

SUBJECT: Continuing the Texas Alcoholic Beverage Commission

COMMITTEE: Licensing and Administrative Procedures —favorable, without amendment

VOTE: 7 ayes — Geren, Jones, Goolsby, Hamilton, Miles, Quintanilla, Thompson
0 nays
2 absent — Flores, Isett

SENATE VOTE: On final passage, March 28 — 30-0, on Local and Uncontested Calendar

WITNESSES: (*On House companion bill, HB 2425 by Truitt:*)
For — (*Registered, but did not testify:* Rick Donley, The Beer Alliance of Texas; Fred Marosko, Texas Package Store Association; Mike McKinney, Wholesale Beer Distributors of Texas; Ralph Townes, License Beverage Distributors; Alan Gray, Licensed Beverage Distributors
Against — None
On — (*Registered, but did not testify:* Karen Latta, Sunset Advisory Commission)

BACKGROUND: The Texas Alcoholic Beverage Commission (TABC) enforces the Alcoholic Beverage Code and licenses and regulates the three tiers of the alcoholic beverage industry — manufacturers, distributors, and retailers. The specific duties of the commission include regulating sales, taxation, importation, exportation, manufacturing, transporting, possession, and advertising of alcoholic beverages.

The 44th Legislature enacted the Alcoholic Beverage Code and created the Texas Liquor Control Board in 1935, two years after the repeal of Prohibition. The original purpose of regulating the alcoholic beverage industry — including the three tiered system of alcoholic beverage regulation — was to prevent close financial and familial ties between the manufacturers and sellers of alcohol. In 1970, the Legislature changed the

name of the agency to TABC, but its functions have stayed essentially the same during the past seven decades.

The policy-making body of the agency is a three-member governing board appointed by the governor with the advice and consent of the Senate. Members of the commission hold office for staggered terms of six years, with the term of one member expiring every two years. An administrator, appointed by the governing board, directs the commission's daily operations.

In fiscal 2006, TABC had 686 employees, compared with 215 in 2003. The licensing division of TABC issues 66 different licenses and permits to manufacturers, wholesalers, and retailers. Each year, the agency processes applications or renewals for almost 119,000 licenses, and the commission also can refuse, suspend, or cancel permits and licenses. The enforcement division, which includes more than 300 commissioned law enforcement officers, conducts investigations, while the legal division assists in the prosecution of violators. The compliance division ensures the proper amount of taxes and fees have been assessed, reported, and paid by licensees and permit holders. TABC also adopts standards of quality and approves labels and the sizes of containers for all alcoholic beverages sold in Texas.

The agency spent more than \$38.2 million for its operations in fiscal 2006 — all of which came from licensing fees and surcharges. TABC collected more than \$227.4 million in revenue from regulation of the alcoholic beverage industry. The Legislature would appropriate about \$77.6 million for TABC in fiscal 2008–09.

In 1993, the 73rd Legislature enacted HB 1425 by Hilbert, which authorized the issuance of a brewpub license to permit establishments to brew and sell limited amounts of malt liquor, ale, and beer for either on- or off-premise consumption. Alcohol Beverage Code, sec. 74.01 limits this exception to the three-tiered system by prohibiting a brewpub license holder from having or having an interest in a manufacturers' or distributors' license or permit.

In 2005, the House passed HB 2544 by Hamric, et al. that would have continued TABC until September 1, 2011, but the bill died in the Senate. The 79th Legislature enacted HB 1116 by Solomons et al., which

continued the operations of several agencies under Sunset review, including extending the Sunset date of TABC until September 1, 2007.

DIGEST:

SB 904 would continue the Texas Alcoholic Beverage Commission until September 1, 2019. The bill would require the agency to:

- develop a risk-based approach to enforce its regulations and assess sanctions;
- expedite processing of complaints against licensees;
- establish an internal affairs office;
- work with industry representatives to develop policies for making market practice regulations;
- end the duplication of alcoholic beverage testing performed by federal agencies;
- require health warning signs about the risks of drinking while pregnant; and
- impose criminal penalties for failure to allow inspections or serving alcoholic beverages during prohibited hours.

Risk-based enforcement. SB 904 would establish a mission statement requiring TABC to:

- protect public safety;
- promote legal and responsible alcohol consumption;
- ensure fair competition in the alcoholic beverage industry;
- provide for consistent, predictable and timely enforcement of the Alcoholic Beverage Code and the granting of permits and licenses;
- foster voluntary compliance with alcohol laws; and
- communicate the requirements of the laws clearly and consistently.

The bill would require the commission to develop a risk-based enforcement system that would focus on detecting serious violations and monitoring establishments with a history of complaints and violations. The commission also would be required to establish benchmarks and goals for enforcement programs and track the type and disposition of violations on a statewide and regional basis. SB 904 would require compiling statistics on a monthly basis for the TABC executive management and board members and providing a summary available to the public on the agency's web site.

SB 904 would require TABC to adopt a schedule of sanctions for violation of state laws or agency rules. The sanctions schedule also would be required to include a list of most common violations and guidelines on when it would be appropriate to deviate from the sanction schedule. The sanction schedule would be made available to the public, including posting on the agency's web site.

Expediting complaint resolution. The bill would require TABC to define its complaint process and develop a standardized form for making complaints. The policy and forms would be made available on TABC's web site. The commission would be required to apply a risk-based schedule to give priority to resolving the most serious complaints first. The bill also would require collection of statistics about complaints and their resolution and to make that information available to the public on the agency's web site.

Internal affairs office. SB 904 would authorize the TABC administrator to establish an internal affairs office and appoint its director. The internal affairs office would have original jurisdiction over complaints against TABC personnel. The agency would have to inform the public about the process for filing a complaint.

The internal affairs office would be authorized to initiate investigations of complaints, but would be required to obtain permission from a division director or upper level agency management to investigate an employee when no complaint had been made.

The internal affairs office would be required to file a monthly report to the TABC administrator and a quarterly report to the board on the nature and status of investigations and recommendations to avoid future complaints.

Policy development. TABC would be required to develop a formal process to make market practice policies and gather input from a diverse group of industry representatives, including representatives from the manufacturing, distribution, and retail tiers.

End duplication of testing. SB 904 would allow the holder of the proper permit to ship or sell distilled spirits or wine if the permit holder had received a registration of label approval from the United States Alcohol and Tobacco Tax and Trade Bureau for that product. TABC would continue to require independent testing of beer, ale, and malt liquor and

would be able to test any alcoholic beverage already on the shelf or on a complaint basis.

Warning signs. The bill would require establishments permitted to sell alcoholic beverages on-premises to post a warning sign on the door to each restroom warning of the risks of drinking alcohol during pregnancy. The TABC would establish a rule to specify the language of the sign, including the font size and type used for the warning.

Criminal penalties. SB 904 would make the sale or consumption of alcoholic beverages during prohibited hours a class A misdemeanor (up to one year in jail and/or a maximum fine of \$4,000). Premises licensed or permitted under the Alcoholic Beverage Code would be defined as a public place for the purpose of enforcing these restrictions. Refusal to allow a TABC officer or other peace officer to enter and inspect a licensed or permitted establishment also would be a class A misdemeanor.

Other provisions. The bill would apply, update, or modify standard Sunset provisions governing conflicts of interest, unbiased appointments to the agency's policymaking body, gubernatorial designation of a presiding officer, grounds for removing a board member, training of board members, complaint procedures, separation of policymaking and staff functions, public access through technology, and alternative rulemaking and dispute resolution procedures.

The bill would require TABC to report to the Legislature every October 31 of even-numbered years on enforcement efforts against sale or consumption of alcoholic beverages prohibited hours.

The bill would take effect September 1, 2007.

**SUPPORTERS
SAY:**

SB 904 would help modernize statutes regulating TABC to ensure that the agency placed a high priority on protecting public safety and being responsive to both the alcoholic beverage industry and to citizens. Too many regulations and practices date to pre-Prohibition days when competition among saloons associated with brewers, or "tied houses," led proprietors to encourage over-consumption by serving free and salty meals or promoting "side vices" such as gambling, cockfighting and prostitution. These problems that led to passage of Prohibition are long past, and TABC needs to address the problems of the 21st Century.

Sunset review should be limited to oversight of the operations and efficiency of TABC, and other policy questions regarding alcoholic beverages should be decided independent of the Sunset process. Dozens of bills have been filed to address specific concerns about regulation of alcoholic beverages. SB 904 should remain a review of the agency and not be turned into a “Christmas tree” for amendments that continue intramural battles among segments of the alcoholic beverage industry. Further study of the industry, if needed, can occur during the interim or during future legislative sessions.

Risk-based enforcement. SB 904 would institute a risk-based approach to focus TABC’s enforcement activities and sanctions against those establishments that pose the most danger to the public. Current budgetary performance measures reward quantity over quality by requiring TABC to inspect 80 percent of the more than 42,000 licensed establishments. Rather than scrambling to visit as many establishment as possible, TABC agents should focus their efforts on inspecting establishments that have a history of problems or detecting violations that affect public safety. The risk-based approach would require the agency to prioritize the use of its limited resources to protect public safety.

Internal affairs and complaint process. TABC created an internal affairs division to combat widespread allegations of corruption in the agency in the 1980s. Since the 2005 Sunset review, the agency has raised the profile of the office, now called the Office of Professional Responsibility. SB 904 would make the statutory changes needed to implement changes needed to maintain high professional standards. It also would spell out ways to make the complaint system more accessible to the public and would ensure that complaints against license holders were investigated and resolved in a timely manner.

Policy development. The agency makes marketing practices decision that affect all segments of the industry, and most of those decisions deal with competition and separation of the three tiers of the industry. Typically, these regulatory decisions do not affect citizens or public safety directly. The bill would provide for a formal mechanism for industry representatives to address these issues, but it would not preclude the agency or industry from soliciting input from groups such as Mothers Against Drunk Drivers (MADD) or members of the public.

End duplication of testing. Distilled spirits manufacturers and wineries already have to submit their products for testing through the federal Tax and Trade Bureau. The federal program is sufficient to ensure that these products are safe for human consumption and accurately reflect the alcohol content. SB 904 still would grant TABC the authority to test products as necessary or allow for random tests of products already on the shelf. The agency also would be able to test in response to consumer complaints. SB 904 would allow TABC to retain the ability to approve beer labels because the state has additional labeling requirements — such as labels for beers with an alcohol content of less than 4 percent — not found in federal law. TABC agents still would be able to determine from reading a label if a particular beer was legal for sale in that jurisdiction.

Warning signs. Health warning signs about the risks of drinking alcohol while pregnant are needed in establishments that sell alcoholic beverages. According to survey data from the Texas Department of State Health Services, up to 50 percent of women do not connect the use of alcohol with birth defects. Currently, 19 other states and the District of Columbia require those who sell alcohol to post health warning signs about the risk of drinking alcohol during pregnancy. TABC developed a pilot program four years ago to send warning signs to those who apply for a license or renew an existing license. Posting of the signs is discretionary, and TABC does not check for the signs during inspections. These warning signs should be made mandatory.

Criminal penalties. One continuing source of risk to the public remains licensed establishments that continue to serve alcohol after legal closing time. Currently, violators have the option of closing their business for a required number of days or paying a fine. Usually, the license or permit holders pays the fine because it is less than the loss of revenue from being closed. SB 904 would let TABC, not the violator, make the decision and would allow for criminal penalties as well.

Those who sell alcoholic beverages illegally pose a particular danger to the public, and criminal penalties, including the possibility of jail time, is an appropriate response. These penalties meet the Sunset Advisory Commission's standard that "Criminal penalties should exist only for agencies overseeing practices that can have dire consequences on the public health and welfare."

Violations must be very persistent or pose a danger to public safety before TABC can seek criminal penalties. SB 904 would include a reporting requirement to the Legislature, and cases of selective enforcement or systematic harassment would be reflected in those data.

Other issues. Despite the criticism of the three-tier system, prices for beer, wine and distilled spirits in Texas are comparable to the prices of these products in other states. Allowing large retailers such as Wal-Mart to hold both wholesale and retail licenses could result in predatory pricing practices and would not result in savings for bars and restaurants or for consumers.

Prices for alcoholic beverages deliberately are kept high for policy reasons — to collect tax revenue and discourage consumption. If lower prices for alcoholic beverages are a priority for policy makers, they should reduce excise, gross receipts, and sales taxes on these products.

No one has shown any connection between the size of an agency's governing board and the efficiency and effectiveness of the agency itself. Plenty of examples can be found of boards with wide geographical and ethnic representatives that have been unable to manage the state agency. Finding three members for boards that oversee complex regulations, such as the Public Utilities Commission or TABC, can be difficult, and it might not be possible to find five qualified and willing candidates on a consistent basis.

OPPONENTS
SAY:

Texas's system of alcoholic beverage regulation still is based on Prohibition-era concerns and remains in need of revision. The Legislature should establish a joint interim committee to study revisions to the state's alcoholic beverage structure, including the three-tier system.

Risk-based enforcement. Legislative changes to shift to a risk-based enforcement system would not ensure that TABC would not be fixated on generating large numbers of inspections on a smaller number of establishments. The policy also could lead to selective enforcement and potential harassment against certain licensees.

Policy development. Groups concerned with alcohol safety issues such as MADD and the general public should be represented on TABC marketing policy boards. There is not always a clear distinction in marketing policies between business practices and larger public policy concerns.

Warning signs. While posting signs warning about the dangers of drinking while pregnant could have some benefit, the recommendation only illustrates the continuing moral ambiguity society has about alcoholic beverages. The Sunset Advisory Commission report correctly criticizes the vestiges of old societal attitudes that exist in modern alcoholic beverage regulations, but it recommends adding another requirement intended to improve behavior. Establishments already must display numerous warning signs, and another one would be lost in the clutter.

Criminal penalties. SB 904 would contribute to the growing trend of over-criminalizing business practices and making violations of administrative rules subject to jail time.

Other issues. Maintaining the tier system stifles competition and leads to higher prices for consumers. Large retailers such as Wal-Mart should be given a fair chance to compete in the wholesale alcoholic beverage market.

OTHER
OPPONENTS
SAY:

Membership of the TABC board should be expanded from three to five members to better represent the ethnic and geographic diversity of the state. The small size of the board also creates potential open meetings conflicts when two members can constitute a quorum.

NOTES:

SB 904 was placed on the House Major State Calendar on April 23, but was recommitted to the House Licensing and Administrative Procedures Committee.

Rep. Miles has pre-filed two amendments that would increase the TABC board to five members and would allow the holder of a TABC manufacturers' license to loan money to help create a minority-owned general distributor.

HB 2425 by Truitt, the House companion bill, was reported favorably by the Licensing and Administrative Procedures Committee on March 20.