludes inventory. The calculated data include all recorded transfers during 1950 and 1958 in Zone 1, except for cases where only one-half interest was sold, information was incomplete, or there was no monetary consideration.

61 All percentages relate to aggregates for the number of stores specified.

62 Aggregate sale and purchase prices refer exclusively to transfers where 1949 gross sales were reported.
each county a calculation was made of the ratio of the aggregate prices of the stores sold to their aggregate gross sales during the year preceding the sale and to their gross sales in selected years afterwards. The trends in these ratios over time would suggest trends in actual returns on total investment. Any change in these ratios as between 1950 and 1958 would further suggest the extent to which the current value of income-earning expectations may have changed.

In regard to aggregate purchase prices of package stores in these counties an additional conclusion can be drawn. The cost of entry appears to have risen noticeably between 1950 and 1958. Thus, the median of aggregate purchase prices for transferred stores was $19,490 in 1950, as compared with $39,503 in 1958. The ratio of these median prices to gross sales for the year prior to sale rose from 29.8% in 1950 to 47.8% in 1958. The increase in cost of entry was especially apparent in Nassau County, where the comparable prices went from $19,000 in 1950, 34% of gross sales, to $54,850 in 1958, 58% of gross sales; and in Suffolk County, where median prices rose from $16,000 in 1950, 29.7% of gross sales, to $45,000 in 1958, 49.4% of gross sales. If the steady growth of liquor sales after 1950 helped generate buoyant income hopes, package store buyers would be expected increasingly to capitalize these expectations in their purchase prices. The marked rise in the aforementioned ratios suggests that this is precisely what happened.

Thus, the buyer's knowledge of the steady growth of gross liquor sales apparently generated future income expectations high enough to warrant a substantial rise in the market value of package stores between 1950 and 1958. The growing sales volume of the stores in the sample probably reflects the influence of rising family income—or of rising population in some cases—in a situation in which the number of licenses in each market remained almost the same.\(^5\)

Also of interest is the magnitude of the aggregate purchase prices. In eighty-two cases in which package stores were sold outright in 1958, purchase prices totalled $3,258,900 exclusive of inventory. Assuming replacement value of furniture and fixtures of approximately $12,000 per store, there would remain over $2,200,000 as a rough measure of the value of good-will, leaseholds, working capital, and the licenses themselves. Without trying to put any price tag on licenses for tax purposes, there is probably one sense in which the whole spread between aggregate purchase prices and estimated replacement value of fixed assets may be said to constitute the value of the eighty-two licenses. After all, no one may enter or remain in the

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\(^5\) In Kings and Bronx counties the number of licenses actually declined about 10%. 
package store business without a license; no one may remove or sell his premises without SLA approval; and limitations on the number of licenses in the market clearly make package store operation more profitable and raise the premium one must pay to enter the market.

However, licensees show varying ingenuity in developing their business. It may, therefore, be more reasonable to view licenses as imposing conditions under which varying amounts can be earned rather than as determining precisely what amounts will be earned. Nonetheless, even after adjusting the spread between aggregate purchase prices and estimated value of fixed assets to allow for considerable good-will, going-concern value, and working capital (perhaps an average of 35% in all), the residual estimate of franchise value remains impressive.\textsuperscript{55}

c. The Profitability of Package Stores

I have not attempted to estimate the "profitability" of package store operation in New York State. This is because estimates of "rates of return" based upon the available accounting data are irrelevant for that purpose. For example, if the present owner of a liquor store first acquired his property in 1955 by paying $50,000\textsuperscript{56} and in 1962, after meeting all expenses, the store produced an income of $10,000, the owner would have obtained a 20% rate of return. If, however, the store was resold in 1961 by the original buyer for $100,000, the new owner would have earned, in 1962, a 10% rate of return on his original investment of $100,000. Thus, the "rate of return on investment" in a package store depends largely on when its present owner acquired it. This rate of return is obviously of great concern to any package store licensee since it shows, among other things, the soundness of his business judgment. But it is irrelevant to public officials or the general public since there is no reason to compensate licensees for their errors in predicting regulatory actions which may jeopardize their profits.

\textsuperscript{55} Many economists will object to allocating this much to good will, etc. The present restrictive licensing system actually deprives package store owners from fully exercising their business initiative. Licensees bear few if any risks with regard to the possible entry of new competitors. The law drastically curtails their freedom to compete in price or advertising, further reducing the risks they face in the market. Some economists may even wonder whether they are providing any managerial service at all commensurate with the returns obtained, or whether licensees are often mere beneficiaries of an economic rent inherent in their market position. However, if we apply the rough and tentative relationships reviewed above to all 4,236 package stores in New York, aggregate franchise value would stand at a minimum of $113,648,700. Further adjustments are undoubtedly needed to allow for variations in the distribution of earnings.

\textsuperscript{56} In this example we assume that the store's furniture and fixtures are worth $10,000 with the remainder of the purchase price paid for the license. We also assume that the value of furniture and fixtures is the same in 1962.
If there exists a market in which liquor stores can change hands, the prospective future earnings of a store will be taken into account by the seller and prospective buyers. The estimates of these earnings will reflect, among other things, predictions of the rules and regulations that will continue to govern package store operations. When the current annual income of a store constitutes a low percentage of its current market value, say 3%, either most persons in the market view the store as a “safe” investment or they expect its annual income to increase in the future. Conversely, when the current annual income of a store constitutes a high percentage of its current market value—for example, 20%—either the market views the store as a high-risk investment or the market anticipates that its future annual income will fall.

Clearly, then, the current market value of a package store is affected greatly by how its owner and prospective buyers view the future of the present moratorium on new licenses. If they become increasingly confident that the moratorium is here to stay, package store prices will rise. If they begin to believe that it will be relaxed, package store prices will fall. But whatever the rate of return on investment for bookkeeping purposes, three important truths must be stressed. Inflated franchise values are perfectly consistent with low rates of return on investment, and it is the franchise values which create regulatory problems. Licenses that permit a favored few to operate package stores are valuable because their number is limited by SLA policy, not because they represent productive social capital employed in retail liquor distribution. However large the premium which a buyer may pay for his store, he gains no property rights in his license; he does not even gain a guarantee that the moratorium on new licenses will remain in force long enough for him to recoup his investment.

2. Differential Economic Impact of Restrictive Licensing

Restrictive licensing operates not only to raise the gross sales and profitability of package stores but also to intensify differences in the profitability of licenses in different markets. Ordinarily, in unregulated industries where the scale of efficient operation is small, increases in income, population, and demand will cause new firms to enter. Since the entry of new firms is difficult under the present licensing system, licensees in lush markets enjoy important economic advantages.

Licensees in the poorer, less desirable markets, however, are affected in the opposite way by restrictive licensing. In an unregulated
industry they could move to more attractive markets, but this mobility is curtailed by the SLA's policy on removal applications. Thus, licensees in profitable locations are protected against new competition, and less fortunate licensees are prevented from relocating. Restrictive licensing, therefore, does not necessarily give every licensee a gold mine—it may even reduce the earnings of some. The system relieves some lucky licensees from having to exercise much discretion in risk-bearing, and it prevents the unlucky ones from being able to do so.\(^{67}\)

This differential impact on package store licensees can be illustrated by a brief example. Suppose that there are two markets—\(A\) and \(B\)—both of which had three package stores in 1948. Suppose also that by 1962, income, population, and traffic flow had remained about the same in market \(A\), but had doubled in market \(B\). Clearly the licensee lucky enough to be located in \(B\) would gain a windfall if no new licensee were allowed to enter his market, and if licensees at \(A\) were not allowed to move there. Likewise, the licensees in market \(A\), although now relatively worse off, would be unable to show initiative in trying to improve their status.

Except for some intracounty removals, the above example accurately describes what has happened in New York State since 1948:

Assuming a rational geographical allocation of package stores when the moratorium was imposed—an allocation corresponding roughly to tastes, population, and income—marked disparities in the rate of population and income growth since 1948 would presumably have had a differential impact on the fortunes of package stores in different markets. That is, one would expect different windfalls to be enjoyed by different licensees.

That this uneven distribution of windfalls has occurred in New York is suggested by data on the actual percentage changes in population, income, and liquor store sales in New York, 1950-1960 (Table 5).

Further evidence consistent with a hypothesis of differential economic impact is contained in Table 6, which divides New York State into three zones. When 41.8% of licensees, with gross sales of $79,000 or less, handle only 17.9% of aggregate sales, and a scant 8.2% of licensees, with gross sales above $239,000, handle as

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\(^{67}\) This provides an answer of sorts to those who cite statistics on package store mortality and average profit margins or returns on net worth as evidence that restrictive licensing has had no significant economic effect. Even when average financial ratios for package stores are in line with those in other retail businesses there remains the question of how the profits and losses are distributed among different classes of licensees. A more liberal removal policy might help to rectify this situation. However, the profit data cited undoubtedly reflect also the continued existence of inefficient retailers under the shield of resale price maintenance.
TABLE 5

Median Percentage Changes in Gross Liquor Store Sales and Other Economic Variables, All New York Counties, 1950-1960

<table>
<thead>
<tr>
<th>Percentage Changes in</th>
<th>Median Percentage Change</th>
<th>Range of Percentage Changes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Median Income</td>
<td>87.5</td>
<td>54.7 to 114.6</td>
</tr>
<tr>
<td>Adult Population</td>
<td>11.1</td>
<td>-13.4 to 141.5</td>
</tr>
<tr>
<td>Sales per adult capita</td>
<td>61.0</td>
<td>-30.7 to 269.9</td>
</tr>
<tr>
<td>Sales per licensee</td>
<td>77.4</td>
<td>11.0 to 291.3</td>
</tr>
<tr>
<td>Licensees per capita</td>
<td>.1</td>
<td>-.6 to .2</td>
</tr>
</tbody>
</table>

much as 25.9% of New York’s business, doubts are raised about the fairness of the moratorium. Similar doubts are raised by variations in the distribution of sales within, and among, the three regulatory zones. Indeed, even if comparable retail trades showed comparable frequency distributions of sales, the fact that the New York data pertain to a tightly controlled situation would still lend credence to the thesis regarding the differential impact of licensing.

A final indication of this differential impact is suggested by the prior discussion of package store profitability. Similarly located, licensees enfranchised before 1948 have undoubtedly benefited more from the moratorium than those who have bought package stores since then. Holders of “old licenses” know they have a “good thing” and are therefore unwilling to sell unless they get a price that reflects what they could earn by continuing to operate the stores themselves. Hence, newcomers who buy stores from them must ordinarily pay a sum equal to the discounted value of the future income that the seller could have earned.

Holders of “new licenses” can have benefited from the moratorium for only one of two reasons. Either the party from whom they acquired the store after 1948 underestimated the income that he could


59 The significance of Table 6 cannot be minimized by claiming that the licensees who handle the larger grosses have simply invested more from the beginning. Furniture and fixtures hardly vary that much. If licensees had to buy entry rights from someone else their purchase price merely reflects the discounted current value of the income they expected to earn at the desired location. A willingness to pay premiums to enter a preferred market is hardly inconsistent with the thesis that licensees doing the most business, as a class, operate in the most profitable markets.
TABLE 6


<table>
<thead>
<tr>
<th>Gross Sales (in thousands)</th>
<th>Zone I</th>
<th>Zone II</th>
<th>Zone III</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Cumulative Percentage of</td>
<td>Cumulative Percentage of</td>
<td>Cumulative Percentage of</td>
<td>Cumulative Percentage of</td>
</tr>
<tr>
<td></td>
<td>Licensees</td>
<td>Sales</td>
<td>Licensees</td>
<td>Sales</td>
</tr>
<tr>
<td>39 and under</td>
<td>2.5</td>
<td>.4</td>
<td>33.2</td>
<td>13.6</td>
</tr>
<tr>
<td>79 and under</td>
<td>25.4</td>
<td>9.4</td>
<td>76.9</td>
<td>54.7</td>
</tr>
<tr>
<td>119 and under</td>
<td>50.9</td>
<td>25.3</td>
<td>93.2</td>
<td>80.7</td>
</tr>
<tr>
<td>159 and under</td>
<td>69.8</td>
<td>41.7</td>
<td>97.4</td>
<td>89.8</td>
</tr>
<tr>
<td>199 and under</td>
<td>83.0</td>
<td>60.6</td>
<td>98.7</td>
<td>94.1</td>
</tr>
<tr>
<td>239 and under</td>
<td>87.6</td>
<td>71.0</td>
<td>99.1</td>
<td>95.4</td>
</tr>
<tr>
<td>279 and under</td>
<td>91.7</td>
<td>77.7</td>
<td>99.6</td>
<td>97.5</td>
</tr>
<tr>
<td>319 and under</td>
<td>95.4</td>
<td>84.6</td>
<td>99.6</td>
<td>97.5</td>
</tr>
<tr>
<td>Over 319</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
</tr>
</tbody>
</table>

Average Sales ......... $180,000  $61,000  $78,000  $120,000
Median Sales ......... $118,000  $50,000  $60,000  $95,000
First Quartile ......... $78,000  $30,000  $38,000  $55,000
Third Quartile .......... $180,000  $76,000  $78,000  $150,000

Derived from the files of the SLA. The three zones refer to the SLA's administrative-geographic groupings of all New York counties: Zone I centers around New York City, Zone II around Albany, and Zone III around Buffalo.
have earned by retaining the store; or the party who sold was forced to do so by hardship—ill-health, old-age, death of a partner, etc.—at a time when the market did not share his optimism respecting the earning power of his store. Given the rapid growth of population and income in New York State since World War II—a growth that few people predicted in 1948—it seems probable that some late-comers to the package store trade have received some part of the lucrative windfalls conferred by the moratorium. But, on balance, the major beneficiaries have undoubtedly been those persons who managed to get licenses before 1948

C. A Comment on Resale Price Maintenance

This Article will not deal with the effects of resale price maintenance on the New York package store business. However, a word is in order on its relation to restrictive licensing, franchise value, and regulatory reform.

The more important economic effects of price maintenance without entry control are well-known—wider profit margins for the retailer than under competition, the entry of more retailers than otherwise, the bidding up of distributor costs by spreading a given volume of sales over more and more outlets, and the diversion of competition from price to service and advertising. The final result is that, under price maintenance without entry control, the original firms will eventually earn no more than at the outset since their initial profits will cause new firms to enter the field. The case of price maintenance with entry control is somewhat different. Under the present package store moratorium, for example, wider profit margins do not result in the entry of additional firms; rather, entry into choice markets is through the relocation of an existing store.

As noted earlier, for the right to change location licensees are willing to pay premiums that vary directly with their expectations of future income. These expectations will be higher, and the value of the removal rights greater, the more effectively the SLA enforces resale price maintenance, and the longer its package store moratorium is expected to continue. In short, franchise value is greater when entry control and price maintenance are combined than when price maintenance is imposed alone.

Franchise value would probably be much smaller today had existing entry controls been combined from the outset with the im-

position of maximum prices designed to limit the licensee to some "fair" rate of return as in the case of public utilities. In this field, the market value of franchises appears to have been deflated, and speculation in licenses curtailed, by combining rate maxima, tangible service standards, and provisions to exclude franchise value from the rate base for rate-fixing purposes.

In radio and television almost the reverse is true. Conduct standards are vague and elusive. Renewals are virtually automatic and the risk of revocation nil. Rates are completely unregulated and licenses freely transferable in fact, if not in legal theory. The number of licenses, however, is tightly limited by technical constraints. The net result is that TV franchises are extremely valuable and there is an active market for them.\(^{63}\)

The above discussion is directly relevant to the case of package stores since entry is tightly controlled without the imposition of maximum prices or controls on the rate of return. On the contrary, the advocate of strict alcohol consumption control would argue that the higher the price charged to the consumer the better. It is minimum prices that are imposed and policed to reinforce the guarantee that licensees will not cut price whatever the temptation. The obvious question is what does the community get in return for this. Are the conduct standards imposed so rigorous, and the licensee's community responsibilities so onerous, as to repay the state in kind? If not, what alternate arrangements might improve the situation, especially when the known economic consequences of restrictive licensing are balanced against its inconclusive effects on alcohol consumption?

### III. The Deterioration of Regulation \(^{64}\)

The economic consequences of New York's licensing laws appear to have seriously disrupted the whole regulatory process. They have diverted the SLA, already overburdened and understaffed, into endless attempts to plug holes in the regulatory dike. Even when acting rationally from the viewpoint of its own rules and procedures, the SLA is necessarily forced to divert more and more of its energies from the substantive problems of alcoholic beverage control. Formal administrative rationality diverges increasingly from substantive rationality.

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\(^{64}\) What follows should be considered in light of the obvious fact that able, honest administrators are crucial for fair and efficient regulation. The point is simply that honesty and competence do not suffice. Outmoded regulatory arrangements can ruin even good men. This does not deny, of course, that bribery and corruption are more likely when the quality of administrator is dubious.
Specifically, the picture that emerges is this: 65

Even when regulatory-licensing standards are clear, coherent, and concrete, they are hard enough to apply in cases involving difficult choices between qualified candidates. The rationing problem is even more disconcerting when standards are vague and inconsistent, and when the public consequently suspects administrative integrity even when regulators try to be as fair as possible. 66

A few spectacular cases of improper influence, impropriety, and payoffs discredit the whole system. 67 These cases have apparently sufficed to lead licensees and the general public into thinking that improper influence and payoffs are the only sure way to gain fair treatment. 68 Integrity of the SLA is questioned and public confidence deteriorates.

Rather than deal with the substance of regulation, the SLA is diverted to defending its honor and seeking out endless safeguards of procedural fairness. Time, energy, and resources are dissipated increasingly in reviewing such things as the relation between a lawyer charging contingent fees—or the number of times he appears before the SLA annually—and his rate of success in winning cases for clients. 69

There are several questions that the SLA continually asks when policing the abuses which its own policies have actually helped to create. Does an applicant's ability to hire one of the specialized legal firms practicing in this area militate strongly in his favor? Do enough people believe this is so to enable these firms to exact fees far higher than otherwise? Are the credentials of those who practice before the SLA adequately screened? Can they be so screened without licensing the lawyers themselves? 70

65 Recent corroboration of this outline appears in N.Y. Moreland Comm'n on the Alcoholic Beverage Control Law, Report and Recommendations No. 1, at 8, 14, 20-21, 28-29 (1963).

66 As already suggested, the SLA's "rationing" problem occurs when it is forced to choose between multiple removal applicants. Then it fears for excessive "clustering" of package stores in a few lush markets. It occurs also when a choice must be made between competing applicants for new licenses, as in the flood of postwar package store applications in 1946. The need to choose between applicants may well occur wherever unlimited licenses for all qualified applicants are not forthcoming. These matters are examined at greater length in a discussion of license distribution by rationing in Part IV-C below.


70 See authorities cited notes 67-69 supra.
Will the applicant be the "bona-fide" owner, or is he a "front" for someone else? \(^{71}\) Does the applicant for a new grant intend to stay put, or to request early permission to remove to a more profitable market, and then resell at a capital gain? Will making him promise not to move for two years, or not to sell out for two years, act as an adequate deterrent? \(^{72}\) Can improper influence, pay-offs, and bribes be curbed by requiring applicants to list everyone who has assisted them together with full information on compensation paid or other arrangements made? \(^{73}\)

In brief, the SLA spends an impressive portion of its energies and resources policing abuses which its own policies and procedures exacerbate. Regulatory efficiency is judged increasingly by the Authority's success in preventing violations of its regulations rather than in testing their validity and revising them in the light of known effects. \(^{74}\) Regulatory efficiency comes to be judged also by the speed with which applications are processed and hearings conducted, rather than by the validity of the licensing criteria themselves and of the case for restrictive licensing. \(^{75}\) Any search for fundamental reform is scotched in hasty attempts to patch up existing procedures and to gain better compliance with old rules. Viable alternatives to restrictive licensing and price control are not even considered, let alone investigated.

IV. ALTERNATIVE APPROACHES TO REFORM

The purpose of regulatory intervention in the liquor business is to promote public and not private interests. Elsewhere, when state regulation confers coincidental private advantages on those fortunate enough to secure franchises, the community has claimed a quid pro quo. In public utilities this is done by imposing elaborate rate controls


\(^{72}\) 1955 SLA ANN. REP. 11-16.

\(^{73}\) 1951 SLA ANN. REP. 20-21.

\(^{74}\) A good case in point is the fear sometimes found in regulatory circles that the enforcement of minimum consumer resale prices would be made extremely difficult if wine or beer were deregulated, or if the distribution of package liquor were opened up to groceries, supermarkets, or drugstores. Honest differences of opinion exist on the wisdom of giving liquor licenses to such establishments, or of deregulating beer and wine sales at retail. However, the enforcement of resale price controls hardly constitutes an adequate reason for rejecting these possibilities out of hand.

\(^{75}\) See 1955 SLA ANN. REP. 6; 1956 SLA ANN. REP. 16-18; 1957 SLA ANN. REP. 11; 1959 SLA ANN. REP. 8-10; 1960 SLA ANN. REP. 6-7; 1961 SLA ANN. REP. 7-8. This is not to deny that lengthy delays in application processing and hearings are serious regulatory problems. The point is only that delays may be needed for a careful, meaningful selection and screening of applicants. But without a comprehensive empirical study of the total effects of restrictive licensing, we cannot judge how much cost, in delays and improper influence, is really worth incurring.
LIQUOR LICENSING

to insure that consumers gain from the efficiency of large scale production. In utilities and transportation, licensees are sometimes required to subsidize certain desired but uneconomic services. The hard questions posed by these analogies is whether the conduct standards imposed on package store licensees today are so meaningful, their enforcement so rigorous, and the restraining impact of restrictive licensing on alcohol consumption so effective, that licensees "earn" the valuable franchise privileges they currently enjoy; or whether there are in fact other, less restrictive ways to administer the system of liquor control.

A. A Nonrestrictive Approach: Unlimited Package Store Licenses

A crucial distinction must be made between restrictive and nonrestrictive licensing in the alcoholic beverage industry. Nonrestrictive or "qualitative" licensing is frequently used to maintain standards of professional competence required for protection of the public. In theory at least, every qualified applicant can secure a license for the asking once he establishes his qualifications. The art of nonrestrictive licensing is to designate a few clear-cut standards vital to the "public interest" and likely to suffer in an unregulated situation, and then to license any qualified applicant who meets them. It is not suggested that felons or criminal elements, or those who are associated with producer-wholesaler interests or with the SLA, cannot be excluded from securing or retaining off-premise liquor licenses. It might even be desirable to exclude bona fide applicants

76 Whatever its initial purposes, licensing of this sort may be manipulated to restrict entry into a business or profession. See Moore, The Purpose of Licensing, 4 J.L. & ECONOMICS 93-117 (1961). But qualitative licensing is formally and explicitly designed to safeguard public health and safety and standards of professional competence. Its perversion to restrict competition is one thing; the deliberate imposition of quantitative limits on licenses for qualified applicants is something quite different. See Moore, supra at 117. See generally CLARK, SOCIAL CONTROL OF BUSINESS 95, 490-94 (1939); EDWARDS, MAINTAINING COMPETITION 201-15 (1949).

77 The bona-fide restaurant rule is an imperfect attempt at qualitative liquor licensing. To be sure, the SLA has not always applied the rule this way. It has sometimes sought to reduce the number of on-premise outlets. See 1955 SLA ANN. REP. 16-17; 1951 SLA ANN. REP. 9-13; 1942 SLA ANN. REP. 13-14; 1939 SLA ANN. REP. 9; 1937 SLA ANN. REP. 7. However, any bona fide restaurant can get a license for the asking today. See 1960 SLA ANN. REP. 10-14. The theory is that restaurants are primarily interested in selling food and therefore compete more in the character and price of their cuisine and service than in the sale of liquor. Hence, licensing has been far more restrictive here. Nonetheless, corruption, bribery, and falsification have resulted from attempts to impose food requirements on taverns and bars, and it has therefore been proposed that separate classes of licenses be issued to restaurants and taverns. See 2 N.Y. MORELAND COMMISSION, REPORT AND RECOMMENDATIONS ON THE ALCOHOLIC BEVERAGE CONTROL LAWS 7-9, 16-23 (1964).

78 For a list of criteria prescribed by public administrators as crucial in retail liquor licensing see ALCOHOLIC BEVERAGE CONTROL 69. On the criteria presently prescribed in laws throughout the country see id. at 107-08.
unable to meet stiffer financial standards than those presently imposed. Larger bonds could be required to be posted with the SLA, to be forfeited in the event of violations.\textsuperscript{79} This is significantly different from the current policy that excludes applicants even though they satisfy all prescribed standards.

A policy of nonrestrictive licensing of package stores, and the replacement of resale price maintenance by a tax, would eliminate the bulk of franchise value in off-premises distribution. At the same time, it would eliminate a major source of improper influence, regulatory manipulation, and bribery. Corruption and bribery might still occur when rules are obsolete and unclear. But if all qualified applicants for liquor licenses are accommodated, those complex cases in which competing applicants seek the same valuable rights will never arise.

Defenders of the status quo may still contend that nonrestrictive licensing will increase the likelihood of irresponsible licensee behavior toward minors and alcoholics. But this need not happen if sufficiently rigorous financial qualifications are prescribed. The art of determining "adequate financial responsibility" lies at the heart of qualitative licensing policy.\textsuperscript{80}

To be sure, even under a nonrestrictive system, a Licensing Authority that screens the qualifications of an applicant may act arbitrarily. It is admittedly hard to institute minimal safeguards to maintain the "plane" of competition without at the same time creating opportunities for powerful groups to turn these safeguards to their own economic interest. However, at least one fruitful source of corruption and bribery is absent when the franchise value created by restrictive licensing is eliminated.

B. A Nonrestrictive Approach: Resale Price Maintenance, Exclusive Liquor Stores

Nonrestrictive package store licensing is only the first step toward eliminating excessive franchise values. A thoroughgoing nonrestrictive approach must also include the relaxation or abolition of price maintenance and of the rule requiring that all liquor be distributed exclusively by specialized liquor stores. But such reforms, like unlimited

\textsuperscript{79} Financial responsibility is included among the ten preferred licensing criteria of the Joint Committee of the States. \textit{Id.} at 69. However, New York is not among the nine states whose statutes explicitly require applicants to demonstrate adequate financial responsibility. \textit{Id.} at 107.

licensing, are usually rejected out-of-hand because of their alleged threats to temperance.

1. Resale Price Maintenance

It is widely held that artificially high liquor prices are an effective technique to deter consumption. But even granting the premise, it can be argued that a tax will achieve this objective more efficiently than the SLA’s current licensing and pricing policies do.

When prices are raised above market level by resale price maintenance, opportunities for extraordinary profits are created. Liquor dealers thereby become the main beneficiaries of a regulation designed to restrict consumption. More precisely, price maintenance must result either in the retail liquor dealer’s earning extraordinary profits, in his providing additional services to his customers, or in inefficiency. For if the minimum prices are operational they must be set at higher levels than would prevail under free competition. Hence, if price maintenance does not result in higher profits it can only be because dealers have passed these profits on to the customer in additional services or because they have become less efficient.

From a social point of view none of these possible effects is desirable. A system which permits retail liquor dealers to earn extraordinary profits cannot be justified on economic grounds. Nor can a system that tolerates and even encourages inefficiency be justified. If both extraordinary profits and inefficiency are avoided as a result of providing additional services, the achievement of the one explicit objective of social value at which the dealers claim resale price maintenance is directed—restraining the level of consumption—will be at least partly frustrated. This is because these services—if they are not entirely useless—will reduce the cost of liquor, thereby, at least in part, offsetting the higher prices that result from the regulation. If the services provided by the dealers are entirely useless, their provision is as socially wasteful as inefficiency.

In the case of taxes, on the other hand, the state, rather than the dealers, reaps the benefit of the higher prices. Since raising prices by imposing taxes does not create opportunities for extraordinary profits, the need for official restrictions on the number of firms in the industry is eliminated. In fact, replacing the “fair trade” regulation by additional taxes eliminates the only rational justification for the current restrictive licensing policy.81

81 It is somewhat ironic that the replacement of “fair trade” by higher liquor taxes could even result in a reduction in the number of package stores. This could happen if some firms have survived only because of the umbrella which “fair trade” provides. The elimination of this umbrella may lead not only to increased efficiency
The objection most frequently raised against higher excise taxes is that they will increase the temptation to engage in unlicensed production and distribution of distilled spirits. Liquor regulators have long been opposed to giving excessive weight to the revenue-producing function of liquor taxation, even though they acknowledge its value in consumption control. Their principal fear is that heavy taxation for either purpose may, at some "empirically unmeasurable and unpredictable point," make "bootlegging" economically attractive. Indeed, the hazards of "excessive taxation" are often lamented in terms strikingly reminiscent of the aforementioned hazards of "excessive competition." Yet, there is a real question as to whether the former are any more valid than the latter.

The fears that higher liquor taxes would precipitate additional bootlegging are obviously irrelevant when a state-wide excise tax, imposed after price maintenance is dropped, merely keeps prices at their previous level. This would be true if price maintenance were replaced by a tax on liquor equal to the difference between its market price and the present control price. Also, it is by no means clear that the level of liquor taxes in New York is already so high that all increases must necessarily precipitate the dangers just mentioned. Furthermore, empirical estimates of the degree of responsiveness of liquor consumption to price change raise doubts about the magnitude of any increase in consumption that would follow the return to free-market pricing,

of the firms which remain, but to elimination of less efficient firms. The continued existence of the latter really confirms the power of entry control and price maintenance to support inefficiency. It does not confirm the claim that off-premise licensing policies have no significant economic impact because "many licensees are struggling for survival."

82 See Joint Committee of the States To Study Alcoholic Beverage Control Laws, Impact on Alcoholic Beverage Control of Taxation and Mark-up 10, 26, 29-31, 34 (1953) [hereinafter cited as Taxation and Mark-up].

83 Id. at 17, 22-23, 25, 29-31, 33-34. See also N.Y. State Comm'n on Alcoholic Beverage Control Legislation, First Report 5 (mimeo. 1933).

84 Compare Taxation and Mark-up 12, 30, 33-35, with discussion in Parts I-A and I-C of this Article.

85 There is some doubt about the real burden of New York's alcoholic beverage tax burden today. Two measures frequently used are the level of per capita tax revenues derived from that source and the percentage of total state revenues derived therefrom. On neither account is New York really out of line with other states. Thus, in both 1950 and 1960 New York ranked twenty-eighth of all states in per capita revenues, and thirteenth of thirty-two license states. However, she ranked only twenty-sixth in the percentage of total tax collections derived from alcoholic beverage taxes in 1953 (6.5%) and actually fell to forty-first place in 1961 (3.9%). Even looking only at the license states, New York fell from tenth to twenty-fifth place in its percentage of alcoholic beverage tax revenues, and from seventh to thirteenth in the percentage it derived from distilled spirits only. These statistics are derived from 1962 Facts of the Licensed Beverage Institute; 1954 Facts of the Licensed Beverage Institute; Distilled Spirits Institute, Annual Statistical Review 2-4 (1960).
even without a tax.\(^{86}\) However, uncertainty about the effect of complete removal of price maintenance points up the importance of scrutinizing at least two transitional measures. One would be to impose the tax just described, but then reduce it over a specified period, in stages, until liquor prices are completely market-determined.\(^{87}\) Another option would be to remove different types of liquor from minimum price controls at periodic intervals to give consumers and distributors time to adjust.\(^{88}\)

The replacement of price maintenance by a tax would not only forestall the purported threat to temperance but also reduce the value of liquor licenses and, accordingly, the threat of improper influence and manipulation. Just as the interaction of entry controls and price maintenance has aggravated franchise values in this field, so the elimination of both, even on a gradual basis, would deflate them. In the final analysis, restrictive licensing and price controls must be viewed together. Any decision to open entry without dropping price maintenance will, eventually, result in higher prices than if prices were left free, greater excess capacity, and lower distributive efficiency.\(^{89}\) Policing problems will also be greater than when prices and entry are both controlled. The only justification for paying this price of economic inefficiency is the alleged promotion of temperance. Aside from the dubious character of artificially high liquor prices as a control technique, a tax appears capable of achieving the same result without impairing economic or regulatory efficiency to the extent that entry and price controls do.

2. Specialized Liquor Stores

The regulation that limits the sale of packaged liquor to specialized liquor stores is a logical outgrowth of the theory of restrictive licensing. The SLA is better able to control the number of outlets when it can

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\(^{86}\) In reviewing earlier studies of price elasticity of demand for distilled spirits, Harold L. Wattel notes that in only five out of thirteen studies was demand found to have elasticity greater than unity. In all other cases, a 10% decrease in price was estimated to be followed by an increase in liquor sales ranging from a mere 1.3% to 9.2%. See Wattel, Resale Price Maintenance in the Liquor Industry 52-53 (N.Y. Moreland Comm'n Paper No. 5, Oct. 1963). Although Wattel's study of more recent data for Pennsylvania, and for all monopoly states, produced measures which he deemed "insufficiently significant," he concluded that "the history of the industry suggests that . . . the demand curve is for the most part price inelastic." Id. at 54.

\(^{87}\) Id. at 58.

\(^{88}\) Ibid.

\(^{89}\) Specifically, a flood of newcomers will enter and share a fixed volume of business, with less business for the average licensee. There may even be greater pressures on the distillers for higher markups, and conceivably higher bottle prices for the consumer. Insofar as sales are spread among more sellers, costs may rise even though returns on investments are steady. As costs rise, profit margins, although higher than under competition, come to look reasonable, and it is hard to know what the costs would be without price maintenance. See Yankey, The Economics of Resale Price Maintenance 73-83 (1954).
limit the kind of establishment eligible for retail liquor licenses to those which will handle no other commodity. The advantages claimed for this restriction can best be indicated by noting what is predicted to occur in its absence.

It is alleged that permitting liquor distribution by nonspecialized retail stores will make liquor more readily available; reduce the public's inconvenience in buying it, thereby increasing its consumption; render the policing of minimum price violations far more difficult; and reduce the value of liquor franchises from what they would be under a restrictive system limited to specialized stores, thereby impairing licensee responsibility in sales to minors and alcoholics. However, the accuracy of these predictions is far from self-evident.

The first claim implies that regulation has reduced the availability of liquor and thereby deterred its consumption. But this is subject to the same criticism leveled against the more general claim that license limitation will deter off-premise consumption. Indeed the evidence presented in Part I of this Article applies with equal force here. It cannot be assumed that any given volume of liquor is more likely to be sold in a specific market when it is handled by a multitude of general retail stores than by a few specialized package stores.

At first glance the second and third claims may seem more convincing. It is often said that policing is harder when outlets are more numerous and that the incentive to comply with liquor regulations is lessened when licenses are less valuable. If so, these incentives would clearly be greater for specialized liquor stores—where a license means life or death—than for a grocer or supermarket, where liquor is only a sideline.

Yet, the danger that administrative convenience will diminish when the number of licensees mushrooms is less cause for concern if the expansion of license distribution reduces those very forces which create the regulatory problems that most require policing. Furthermore, although policing considerations weigh heavily against grocery stores and supermarkets as licensees, they appear to be less important with regard to drugstores. Druggists are already licensed and subject to regulations more rigid—and socially more important—than those applicable to the sale of liquor. Moreover, there can be no fear that permitting druggists to sell liquor would increase the dangers of criminal infiltration of the industry. Indeed, drugstores are already permitted to sell liquor by the bottle in twenty-two of thirty-three private license systems today.90

90 In contrast, only ten states limit liquor distribution to exclusive package stores, only thirteen license both drugstores and grocery stores, and only three license liquor stores, drugstores, and grocery stores. See Table I supra.
Opening up retail liquor distribution to outlets other than exclusive package stores would reduce waste in inefficiently employed manpower and excessive investments in facilities by making off-premise liquor distribution incidental to other retail activities, and might help cushion the liquor licensee against the dangers and enforcement problems which excessive competition in the liquor trade is alleged to precipitate. If so, a gradual relaxation of the exclusive package store regulation would reinforce those other safeguards against irresponsible behavior.

C. Restrictive Licensing Free of Subjective Factors in the Selection of Licensees

Another argument invoked by defenders of the status quo is that many licensees have paid large sums for their licenses on the assumption that the restrictive policy would be continued. Nevertheless, business equities should not be protected at the expense of injuring the regulatory system by creating unmanageable franchise values. Protecting investment seems particularly hard to justify insofar as license limitation is neither necessary nor sufficient to promote licensee responsibility or temperance, and account can be taken of private business equities in mapping out a transition to unlimited licensing or to arrangements to distribute licenses on an objective basis.

The SLA has not made any commitment to retain the license moratorium indefinitely. Its behavior cannot reasonably be interpreted as giving any tacit promise to do so. On the contrary, all licensees know from the outset that the SLA has the power to vary the number of licenses to further the public interest. They should also know that changes in the rules are a normal risk of any regulated business in which the regulatory agency has broad discretionary powers.

It can still be argued, however, that since the licensees’ “mistakes” have already been made, the question is really the degree of hardship they must be forced to suffer for their bad judgment. Here serious practical problems arise. When firms make erroneous predictions about the market behavior of their rivals, or potential rivals, competition may impose harsh penalties. On the other hand, the penalties suffered by firms as a result of the action of a regulatory agency may have to be softened to placate public pressure.

There are in fact several ways in which the shift to unlimited licensing can be made gradually. The moratorium could be replaced by restrictions based on population which could be liberalized each year. Similarly, with appropriate statutory authorization to the SLA, the
distances required between package stores could be successively reduced each year.

However, it must be emphasized that a mere "lifting" of any license moratorium will not eliminate the inflated franchise values which have been a major source of bribery and corruption. Inflated values will emerge whenever the number of applicants for liquor licenses exceeds their supply. With anything short of unlimited licensing, applicants will still have strong temptations to buy their way into the liquor business, by fair means or foul.

This does not mean that an orderly phasing out of the present rules is not possible or desirable, provided it goes far enough. But if licensing officials continue to exercise broad discretion on the number of licenses any market "needs," the same problems will recur. There is no easy way out between the dangers of restrictive licensing and corruption on one hand, and the destruction of private equities on the other. Either unlimited licensing can be followed to its logical conclusion or a permanent scheme can be adopted whereby a limited number of licenses can be distributed by impersonal techniques—such as first-come, first-served, auctions, or lotteries—which are less subject to manipulation by interested parties. None of the options is without its hazards, but each is better than the present situation.

1. First-Come, First-Served

The SLA has normally distributed its limited retail licenses and removal rights on a first-come, first-served basis. It has generally followed the policy of not issuing any further licenses for a specific area once an "adequate" number has been issued for that area. However, first-come, first-served is not always acceptable. In 1945, the SLA was deluged with a flood of competing applications when it temporarily lifted the package store moratorium. At that time the SLA was confronted with numerous cases in which qualified applicants, many of them veterans, sought rights to operate in the same vicinity. Because of the restrictive licensing theory, the SLA was often forced to choose one from among many qualified applicants. These decisions were frequently made on the basis of criteria which had not even a remote connection with the objectives of control. Another situation in which first-come, first-served is unacceptable is when two or more existing licensees seek to move to more profitable markets already served by numerous licensees. This situation has been aggravated by the SLA's current practice of accepting removal applications during a single month only, in order to evaluate more ade-

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91 See 1946 SLA ANN. REP. 10-11.
LIQUOR LICENSING

quately the requests in an orderly and fair manner.\textsuperscript{92} Here again, the important question is whether the criteria used in making the choices are more conducive to alcohol consumption control than a strict distribution by "priority of application." These matters would be especially relevant if any sudden lifting of the moratorium should result in a flood of simultaneous applications to operate in the same market.\textsuperscript{93}

At first glance, the next logical step would seem to be the institution of formal comparative proceedings, at least when a set of clear-cut priorities cannot facilitate an automatic choice.\textsuperscript{94} Such procedures have long been employed by federal regulatory commissions. Applicants there are evaluated with reference to each other, each having a chance to contest the commission's evaluation. The formal basis for federal regulatory decisions in comparative cases is sometimes spelled out in great detail and is publicly available for all to see.\textsuperscript{95} These procedures have been defended as a fairer rationing device than first-come, first-served.\textsuperscript{96} However, their hazards are also well-known. They are very expensive and time-consuming in fields where delays create their own inequities. Above all, comparative hearings make processing lines longer and hearing dockets more crowded. Hence

\textsuperscript{92} See 1955 SLA ANN. REP. 11-12.

\textsuperscript{93} "Mutual exclusivity" of license applications may be judged by technical-physical or economic criteria. In the broadcast field requests for the same operating rights are often deemed mutually exclusive on technical-physical grounds where approval of both grants would cause unacceptable electrical interference. In air transport, on the other hand, mutual exclusivity of competing route applications depends on the Civil Aeronautics Board's economic findings regarding revenue potential of particular markets and the likelihood that granting both requests would debase the quality and reliability of service. Mutual exclusivity of the second type seems inherent in any tightly restricted licensing situation and is more pertinent to the package store field. These distinctions are considered at length in Note, \textit{The Ashbacker Doctrine and Proceedings Before the Civil Aeronautics Board}, 46 Geo. L.J. 282-83, 294-98 (1957-1958); Note, \textit{The Ashbacker Rule and the CAB: Cumbersome Procedure v. Public Interest}, 44 VA. L. REV. 1147-54, 1164-65 (1958).

\textsuperscript{94} For an opinion that comparative hearings of mutually exclusive retail liquor applications may sometimes be proper and raise problems that merit careful consideration, see Byse, \textit{Opportunity To Be Heard in License Issuance}, 101 U. PA. L. REV. 57, 92-95 (1952).

\textsuperscript{95} This is not to imply that there is no question about the relevance and validity of these complex and voluminous decisions. For an exhaustive critique of comparative proceedings in the broadcast field see Jones, Licensing of Major Broadcasting Facilities by the Federal Communications Commission 48-66, 198-208 (mimeo. ed. 1962). See also Jones, Licensing of Domestic Air Transportation by the Civil Aeronautics Board, A Study for Administrative Conference of the United States 135-48 (mimeo. ed. 1962).

\textsuperscript{96} This is the principle of Ashbacker Radio Corp. v. FCC, 326 U.S. 327 (1945). The potential role of comparative proceedings in retail liquor licensing under conditions of limited license issuance is considered by Byse, supra note 94. However, comparative proceedings may not be suitable in cases of economic exclusiveness in the air transportation field. See Note, \textit{The Ashbacker Doctrine and Proceedings Before the Civil Aeronautics Board}, 46 Geo. L.J. 282 (1957-58); Note, \textit{The Ashbacker Rule and the CAB: Cumbersome Procedure v. Public Interest}, 44 VA. L. REV. 1147 (1958).
they produce even greater temptations for resourceful applicants to manipulate the procedures.  

The dilemma is clear. Restrictive licensing, *ad hoc* changes in license moratoria, or even periodically-revised numerical ceilings on a county basis, are all bound to confront the SLA with recurrent floods of competing applications. They will do so under the very conditions most likely to render the principle of first-come, first-served suspect in the eyes of many. Yet, the most obvious "remedy"—the formal comparative hearing—is at best poorly suited to the problem at hand, and at worst subject to serious abuse in its own right.

2. Auctions

The state could auction off to the highest "qualified" bidder whatever rights are now rationed by the SLA. By selling what has hitherto been given away, the temptations to manipulate regulatory decisions through extra-legal means would be sharply reduced. Yet there is no need to scrap all the regulatory experience of thirty years. Whatever can be salvaged from administrative expertise could be codified into a simplified set of standards that determine who is, and who is not, "qualified" to bid for franchise rights. With proper safeguards the auction approach might avoid some of the more spectacular deficiencies of formal licensing procedures in cases of competing applicants.

Among the misconceptions of persons who oppose license distribution by auction is the belief that only wealthy applicants will be able to bid. Even without special safeguards this need not be so.  

However, it is obviously possible to limit certain contests to small businesses only. Continuation of the one-to-a-customer rule in off-premise licensing could in turn check ownership concentration.

As a first approximation, the procedure could be set up roughly as follows:

All applications for new licenses and removal rights in the package store and on-premise fields would be auctioned to the highest qualified bidder, after thorough preliminary screening for general fitness. The auctioning of transfer and renewal rights raises special, difficult problems and need not be considered at this stage.

98 Ronald H. Coase has argued that the licenses will go to those who, relatively, can make the best economic use of them. Coase, *The Federal Communications Commission*, 2 J. Law & Econ. 1, 19 (1959).
Under a continued moratorium on new package store licenses—or a new one in the on-premise field—the scheme might best be used to distribute removal rights only. Renewal rights might also be auctioned off at periodic intervals.

With or without a continuous moratorium on new licenses, different kinds of applications would be accepted at specified predetermined times of the year only, rather than on a first-come, first-served basis.

All applicants would be subject to identical minimum standards except when the legislature designates, or permits the SLA to designate, preferred classes of candidates such as veterans or local residents. These classes might be permitted to bid for certain grants on an exclusive basis much as certain lots of federal timber, and certain groups of defense procurement contracts, are now "set aside" or reserved for bids by small business.\textsuperscript{100}

The SLA could institute one of two suboptions in administering the scheme. It could use an ad hoc approach in handling requests for removal rights and new licenses—once the package store moratorium was lifted. Having invited bids at a preannounced time for any and all sites in any community, it could then advertise the sites actually being sought and invite additional interested bidders to come forth, granting the removal rights or licenses to the winners.\textsuperscript{101} Or it could create an "allocation table," with predetermined numerical limits on the number of package stores—or even of tavern licensees—and invite bids for these limited slots. This approach would reduce the pressure on the SLA

\textsuperscript{100} On the possibility that clear-cut priorities in licensing will minimize the chance for administrative abuse both in initial screening and in choosing between qualified candidates see Jones, Licensing of Major Broadcasting Facilities by the Federal Communications Commission 204-08 (mimeo. ed. 1962). In the final selection from among comparable applications, auctions are not an innovation. \textit{Id.} at 205-06. See also Schwartz, \textit{Comparative Television and the Chancellor's Foot}, 47 Geo. L.J. 655 (1959); H.R. Rep. No. 1258, 86th Cong., 2d Sess. 58-59 (1960); \textit{Hearings on the Administrative Process and Ethical Questions Before a Subcommittee of the House Committee on Interstate and Foreign Commerce}, 85th Cong., 1st Sess. 160-61, 172 (1958); \textit{Hearings on the Major Administrative Process Problems Before a Subcommittee of the House Committee on Interstate and Foreign Commerce}, 86th Cong., 1st Sess. 706, 710-13 (1959).

\textsuperscript{101} Exclusive concession rights to operate restaurants on the New York Thruway were distributed in roughly this way. When it opened the Erie segment, the Thruway Authority invited sealed bids by a preannounced deadline from applicants who met specified standards. Exclusive leases went to the highest qualified bidder. Bids were made as a percentage of gross restaurant receipts, whenever these would exceed an annual minimum of $100,000. See N.Y. State Thruway, General Information in Connection with Leasing of Restaurants on the Erie Section 8 (mimeo.). Variants of this procedure also appear in the distribution of contracts by the Atomic Energy Commission. The Commission may either: (a) advertise a particular contract widely and accept bids from any qualified applicant; (b) invite bids from a pre-selected list of contractors only; (c) pre-determine a single "preferred" applicant and negotiate directly with him. \textit{ATOMIC ENERGY COMM'N, CONTRACT POLICY AND OPERATION} 41-50 (1951). The arrangement is also used extensively by the Bureau of Land Management in distributing rights to drill for oil on public lands. See 43 C.F.R. §§ 192.40-42 (1963).
to approve all requests for new licenses or removals when, consistent with distance requirements, applicants seek different sites in the same neighborhood.  

The probable economic-regulatory effects of an auction system would appear to be that:

The SLA could recapture premiums that applicants have sometimes paid to existing licensees, real estate brokers, landlords, specialized lawyers, regulatory officials, staff members, or enforcement personnel in seeking entry into the most profitable markets sometimes with an eye on subsequent resale.

In recovering these premiums the SLA would come much closer to recapturing the full value to the licensee of the right to remove or operate, and not just sums that cover the cost of administering the regulatory system. In the light of this additional income, the state liquor tax structure might be reexamined with auction receipts replacing taxes.

Public auctions would reduce the opportunity and temptation for improper influence, bribery, and corruption since with fewer valuable rights being given away, there would be fewer temptations on the part of applicants, enforcement agents, and other intermediaries, to rig the decision-making process.

Initiation of an auction scheme might also precipitate a move to clarify existing standards and responsibilities of licensees. Applicants might desire a clearer idea of what is expected of them before they bid. The SLA and the legislature might be induced to reexamine the importance of certain goals which auctions might jeopardize such as the widespread diffusion of licenses.

The letting of exclusive leases to operate gasoline service stations on the New York Thruway was handled in this way. Separate bids were invited for each of a predetermined number of service stations, located at preassigned points. Bids took a form roughly comparable to those submitted for the restaurant leases. See New York State Thruway, General Information Regarding Bidding for Leasing of Gasoline Service Stations at the Ardsley and Seneca Areas (mimeo.). Some such arrangement would seem relevant to those twenty-one states which now impose numerical ceilings on a county basis on the number of retail liquor licenses. Competing applications will probably be received periodically whenever ceilings were revised in line with new population censuses. Although twelve license states now use a numerical ceiling, the New York Liquor Authority has consistently opposed it. See 1939 SLA Ann. Rep. 9; 1951 SLA Ann. Rep. 10-12; 1954 SLA Ann. Rep. 12-13.

What follows is based on the analysis of license distribution by auction in Levin, Federal Control of Entry in the Broadcast Industry, 5 J. Law & Econ. (1962). See also the more general mathematical analysis of auctions and franchise value in Vickrey, Counterspeculation, Auctions, and Competitive Sealed Tenders, 1961 J. Finance 8.

If competitive bidding aggravated the clustering of licensees in a few markets in each county, the local neighborhood concept might be reexamined and subsequently scrapped or protected by special safeguards. The one-to-a-customer rule presently precludes ownership concentration or chain ownership of package stores. An auction approach might force its reexamination.
By increasing the capital costs of licensees, auctions might induce them to increase their sales through those very tactics which restrictive licensing was instituted to prevent.\textsuperscript{105} Even if this is true, it would simply act to spur the legislature, the SLA, and the public to support a speedier codification of the standards which licensees are expected to meet.

3. Lotteries

Licensees who have paid substantial sums for their privileges may be less willing to comply with regulations, and more likely to defend their "property rights" with expensive litigation. Hence a lottery might have advantages that an auction system lacks. It could, in any case, be instituted under the same framework as the auction, with the same suboptions discussed above.

California employs such an arrangement. Whenever the population in any county increases by more than 2,000 inhabitants, the licensing authority may issue "one on-sale general license and one off-sale general license."\textsuperscript{106} Applications are widely solicited. Should there be more applicants than there are licenses available for issuance the authority conducts "a drawing to determine the priority in which all of such applications filed with it shall be considered."\textsuperscript{107} No more than one drawing per county can be made annually. Though the number drawn by any applicant indicates the priority his application will receive, it does not insure issuance of a license.

Such a system would have all the advantages of auctions in reducing the authority's need to make decisions with vague standards. It could thereby help eliminate a major source of improper influence. Superficially it might even seem less likely to "favor the wealthy," or to bid up capital costs in a way that induces licensees to increase sales volume by illicit strategies. The disadvantage of lotteries is that they do not recapture franchise value for the community.

V. Conclusion

When all qualified candidates can get a license for the asking, franchise value is negligible. Once adequate basic standards are set, the problem of license distribution has a mechanical solution. Only

\textsuperscript{105} However, the capital values of licensed premises are already bid up under the current moratorium. The social dangers which the opponents of auctions fear already exist. A priori there is no reason to expect auctions to do more than replace the current upward pressure on capital values inherent in current licensing arrangements. See Levin, \textit{Federal Control of Entry in the Broadcast Industry}, 5 J. Law & Econ. (1962); Levin, \textit{Regulatory Efficiency, Reform and the FCC}, 50 Geo. L.J. 1, 30-32 (1961).

\textsuperscript{106} \texttt{CAL. BUS. & PROF. CODE} § 23821.

\textsuperscript{107} \texttt{CAL. BUS. & PROF. CODE} § 23961.
when the number of licenses is deliberately restricted below the level of qualified candidates do serious problems appear: inflation of franchise values, intensification of attempts to manipulate the distribution of public privileges, and danger of subverting the regulatory process. With a restricted number of licenses available, impersonal techniques to distribute them become absolutely essential for efficient regulation.

The remedial alternatives discussed in this Article do not exhaust the logical possibilities. Excluded are two more extreme options: outright deregulation of all licensed retailers and a state monopoly of retail liquor distribution. The former option has never been seriously considered by an American state, although it is an arguably acceptable alternative. As already suggested, a far-reaching degree of deregulation might be consistent with the goals of alcohol consumption control provided that certain basic rules were simultaneously instituted. Among these rules would have to be stringent control of hours of sale, prohibition of free delivery, retail distribution by other than specialized package stores, and the replacement of price maintenance by an excise tax. Some experts would even place full reliance upon proper temperance education and permit the consumer to determine his own conduct. The influence of family, church, and community would shape consumer behavior, with the supply of liquor and the number of off- or on-premise outlets completely free to respond accordingly.

On the other hand, state monopoly systems are familiar arrangements for retail liquor distribution in the United States. Omitting the monopoly as a remedy for New York is not a reflection on its efficacy elsewhere. On the contrary, monopoly systems have long had strong appeal to investigators in this field. If all remedial options consistent with a private system were rejected, a full-fledged state monopoly would remain as one further solution.

This option need not necessarily take the form of state-owned and state-operated stores. Under a system of state "agencies," concession rights could be auctioned to the highest bidder on a county basis much as the New York Thruway has auctioned off its restaurant and gasoline station leases. Advantages of this system to the state include recovering the franchise value and not having to make large capital outlays required to institute a system of state stores.

There is one other aspect of New York's present system which may be of interest to liquor regulators elsewhere. Although her restrictive policies now confer economic benefits on off-premise retail

licensees far more than they control consumption, a sufficiently drastic reduction of package stores might curb consumption substantially. However, such an extreme limitation of licenses would seriously inflate franchise values, thus multiplying the regulatory-enforcement problems already present. Therefore, if license limitation is used to reduce consumption, some form of state monopoly may be necessary to prevent the disruptive side-effects already mentioned.\(^{109}\)

**STATISTICAL APPENDICES**

Multiple regression analysis permits us to estimate the relative importance of variations in two or more independent variables \((X_1 \ldots X_n)\) which seem to explain variations in one or more dependent variables \((Y_1 \ldots Y_m)\). My main statistical task in this paper is to measure the degree to which variations in alcohol consumption per adult (or in gross liquor store revenues per licensee) are explained by variations in family income, package stores per adult, flows of traffic and transients, and population per square mile. The relative power of each independent variable to explain the dependent variable is estimated holding constant all other independent variables.

The variables I have analyzed in six separate tests are listed in Appendix A:

**APPENDIX A**

**VARIABLES ANALYZED IN SIX MULTIPLE REGRESSIONS**

1. New York County Study: Liquor Store Sales Per Adult \((N = 62)\)
   - \(Y_1\) = liquor store sales per adult
   - \(X_1\) = median family income
   - \(X_2\) = adult population per off-premise license
   - \(X_3\) = sales of eating and drinking places per adult
   - \(X_4\) = adult population per square mile

\(^{109}\) At the least, charts in Entine, *op. cit. supra* note 30 reveal that the monopoly states as a group now have far fewer off-premise licenses per capita than New York, considerably higher liquor store sales per outlet, and somewhat lower per capita off-premise consumption. A separate review of tax revenues suggests also that monopoly states may well derive substantially more tax revenues per capita from alcoholic beverages than New York does and a larger fraction of their total state revenues. This is probably true even after adjustments to make the data fully comparable.

\(^{110}\) Sources:

- Median Family Income: U.S. Bureau of the Census, *Dep’t of Commerce, 1962 County and City Data Book* Table 1 (item 22).
- Adult Population and Population per Square Mile: *Id.* (items 4, 11).
- Off-Premise Sales: *Id.* at 1-59 (Table 7); New York State Liquor Authority, unpublished records.

Data for Test I, and results of test, appear in Brief, *op. cit. supra* note 30; basic data for Tests II-VI prepared by the author. All statistical calculations for Tests II-VI undertaken with cooperation of Lowry L. McKee and the Hofstra University Computer Center.
II. New York County Study: Liquor Store Sales Per Licensee (N = 62)

\[ Y_s = \text{liquor store sales per off-premise licensee} \]
\[ X_1 = \text{median family income} \]
\[ X_2 = \text{adult population per off-premise license} \]
\[ X_3 = \text{sales of eating and drinking places per adult} \]
\[ X_4 = \text{adult population per square mile} \]

III. All State Study: Liquor Consumption Per Adult (N = 49)

IV. License State Study: Liquor Consumption Per Adult (N = 32)

\[ Y_t = \text{apparent liquor consumption per adult} \]
\[ X_1 = \text{median family income} \]
\[ X_2 = \text{adult population per off-premise license} \]
\[ X_3 = \text{sales of eating and drinking places per adult} \]
\[ X_4 = \text{adult population per square mile} \]

V. All State Study: Liquor Store Sales Per Licensee (N = 49)

VI. License State Study: Liquor Store Sales Per Licensee (N = 32)

\[ Y_s = \text{liquor store sales per off-premise licensee} \]
\[ X_1 = \text{median family income} \]
\[ X_2 = \text{adult population per off-premise license} \]
\[ X_3 = \text{sales of eating and drinking places per adult} \]
\[ X_4 = \text{adult population per square mile} \]

In each case the estimating equation was:

\[ \log Y = a + b_1 \log X_1 + b_2 \log X_2 + b_3 \log X_3 + b_4 \log X_4 \]

The main results for each test are tabulated below in Appendix B. Each regression coefficient (col. 1) reveals the change in \( Y_t \) (or \( Y_s \)) associated with a unit change in one of the independent variables—holding all the others constant. E.g., in Test I the regression coefficient for \( X_1 \) is .63029. This means that for any change in median family income of 1%, other things being equal, liquor store sales per adult change +.63% in a sample consisting of data for 62 counties in New York, 1958.

Multiple regression deals with samples. Hence it is possible that the computed coefficient in any test may differ from the true coefficient of the parent population from which the samples are drawn. That is, the form of the relationship between the dependent and independent variables discovered in the sample may or may not indicate the actual relationship that exists in the parent population. The crucial question is whether the difference between the calculated coefficient and the true coefficient is due to pure chance. If not, the relationship found in the sample cannot be accepted as indicative of the true relationship between the variables in question.
## Appendix B

### Major Results of Multiple Regression Tests

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<th>Variables</th>
<th>Regression Coefficient</th>
<th>Standard Error</th>
<th>T-Ratio of T at .01 Confidence Level</th>
<th>Multiple Coeff. of Corr. at .01 Conf. Level</th>
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The remaining material in Appendix B (cols. 2-6) provides information necessary to ascertain the statistical significance of the relationships between the variables studied. For readers familiar with statistical methods, or having access to statistical expertise, the results in Table B will be self-explanatory. For others, no simple explanation is possible in the short space available and they are referred to such standard textbook treatments as Ezekiel & Fox, *Methods of Correlation and Regression Analysis* (1961), especially chs. 2, 10, 17. Suffice it to note also that the significance of the coefficients in col. 1 can be ascertained quickly in Appendix B by comparing columns 3 and 4. Whenever the figures in col. 3 (the t-ratios) exceed those in col. 4 it can be assumed, for purposes of this Article, that the relationships quantified in col. 1 (the regression coefficients) are in fact significant.

At the least, it is hoped that all readers will study the results recorded in col. 1 to compare the relative strength of the different factors which influence liquor consumption per adult and liquor revenues per licensee.