Sunset Advisory Commission

Texas Alcoholic Beverage Commission

Staff Report
October 2004

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Summary

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The Legislature created the Texas Alcoholic Beverage Commission (TABC) in 1935, following the repeal of Prohibition, to very tightly regulate the alcoholic beverage industry. Fear of large scale corruption and uncontrolled consumption led to a system in which TABC heavily regulates all aspects of the industry – everything from the production, importation, and exportation of the beverages to the storage, distribution, and eventual sale to consumers.

Concerns today focus more on fair and balanced competition, responsible drinking, and reduced government regulation; yet both TABC and the Alcoholic Beverage Code continue to reflect much of the strong controls in place since the post-Prohibition era. While the State still has an interest in regulating the alcoholic beverage industry, TABC and the Code are in clear need of modernization.

While the State still has an interest in regulating the alcoholic beverage industry, TABC and the Code are in clear need of modernization.

In reviewing TABC, Sunset staff focused on evaluating the effectiveness of the agency in managing its broad regulatory role, particularly in light of the significant changes in the industry, technology, and attitudes toward alcohol. The review identified several key areas of concern, as summarized below.

- TABC's statutory mission is outdated; and the agency lacks a comprehensive process for planning its activities statewide and measuring its progress toward achieving its goals.
- Enforcement efforts are not prioritized to focus on problems posing the greatest risk to public safety; and the agency fails to provide consistent and predictable penalties for violations.
- Certain business practices tied to the production and distribution of alcoholic beverages are over-regulated, with no clear public purpose; and the agency provides poor guidance to the industry in interpreting complex statutory requirements.

The recommendations in this report are intended to address these concerns and others by shifting the agency's focus away from a number of unnecessary and costly regulatory processes, and placing it more squarely on issues of public safety.

In conducting this review, Sunset staff also identified concerns related to efforts to maintain a strict separation of the three tiers of the alcoholic beverage industry – manufacturers, wholesalers, and retailers. While all 50 states continue to use the three-tier system, many groups are beginning to question the justification for this level of regulation in today's modern commercial environment, and believe that it deserves serious reassessment. Staff shared this concern, as much of the current system seems to protect the interests of industry segments rather than public safety. Ultimately, staff deemed the issue to be outside its review scope. Appendix A highlights some of the potentially burdensome practices tied to the three-tier system in Texas, and recent legal challenges to the system in other states.

Another factor that directly affects streamlining and modernizing the State's system of alcoholic beverage regulation is the fact that individual communities in Texas, down to the precinct level, determine if alcohol can be sold locally. The ever changing patchwork of "wet" and "dry" areas across the state complicates TABC's oversight, as different areas of the state operate under very different restrictions on what can be sold and how it can be sold. However, Sunset staff chose not to make recommendations that would in any way compromise local control.

Finally, Sunset staff received many comments about the agency's complex licensing process, but did not recommend any changes to the process in this report. While these problems are serious, TABC received $2.3 million last Session to fully automate its licensing process, and plans for the new system to be online at the beginning of 2005. This automation should allow the agency to effectively implement the changes needed to streamline its licensing process without any changes in law. By not making recommendations regarding the licensing process in this report, staff is relying on the agency to successfully complete its automation project and implement changes it has identified to streamline the licensing process to ensure it is providing the best possible service to its licensees.

The following material summarizes the Sunset staff recommendations on the Texas Alcoholic Beverage Commission.

Issues/Recommendations

Issue 1

TABC Lacks the Clear Focus and Strategic Direction Needed in Today's Alcoholic Beverage Regulatory Environment.

Key Recommendations

- Update TABC's mission to better reflect today's alcoholic beverage regulatory environment and the agency's role in public safety issues.
- Direct TABC to improve its strategic planning process so that it helps prioritize the agency's activities and measures its progress toward meeting its goals.

Issue 2

TABC Does Not Manage Its Enforcement Activities to Best Protect the Public's Safety.

Key Recommendations

- Require TABC to maintain a schedule of sanctions that includes all information necessary to ensure fair and consistent application of penalties.

- Authorize the agency to assess penalties according to the economic benefit a licensee may gain through noncompliance.
- Require TABC to develop a risk-based approach to enforcement and to better measure the impact of its enforcement activities on public safety.
- Require TABC to develop standard procedures for handling complaints and for tracking and analyzing complaint data.

Issue 3

Over-Regulation of Certain Business Practices Serves No Consumer Interest, Imposes Unnecessary Costs on the Industry, and Creates Excessive Burdens for the Agency.

Key Recommendations

- Eliminate restrictions on the size of beer containers that can legally be sold in Texas.
- Eliminate label approval and testing for liquor and wine, and instead authorize TABC to register federal certificates of approval for these products.
- Allow distributors to report retailers who are delinquent in making payments for liquor and wine by electronic mail or other means, and work towards phasing out the paper-based delinquency list.

Issue 4

TABC Lacks an Effective Approach for Resolving Key Marketing Practices Regulatory Issues, Resulting in Inconsistent Enforcement and Unnecessary Costs to the Industry.

Key Recommendation

- Require TABC to develop a formal process for making policy decisions regarding marketing practices regulations, and for communicating these decisions to agency staff and the industry.

Issue 5

TABC Lacks a Consistent and Formal Approach to Investigating and Resolving Complaints Against Its Employees.

Key Recommendations

- Require TABC to maintain an internal affairs function to ensure fair, effective, and impartial investigations of alleged misconduct by law enforcement officers and other employees.
- Require the agency to track and report complaint information to the Administrator and the Commission on a regular basis.

Issue 6

Texas Has a Continuing Need for the Texas Alcoholic Beverage Commission.

Key Recommendation

- Continue the Texas Alcoholic Beverage Commission for 12 years.

Fiscal Implication Summary

This report contains recommendations that will have a fiscal impact to the State. These recommendations are discussed below.

- *Issue 3* - Removing container size restrictions for beer could increase fee revenues due to increased product approvals, however reduced wine label approvals may offset these gains. Further, the agency would be able to set its label approval fees to recover the cost of this regulation. The management action directing the agency to phase out the paper-based delinquency list could save $12,000 a year, once fully implemented.

Issues

Issue 1

TABC Lacks the Clear Focus and Strategic Direction Needed in Today's Alcoholic Beverage Regulatory Environment.

Summary

Key Recommendations

- Update TABC's mission to better reflect today's alcoholic beverage regulatory environment and the agency's role in public safety issues.
- Direct TABC to improve its strategic planning process so that it helps prioritize the agency's activities and measures its progress toward meeting its goals.

Key Findings

- The agency's statutory mission has not kept pace with changes in the industry it regulates or social concerns regarding alcohol.
- TABC's strategic planning process does not reflect or address the evolving needs of the agency.
- The agency lacks key management tools necessary to support its strategic planning process.

Conclusion

The Alcoholic Beverage Code does not reflect the modern environment in which TABC operates. The Code also does not provide clear guidance to the agency on what its priorities or strategic direction should be. Without such direction, TABC has had difficulty focusing its efforts on issues with the greatest impact on public safety. In addition, the agency lacks a comprehensive strategic planning process to help guide its daily activities and measure its progress toward meeting specific goals and objectives. The recommendations included in this issue would provide a framework for TABC to have a clearer mission and strategic direction that better reflects today's alcoholic beverage regulatory environment and the public safety needs of the state. These recommendations would also direct the agency to develop better management tools to help it stay focused on its goals and evaluate its effectiveness in regulating the alcoholic beverage industry.

Support

The Alcoholic Beverage Code defines the agency's mission very broadly and requires it to tightly regulate the alcoholic beverage industry.

TABC is charged with protecting the welfare, health, peace, temperance, and safety of the people.

- TABC's enabling statute, the Alcoholic Beverage Code, was originally enacted into law in 1935, two years after the end of Prohibition. The Code is "an exercise of the police power of the state for the protection of the welfare, health, peace, temperance, and safety of the people" of Texas. The agency has adopted that statement as its mission and added language about facilitating fairness, balanced competition, and responsible behavior within the alcoholic beverage industry through voluntary compliance.
- The original purpose of regulating the alcoholic beverage industry was to prevent close financial and familial ties between the manufacturers and sellers of alcohol. Such ties were the main source of corruption in the alcoholic beverage industry and of the unregulated sale of alcohol to consumers before and during Prohibition. As a result, the Legislature created TABC to supervise, inspect, and regulate the production, importation, exportation, transportation, sale, storage, distribution, and possession of alcoholic beverages. The agency accomplishes this mission by licensing manufacturers, wholesalers, and retailers and performing traditional law enforcement activities to uncover violations of the Alcoholic Beverage Code.
- A three-member, part-time governing Board oversees the agency and appoints the Administrator who manages TABC's day-to-day operations. In fiscal year 2003, the agency had a $25.2 million budget and a staff of 515 employees. Only a quarter of these employees are located at the Headquarters in Austin. The rest work in the agency's 52 field offices located throughout the state and 19 ports of entry located along the Mexico border. Most of the agency's personnel in its field offices are commissioned law enforcement officers. Other field personnel include compliance auditors, tax collectors at the ports of entry, and administrative support staff.

The agency's statutory mission has not kept pace with changes in the industry it regulates or social concerns regarding alcohol.

TABC's mission is reminiscent of Prohibition when corruption and unregulated alcohol consumption were serious social and political issues.

- While TABC's mission, as defined in statute, has always focused on public safety, it does not fully reflect today's social concerns regarding alcohol consumption. The idea that an agency of the state should regulate alcohol to protect the welfare, health, peace, and temperance of the people is reminiscent of the era following Prohibition when large-scale corruption in the alcoholic beverage industry and unregulated alcohol consumption were serious social and political issues. Today, however, Texans' concerns regarding alcohol focus more on responsible drinking, limiting access to alcohol by minors, and reducing the harm caused by drinking and driving.

- At the same time, the alcoholic beverage industry represents a large and well-established component of our economy. However, the idea that the agency should facilitate fairness, balanced competition, and responsible behavior within the industry through voluntary compliance is not clearly reflected in the Code. The Code does not incorporate the ideas of promoting fairness and consistency in how the agency regulates the industry.

  The Code also does not reflect the industry's duty to act responsibly by voluntarily maintaining appropriate relationships among different tiers in the industry and marketing its products in responsible ways. Rather than promoting responsibility, the Code reflects the era following Prohibition when the State wanted to maintain strict control over all aspects of the alcoholic beverage industry to avoid the problems of earlier times. As a result, the Code approaches the regulation of the alcoholic beverage industry by imposing numerous restrictions on every aspect of the industry and requires TABC to enforce all of these restrictions. As discussed in other issues in this report, many of the restrictions are very difficult for the agency to enforce, especially given its limited resources, and do not always relate to the mission of protecting public safety.

The Alcoholic Beverage Code reflects the era following Prohibition when the State wanted to maintain strict control over all aspects of the industry.

- Another priority of TABC is facilitating commerce by ensuring new businesses are able to receive their licenses and start operating as soon as possible. Although this priority is not reflected in the agency's statute, it is easy to see in the agency's current project to upgrade its outdated computer systems. This project will fully automate the licensing process to reduce large volumes of paper files, ensure faster access to licensing information, and allow some licensees to renew online. The Legislature saw the need for this project last session and gave TABC $2.3 million for its completion.

- The Alcoholic Beverage Code provides little guidance to the agency on what its priorities and goals should be. The Code mainly consists of prohibitions on activities within the alcoholic beverage industry or on the consumption of alcohol. For example, the Code prohibits the sale of alcohol to minors and the possession of alcohol by minors, but it does not clearly reflect the agency's role in preventing and reducing such violations.

  Without clear guidance in its statute, TABC is left to determine how to use its limited resources to enforce the myriad restrictions in statute and is not always able to focus on issues affecting public safety. Priorities can vary significantly depending on decisions of the agency's executive management, industry pressure on the agency, and the discretion of individual agents in the field.

Rather than providing guidance to the agency, the Code mainly consists of prohibitions.

TABC's strategic planning process does not reflect or address the evolving needs of the agency.

- The strategic plan, which all agencies are required by law to develop, can offer important insight into matters that affect an agency's mission over the next five years. Despite its lack of clear direction from statute, TABC has set nine management goals in its strategic plan, as listed in the textbox, *TABC's Strategic Management Goals*, to guide the agency's activities.

TABC's Strategic Management Goals
Fiscal Years 2005 – 2009

1. To ensure that efficiencies and streamlining are identified and implemented where possible as the agency moves through its licensing technology transformation, while pursuing legislative change to eliminate impediments.
2. To focus enforcement programs on identifying retailers who sell to intoxicated persons and minors.
3. To continue to encourage retailers to avail themselves of the benefits of seller training.
4. To continue to focus educational efforts of the agency to the members of the alcoholic beverage industry and on programs to school-aged children and college-aged adults, which will have the most immediate impact.
5. To learn and stay current in the methods of operation among the upper tiers of the industry.
6. To reinvigorate the agency's efforts in partnering with coalitions, groups, and industry members to raise awareness in issues involving the sale of alcohol beverages to minors and intoxicated persons.
7. To address the ongoing issue of training new staff as well as current employees while faced with loss of vast amounts of institutional knowledge.
8. To continue expanding the agency's effort in effective communication, both internally and externally, using all available means.
9. To ensure through available avenues that agency employees receive fair pay based on responsibilities.

- Unfortunately, TABC's strategic planning process lacks several key elements that are necessary to fully implement these goals and measure the agency's progress in meeting them. TABC's ability to strategically plan its future has been hampered by a number of factors over the years. The following examples indicate two shortcomings in the preparation and use of TABC's strategic plan.

  Turnover in the executive management of an agency can cause instability and result in shifting priorities. Over the past twelve years, TABC has had four Administrators, with an Acting Administrator in place between Administrators for six months at a time. The Administrator's job is to ensure the agency stays focused on its priorities as laid out in the strategic plan. However, as Administrators come and go, the agency has had trouble maintaining its strategic direction.

As Administrators come and go, the agency has had trouble maintaining its strategic direction.

  TABC's strategic planning process does not adequately reflect the unique challenges of each individual region of the state. In developing its most recent strategic plan, the agency spent a great deal of effort gathering input from its employees and customers in each of its five regions. For example, the staff in each region was asked to identify their accomplishments and challenges. While much of the feedback was common to all regions, it also represented the unique environment and specific challenges of each region. This input made TABC's executive management more aware of each region's abilities and needs, however, the input was not reflected in the final strategic plan.

The agency lacks key management tools necessary to support its strategic planning process.

- Performance measures are an integral part of the legislative appropriations process and are meant to provide an indication of whether agencies are effectively and efficiently spending tax payer money. However, some of TABC's performance measures are either ill-defined or not appropriately measured, and do not provide a useful indication of whether the agency is successfully performing its functions or what impact the agency is having on licensees' compliance with the law. To be effective, an agency needs clear goals with accurate, attainable performance measures. The chart, *Selected Performance Measure Concerns*, discusses problems with four of TABC's performance measures.

TABC's performance measures do not provide a useful indication of whether the agency is successfully performing its functions.

Selected Performance Measure Concerns

Measure	Actual Performance in FY 2003	Concern with Measure
Percentage of Licensed Establishments Inspected Annually	83.2%	The term "inspected" is not defined. As a result, the agency counts any contact with a licensed establishment, no matter how minor, as an inspection.
Percent of Original License/Permit Applications Processed within 14 Days	99.5%	The agency considers processing time as the number of days from when an application is received at Headquarters to when the license is issued. This measure does not reflect the entire time needed to issue a license. In reality, an applicant may have to wait two months between filling the application and actually receiving the license due to a variety of factors, many of which the agency has no control over.
Percent of Inspections, Analyses, and Compliance Activities Resulting in Administrative or Compliance Action	30.4%	The low percentage would indicate that many of these activities are not resulting in violations, and that the agency, with limited resources, might benefit from targeting these activities based on risk. Further, the term "compliance action" is misleading. While it may indicate action the agency took for failure to comply with the law, in fact two-thirds of the compliance actions in fiscal year 2003 were not related to violations, but were routine administrative activities.
Percent of Report Analyzations Resulting in Administrative or Compliance Action	22.9%	Again, the low percentage would indicate that many of these activities are not resulting in violations, and that the agency, with limited resources, might benefit from targeting these activities based on risk.

An example of a measure that more accurately reflects the agency's effectiveness in enforcing the law is its progress in increasing compliance with laws prohibiting sales of alcohol to minors from 30 percent in the early 1990s to 80 percent today. This increase in compliance was largely accomplished through the effective use of sting operations. Unfortunately, this information is not reflected in the agency's official legislative performance measures.

TABC's strategic plan does not provide information about trends in alcohol consumption or public safety issues.

- Although comprehensive research on issues and demographics affecting the agency is an important management tool, TABC does not make a concerted effort to gather such information. For example, the agency's strategic plan presents some limited projections showing changes in the population of adults, the number of people under 21, and the number of alcohol retailers, from which it draws conclusions about how these changes will affect its activities. However, the strategic plan does not provide more specific information about trends in alcohol consumption or public safety issues related to alcohol, such as traffic fatalities related to alcohol, binge drinking on college campuses, or minor access to alcohol.

  The strategic plan also does not include information about trends in the agency's enforcement activities, such as the most common complaints received or violations found. While certain staff within the agency may have access to this type of information, it is not collected or analyzed in a coordinated way so that management and other divisions may use it in their decisionmaking. Without such information, TABC is unable to assess its effectiveness in regulating the alcoholic beverage industry and enforcing the law.

TABC does not maximize its limited resources to ensure efficiency and focus on its strategic goals.

- The functions of TABC's staff in each of its three main divisions - Enforcement, Licensing, and Compliance - in many cases do not relate to the essential function of that division. For example, enforcement staff spend roughly 18 percent of their time performing licensing functions, such as answering applicant questions and ensuring applications are filled out completely, and 10 percent of their time providing educational programs. These activities do not represent the best use of commissioned peace officers' time, which would be better spent on traditional law enforcement activities.

TABC's legislative appropriations do not adequately reflect the amount of resources the agency devotes to licensing.

  The fact that enforcement staff spend a significant amount of time on licensing activities also indicates that the functions of each division are not well-defined. As such, TABC's legislative appropriations do not adequately reflect the amount of resources the agency devotes to individual functions. The enforcement function represented 57 percent of the agency's budget in fiscal year 2003. While this strategy represents the agency's expenditures on its enforcement staff and activities, the enforcement staff also spent time performing licensing functions. In addition, compliance staff spent at least 10 percent of their time on licensing functions, such as inspections of premises to be licensed. In total, the licensing function probably consumes significantly more staffing resources than the 7 percent of the agency's budget it represented in fiscal year 2003. As a result, the agency's organizational chart, legislative appropriations request, and strategic plan do not accurately represent the amount of resources dedicated to licensing.

- Although TABC puts much emphasis on the need for educational programs to help prevent violations of alcoholic beverage laws, it does not have a clear plan to guide its programs. Several of TABC's goals in its most recent strategic plan concern education, including focusing educational efforts on members of the alcoholic beverage industry, school-aged children, and college-aged adults; promoting training for alcohol sellers and servers; raising awareness of issues regarding the sale of alcohol to minors and intoxicated people; and effectively communicating with the regulated community.

  While these goals all relate back to the idea of education, they encompass many activities located in different divisions within the agency. For example, the Enforcement Division conducts educational programs and administers grants to community groups for their own programs. At the same time, the Compliance Division administers the seller/server training program and everyone in the agency, from the General Counsel to agents in the field, answers questions from regulated businesses about how to interpret the Alcoholic Beverage Code.

  Not only are educational programs spread out within the agency, they often take time away from staff's primary duties. The Enforcement Division has limited staff. Conducting educational programs and administering grants diverts the Division's focus away from its important law enforcement functions. Further, the agency's enforcement agents are an expensive resource and their training is in law enforcement, not public education or grant writing. In fact, no one within the agency except a few employees involved in the seller/server training program, have specific knowledge or experience in developing educational programs or materials for the industry or the public.

TABC's educational activities are spread throughout the agency and often take time away from staff's primary duties.

Recommendations

Change in Statute

1.1 Update TABC's mission to better reflect today's alcoholic beverage regulatory environment and the agency's role in public safety issues.

This recommendation would better define the agency's mission in statute by updating the existing language to focus the agency on:

- protecting the public safety by deterring and detecting violations of the law;
- promoting legal and responsible alcohol consumption;
- ensuring fair competition within the alcoholic beverage industry;
- ensuring consistent, predictable, and timely enforcement of the law;
- ensuring a consistent, predictable, and timely licensing process;

- promoting and fostering voluntary compliance with the law; and
- communicating the requirements of the law clearly and consistently.

Management Action

1.2 Direct TABC to improve its strategic planning process so that it helps prioritize the agency's activities and measures its progress toward meeting its goals.

This recommendation aims to help TABC develop a more effective strategic planning process using the steps laid out in the textbox, *An Effective Strategic Management Process*. More specifically, TABC should incorporate the following activities into its strategic planning process to allow the agency to stay focused on its mission, as laid out above.

> ***An Effective Strategic Management Process***
>
> 1. Collect and analyze data.
> 2. Set strategic direction.
> 3. Create organizational flexibility to implement strategic plan.
> 4. Implement effective performance measurement system.
> 5. Evaluate and report on outcomes.
> 6. Identify improvements for next cycle.

- TABC should work with the Legislative Budget Board and the Governor's Office of Budget, Planning, and Policy to change its strategic plan and performance measures as necessary to carry out the mission laid out in Recommendation 1.1. The goals should relate directly to that mission and the measures should be designed to provide an accurate picture of the effort being measured. The measures should not only capture the agency's activities but should also assess the effect in terms of outcomes.
- TABC should develop region-specific goals as building blocks for the agency's strategic plan. Each region should use local input to determine the priorities for attention and to best allocate resources.
- TABC should establish procedures to monitor progress in meeting its statewide and region-specific strategic goals, and identify organizational and operational changes as needed to address problems that may arise with meeting its goals.

1.3 Direct TABC to focus more effort on research and data collection to better support its mission and goals.

The agency should place a higher focus on collecting and analyzing data related to issues affecting TABC's mission, such as traffic accidents involving alcohol, trends in binge drinking on college campuses, and how changes in the economy will affect the sale of alcohol and the number of licensed retailers. Such data should be collected and analyzed on a regional basis to help TABC's management make decisions about how best to allocate resources.

1.4 Direct TABC to evaluate alternative approaches for administering its educational programs to better support its mission and goals.

The agency should develop a detailed plan to guide its administration of existing programs and implementation of new ones. In creating this plan, the agency could consider consolidating the following duties and dedicating staff who are specialists in educational programs to perform these functions:

- developing educational programs and materials for specific groups, including school-aged children, college-aged adults, community groups, regulated businesses, and others;
- seeking out and applying for grants to fund the agency's educational programs;

- administering the agency's existing grant programs, in which the agency gives money to community groups for their own programs;
- administering the seller/server training program; and
- seeking opportunities to enhance TABC's outreach through its educational programs.

Impact

These recommendations would provide a framework for TABC to have a clear mission and strategic direction that better reflects the modern alcoholic beverage regulatory environment and the public safety needs of the State. The agency would be able to develop better management tools to help it stay focused on its goals and evaluate its effectiveness in enforcing the law and regulating the alcoholic beverage industry.

Fiscal Implication

These recommendations would not have a fiscal impact to the State. Recommendations 1.2, 1.3, and 1.4 are management actions, and the agency should implement them using existing resources.

Issue 2

TABC Does Not Manage Its Enforcement Activities to Best Protect the Public's Safety.

Summary

Key Recommendations

- Require TABC to maintain a schedule of sanctions that includes all information necessary to ensure fair and consistent application of penalties.
- Authorize the agency to assess penalties according to the economic benefit a licensee may gain through noncompliance.
- Require TABC to develop a risk-based approach to enforcement and to better measure the impact of its enforcement activities on public safety.
- Require TABC to develop standard procedures for handling complaints and for tracking and analyzing complaint data.

Key Findings

- TABC's current penalty structure limits the agency's ability to effectively deter illegal activities or ensure fairness and consistency in the penalties it assesses.
- The agency does not prioritize its enforcement activities to focus on the most serious public safety issues.
- TABC does not effectively measure its performance on enforcement activities or ensure that regions consistently follow Headquarter's directives.
- The agency does not have an effective and reliable system to manage complaints from the public and other sources.
- TABC does not maximize the time its enforcement agents spend on enforcement activities.

Conclusion

TABC performs a variety of enforcement activities to protect the public's safety and ensure compliance with alcoholic beverage regulations. Sunset staff evaluated how the agency manages these activities and determined that it lacks the necessary procedures and oversight to ensure fair, consistent, and effective enforcement of the law. With enforcement staff located throughout the state in 52 field offices, TABC needs to have detailed procedures in place for assessing penalties, handling complaints, and overseeing regional operations. For example, to adequately address violations of the Alcoholic Beverage Code, the agency must assess penalties that will deter future violations. It must also focus its enforcement activities on the most serious risks to the public. In addition, the agency must track and analyze the right information to have a clear picture of the problems facing the state and each region. Sunset staff's recommendations are intended to strengthen the agency's enforcement process, ensure the fair and consistent application of penalties, and redirect its enforcement efforts toward the more serious violations.

Support

TABC performs a variety of functions to deter, detect, and resolve violations of the Alcoholic Beverage Code.

- TABC employs 236 law enforcement agents who protect public safety by enforcing laws related to the sale and consumption of alcoholic beverages. These agents work out of 52 field offices located throughout the state in five enforcement regions. TABC agents perform a wide range of law enforcement activities, including investigating complaints; conducting minor stings and other undercover operations; monitoring special events where alcohol is sold; and inspecting roughly 80 percent of the state's 36,500 licensed retail establishments, such as bars and liquor stores, each year.

TABC enforcement agents inspect roughly 80 percent of the state's licensed retail establishments each year.

- TABC employs 58 compliance staff across the state to ensure licensees pay their taxes and stay in compliance with the law and agency rules. TABC's compliance officers perform a wide variety of activities, including reviewing monthly tax returns and conducting on-site audits of wholesalers who pay the tax. The agency also conducts audits to ensure compliance with laws governing the operation of private clubs and requirements for food and beverage permit holders. In fiscal year 2003, compliance officers analyzed about 28,000 excise tax reports, and conducted 112 on-site excise tax audits, 453 private club analyses, and 1,245 food and beverages analyses.
- Through these law enforcement and compliance activities, TABC staff find administrative and criminal violations. Enforcement agents may take three types of action in response to a violation. They may file an administrative case if it involves a licensee who violates TABC law or rule; write a criminal citation against an individual who commits a misdemeanor or felony offense; or give a verbal or written warning. Compliance staff may also take administrative actions to resolve violations they find through their audits and other compliance activities.

  TABC authorizes its agents in the field, and compliance staff, to resolve administrative violations by assessing fines or recommending the temporary suspension or cancellation of a license. Agency staff use a standard penalty chart laid out in rule to determine the appropriate penalty for each violation. In fiscal year 2003, the agency resolved 16,483 administrative violations.

TABC's current penalty structure limits the agency's ability to effectively deter illegal activities or ensure fairness and consistency in the penalties it assesses.

- For most violations, the Alcoholic Beverage Code allows licensees to choose between a temporary suspension of their license, which can range from seven to 60 days, or a fine, which can range from $150 to $25,000 for each day their license could have been suspended. However, as an informal policy, the agency routinely chooses to assess no more than $150 per day of suspension. Although TABC increases the number of days of suspension, and thus the amount of the fine, according to the seriousness of the offense and the number of previous violations, the agency limits its ability to effectively deter the most serious types of offenses by choosing to consistently use the lowest end of its extensive fine authority.

The agency consistently uses the lowest end of its extensive fine authority.

- TABC authorizes its agents to deviate from the penalty chart based on aggravating and mitigating circumstances, but the agency fails to provide direction on what those circumstances may be and how they can affect the penalty assessed. As shown in the textbox, *Examples from TABC's Standard Penalty Chart*, agents have a wide range of sanctions to choose from when assessing penalties, such as seven to 20 days of suspension for the first violation for sale of alcohol to a minor. By not providing any guidance for when seven days is appropriate versus 20 days, for example, the agency cannot ensure fair and consistent application of penalties. Until recently, the agency did not require agents to report deviations from the penalty chart to Headquarters, further limiting the agency's ability to oversee how penalties are assessed in the field.

Examples from TABC's Standard Penalty Chart

Offense	Number of Days of Suspension		
	1st Violation	2nd Violation*	3rd Violation*
Sale to a minor	7-20	10-90	60 days or more or cancellation
Permitting a minor to possess or consume alcohol	7-15	10-90	60 days or more or cancellation
Sale to an intoxicated person	10-15	15-30	30 days or more or cancellation
Gambling, prostitution, or bribery occurring at licensed establishment	15 days or more or cancellation		

*Both second and third violations must occur within 36 months of the first violation.

- Recent legislative changes, effective in fiscal year 2004, prohibit TABC from considering the economic impact on a business of a penalty. As a result of these changes, the Code specifically prohibits the agency from considering a licensee's volume of alcoholic beverages sales, overall receipts, taxes paid, or financial condition. The agency has interpreted this new provision to mean that, when assessing a penalty, it cannot consider the amount of additional income a licensee may have earned by committing a violation. For some licensees, this policy could result in a fine that is less than the economic benefit gained through noncompliance, thus limiting the agency's ability to effectively deter future violations.

When assessing a fine, TABC cannot consider any additional income tied to the violation itself.

- TABC does not address all illegal sales to minors in its penalty matrix and imposes lower sanctions for minors-related offenses than its statute authorizes. TABC's standard penalty chart identifies sales of alcohol to minors who represent themselves to be 21 years of age by displaying a fake ID, but does not address sales to minors that were made without this mitigating factor. In addition, a recent change in law allows the agency to assess stiffer penalties for selling or permitting a minor to possess and consume an alcoholic beverage, but the agency continues to impose significantly lower sanctions than authorized by law.[1] Although the agency is not required to consistently use the higher end of its sanction authority, it is limiting its ability to effectively deter sales of alcohol to minors by not updating its penalty chart to reflect its ability to use these stronger sanctions.

- TABC's standard penalty chart lacks information vital for the regulated community and the public to understand how penalties are assessed and to know stiff penalties exist to deter violations. For example, the chart does not reflect the amount of fines that can be assessed for each violation and only lists the number of days of suspension. The chart also only contains the most common types of violations, mostly related to retailers, with few violations that apply to manufacturers and wholesalers, such as those related to tax payments or marketing practices. Lack of a standard penalty chart for all types of violations hinders the agency's ability to assess fair and consistent sanctions.

The agency does not prioritize its enforcement activities to focus on the most serious public safety issues.

- TABC has no formal policy or goals in place to direct its agents to target their enforcement activities based on public safety risk, such as by focusing on more serious violations or businesses with a history of problems. Instead, the agency's direction focuses officers priority on visiting as many establishments as possible each year.

TABC's goal is to visit as many establishments as possible, not necessarily ones with problems.

- This focus on a high presence in the businesses may come at the expense of not detecting more serious violations. Agents may focus on routine inspections that allow them to more easily meet the expectation for getting out into establishments, rather than using enforcement tools, such as stings, that are more likely to detect serious criminal violations, but require a greater investment of time and resources. For example, in fiscal year 2002, TABC met its performance target related to inspections, but failed to meet its target for detecting criminal violations, such as sales to minors or intoxicated persons. The agency stated in its fourth quarter performance measurement report that:

  "Agents exceeded their inspection and inspection coverage goals, but did not find the number of criminal violations that was expected. This is due in part to the priority given the coverage goal by some field supervisors. Greater coverage means spending more time in places where serious violations are less likely to be found."

  One other concern with not setting clear expectations or placing a clear priority on more serious violations is the inconsistency with which regional staff may approach these problems. For example, in fiscal year 2003, the number of stings to detect sales to minors varied from 71 in one region to more than 1,000 in another region.

- While individual offices or agents may place a greater emphasis on establishments with a clear and known history of violations, the agency cannot ensure that its agents are approaching this in any consistent fashion. Placing a greater focus on monitoring these businesses can help to ensure that they take corrective steps to address past deficiencies. Not addressing known problem establishments can contribute to serious community problems. In addition, other industry members may be less serious about complying with regulations if it is clear that known violations are not being dealt with effectively.

- Agents also expend a significant amount of time on the issuance of administrative warnings. In fiscal year 2003, agents wrote warnings in response to 16,483 violations, representing 71 percent of the agency's administrative violations. Of these warnings, 1,048 were for possession of alcohol that is unfit for human consumption, which largely involved the presence of fruit flies or other insects in bottles of alcohol used to pour mixed drinks in bars. While warnings are a key part of any enforcement effort, Sunset staff determined that the agency could place a greater focus on investigating serious violations without a major loss to its more routine oversight duties.

TABC does not effectively measure its performance on enforcement activities or ensure that regions consistently follow Headquarter's directives.

- TABC cannot ensure that its enforcement program is effective because the agency does not measure its performance in enforcing the law. For example, the agency does not analyze information on each of its enforcement activities, such as stings, routine inspections, or investigations. The agency also does not analyze the outcomes of its enforcement activities. Although TABC relies on its enforcement agents to detect most violations, it does not track or analyze the nature of these violations, their disposition, or the types of businesses that produce most violations on a regional and statewide basis. Without analyzing this data by looking at trends and comparing the performance of each region, the agency cannot get a clear picture of the problems facing the state and each individual region. This can further impact its ability to effectively manage its resources and focus enforcement efforts where they are most needed.

TABC cannot ensure that its enforcement program is effective because the agency does not measure its performance.

- Another concern identified relates to two of TABC's key legislative performance measures. These measures direct the agency to inspect 78.5 percent of all licensed establishments and to conduct about 100,000 inspections annually. As defined in TABC's strategic plan, "the term inspection extends to everything enforcement agents do except when in the office or engaged in educational activities." Because the agency counts so many different activities as inspections, including investigations and even stings, and does not clearly define what these activities entail, the agency may not be accurately reflecting its true performance to the Legislature.

  For example, under its current definition the agency counts any non-licensee activities, such as a vehicle stop or monitoring of a private party, as an inspection towards its 100,000 goal. The agency also double-counts certain activities, such as its minor sting operations. Stings require a minimum of two teams of agents so TABC counts them as two separate inspection contacts with a licensee even though it was only one operation.[2] In fiscal year 2003, the agency counted 5,521 minor stings toward its performance measure, while it conducted only 3,063 stings.

The agency also counts as a routine inspection any physical presence, however brief and for whatever purpose, on a licensee's premise even though the premise may not actually be inspected. In theory, a routine inspection should include a variety of checks to ensure compliance with all requirements for licensed premises, such as posting an up-to-date TABC license and all other required signage and proper handling of tax stamps. However, agents do not always check for compliance to this level. Further, individual agents may check for different requirements, depending on what they consider important according to their training and experience. Lack of specific procedures to follow while inspecting premises can result in inspections that are neither thorough nor consistent.

TABC counts any presence on a licensee's premise as an inspection, even if no inspection is done.

- In addition, TABC does not adequately ensure that its policies and procedures for guiding regional enforcement activities are adequately followed. Many of TABC's policies and procedures are disseminated to regional supervisors verbally or through memoranda, and are not reflected in the enforcement policies and procedures manual for use by the entire staff. Because TABC last updated its enforcement manual in 2000, many of its more recent regional directives may not have been effectively communicated to each agent, which can lead to policies not being consistently followed. For example, Sunset staff reviewed reporting documents that indicated that one region had miscalculated its sting activities by failing to follow TABC's procedural directive.

The agency does not have an effective and reliable system to manage complaints from the public and other sources.

- Although TABC advertises its toll-free complaint line and allows the public to make a complaint against licensed establishments on its Web site, the agency does not provide the public with other useful information or procedures on how to file a complaint. For example, TABC has not developed a standard complaint form that the public can use in making a complaint. Without a standard form that is readily available to the public, the agency may not receive all information necessary to adequately investigate a complaint, thus requiring the agency to follow-up with the complainant at a later time.

  TABC's rules do not contain information on how it handles complaints from receipt to disposition. Consequently, the process lacks transparency to the public, and the agency cannot ensure consistency in the handling of complaints over time. TABC also does not provide information to the public about how it handles and resolves complaints, thus missing an opportunity to demonstrate its responsiveness to the public.

- TABC has no requirement to address complaints according to risk and allows each region to determine how to prioritize the complaints it receives. The agency currently does not know whether its regions address complaints on a first-come, first-served basis or according to the seriousness of the allegations. Consequently, the agency has no way to ensure that the most serious problems are addressed first so that the agency places its attention where it is most needed.

- TABC has insufficient oversight of its complaint process from the opening of a complaint to its disposition. In fiscal year 2003, the agency received 5,719 complaints from the public, local law enforcement agencies, and other sources. However, during the Sunset review, TABC had difficulty providing accurate and meaningful information on its complaint activities.

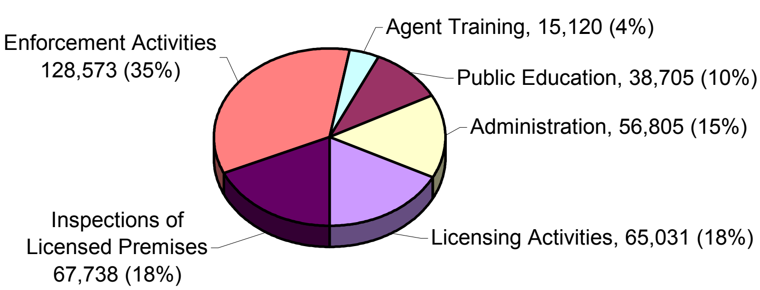
  For example, the agency does not maintain information on the nature of the complaints it receives, the final dispositions of those complaints, or the types of businesses that produce the most complaints. The agency does not track complaints on a regional basis to know how many complaints each region receives and how they are resolved. Although the agency tracks the time it takes to investigate a complaint, it is unable to determine how long it takes overall to resolve most complaints. This is because the agency does not track the length of time from when a complaint is received until it is finally resolved, including taking enforcement action against any resulting violations. And finally, the agency does not provide any information regarding the nature of the complaints it receives or how they are resolved to its Board. TABC's new computer system should greatly facilitate the agency's ability to track and analyze this type of data.

TABC does not maximize the time its enforcement agents spend on enforcement activities.

- TABC enforcement agents spend more than half their time on tasks such as licensing, routine inspections, and administration that do not necessarily require, or most effectively use, the specific training of a commissioned peace officer. This is illustrated in the pie chart, *Use of TABC Agent Work Hours Statewide*.

TABC's agents spend more than half their time on tasks that do not require, or most effectively use, their training.

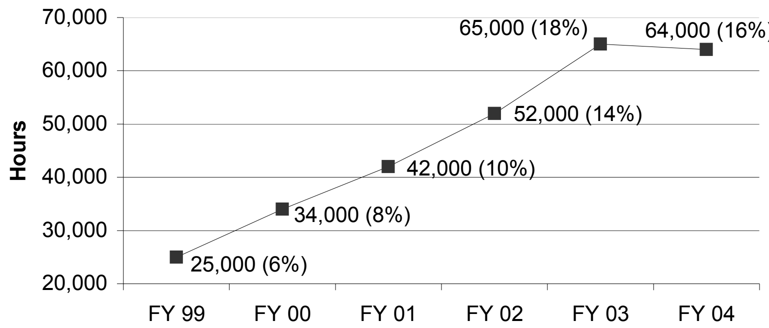
Use of TABC Agent Work Hours Statewide
FY 2003



Enforcement Activities
Complaint Investigations - 52,020 (14%)
Special Events - 26,231 (7%)
Inspections of Non-Licensed Premises - 21,317 (6%)
Case Adjudication - 15,382 (4%)
Minor Stings - 7,458 (2%)
Stings on Sales to Intoxicated Persons - 6,165 (2%)

- Although the agency employs licensing staff, much of a TABC agent's time is devoted to licensing activities. These activities include conducting interviews with applicants, processing application paperwork, checking new locations to see that they meet licensing requirement; and inspecting businesses whose licenses are expired, cancelled, or suspended to ensure they are no longer operating. Over the years, TABC agents have had to spend increasingly more time on licensing activities, as shown in the graph, *Trend in Agent Time Spent on Licensing Activities*. In fiscal year 2003, agents spent more than 65,000 hours, or about 18 percent of their time, on licensing activities, which is equivalent to the work hours of 31 full-time equivalent employees.[3]

Trend in Agent Time Spent on Licensing Activities



- Requiring commissioned peace officers to perform licensing activities takes them away from their primary enforcement duties and is not a cost effective use of staff, especially considering the fact that the agency pays more for their services than non-commissioned employees.[4] Use of enforcement officers to do licensing is particularly problematic in the agency's outposts, which are staffed by only a few agents, as shown in the chart, *Percentage of Hours Spent on Various Activities Across TABC Offices*. In fiscal year 2003, outposts spent an average of 31 percent of their time on licensing, with some outposts devoting as much as half their time on that activity.

Commissioned peace officers should spend as much time as possible on enforcement.

Percentage of Hours Spent on Various Activities Across TABC Offices – FY 2003

	Regional Offices Average (Range)	District Offices Average (Range)	Outposts Average (Range)
Licensing Activities	16 (8-30)	17 (10-27)	31 (5-50)
Routine Inspections	23 (16-34)	19 (18-31)	25 (11-44)
Administration	17 (7-29)	15 (5-27)	11 (0-30)
Public Education	11 (5-17)	13 (6-22)	8 (0-20)
Investigations	14 (6-27)	10 (6-14)	7 (2-19)
Minor Stings	2 (0-4)	3 (1-8)	2 (0-6)

- TABC enforcement agents also devote much of their time to routine inspections of licensee's establishments. In fiscal year 2003, enforcement agents spent about 18 percent of their time inspecting licensees. Most of these inspections are simple checks of retail locations, such as convenience stores and restaurants, to ensure compliance with regulatory requirements, and do not require the presence of an enforcement agent.

Recommendations

Change in Statute

2.1 Require TABC to maintain a schedule of sanctions that includes all information necessary to ensure fair and consistent application of penalties.

This recommendation would require TABC to replace its existing standard penalty chart with one that reflects its full penalty authority and provides more complete guidance in assessing penalties. The agency's schedule of sanctions should include both the number of days of suspension for a particular violation and the corresponding fine amount. In developing the schedule, the agency needs to reflect the range of fines it can assess, from $150 to $25,000, according to the seriousness of the offense, the history of compliance, and other criteria set forth in the Alcoholic Beverage Code.[5] The agency's schedule should address the most common types of violations, including those that apply to wholesalers and manufacturers. The schedule should also reflect the agency's more recent statutory authority with respect to sanctions for minor-related offenses.[6]

The schedule of sanctions should allow for deviations due to mitigating or aggravating factors. However, the agency should develop clear policies to guide its staff in evaluating mitigating or aggravating factors in different circumstances, and how these factors could affect the penalty assessment. As part of this recommendation, the agency should require staff to report to Headquarters for approval of all cases in which executive management determines such approval is needed to allow deviation from the schedule.

The Commission should adopt the new schedule of sanctions in rules, providing for input from both the industry and the public. In addition, the agency should post its new schedule of sanctions on its Web site.

2.2 Authorize the agency to assess penalties according to the economic benefit a licensee may gain through noncompliance.

This recommendation would authorize the agency to assess penalties based on any economic benefit a licensee may gain through violating TABC's statute or rules. In implementing this recommendation, the agency would need to develop policies to guide staff in determining how much economic benefit the licensee realized and how that information should affect the amount of the penalty. This recommendation does not affect the statutory language added by the 78th Legislature to prohibit the agency from assessing sanctions according to the volume of sales, receipts, taxes paid, or financial condition of a licensee. Instead, it only applies to the specific amount of excess revenue a licensee may have earned by not complying with the law.

2.3 Require TABC to develop a risk-based approach to enforcement and to better measure the impact of its enforcement activities on public safety.

This recommendation would require the agency to develop policies and procedures for more effectively conducting and overseeing its enforcement activities according to the following provisions.

- Require TABC to develop a risk-based approach to conducting its enforcement activities by focusing on detecting serious violations with an impact on public safety, and monitoring businesses with a history of complaints and violations, and any other factors the agency deems important.

- Require TABC to develop benchmarks and goals to track key enforcement activities and their results. The agency should track the number of enforcement activities by type, the number of violations detected from each activity, the amount of time spent on specific enforcement activities, and any other information determined necessary by executive management. TABC should also make use of this and other information to compare regional performance and determine best practices.
- Require TABC to track and analyze the nature of violations detected, their disposition, and the businesses that produce the most serious violations, statewide and per region. The agency should compile detailed statistics and analyze trends to get a clearer picture of problems facing the state. The agency should summarize these statistics and trends for executive management on a monthly basis and on a quarterly basis for its Board, as well as making this information available on its Web site.

2.4 Require TABC to develop standard procedures for handling complaints and for tracking and analyzing complaint data.

This recommendation would require the agency to develop policies and procedures for effectively managing the complaints the agency receives according to the following provisions.

- Require the Commission to adopt rules that clearly define the agency's complaint process from receipt to disposition.
- Require the agency to address complaints according to risk by placing complaints in priority order so that the agency handles the most serious problems first.
- Require TABC to develop a standard form for the public to make a complaint against an establishment. The complaint form should be available to the public on the agency's Web site.
- Require TABC to compile detailed statistics and analyze trends on complaint information to get a clearer picture of problems people have with its licensees. This complaint data should include information such as the nature of complaints and their disposition, and the length of time to resolve complaints. The agency should also track this information on a regional basis. The agency should report this information monthly to executive management and quarterly to the Commission. As part of this recommendation, TABC should make general information about the nature and disposition of complaints available on its Web site.

Management Action

2.5 Direct TABC to better define its performance measures to more accurately reflect the agency's enforcement activities.

TABC should work with the Legislative Budget Board and Governor's Office of Budget, Planning, and Policy to redefine its performance measures related to its enforcement activities. As part of this recommendation, the agency could consider creating additional performance measures to more specifically measure its various enforcement activities, such as stings, complaint investigations, and routine inspections. Alternatively, the agency could simply redefine its current performance measures so that it applies to all enforcement activities, not just inspections. TABC should also ensure agents accurately account for their enforcement activities to avoid double-counting and other procedures that inaccurately reflect the agency's performance.

2.6 Direct TABC to develop standard procedures for conducting routine inspections of licensed establishments that include the use of a checklist and non-commissioned staff.

This recommendation would direct TABC to develop standard procedures for conducting routine on-premise inspections, including the use of a checklist of the types of violations staff should consistently check, to ensure that they consistently and thoroughly inspect each establishments. The agency should also consider using non-commissioned staff to conduct routine inspections.

2.7 Direct TABC to develop and implement a plan to increase the time its agents spend on enforcement activities.

This recommendation would direct the agency to develop a plan by September 1, 2006 for increasing the time its agents spend on enforcement activities. This plan should include strategies to reduce time spent on licensing and administrative activities and for using non-commissioned staff to perform routine inspections, as mentioned above. The agency could evaluate different options, such as redirecting some of its existing compliance and licensing staff or requesting additional resources from the Legislature to hire non-commissioned staff to perform a portion of these licensing or inspection duties. The agency's new automated licensing system should greatly facilitate this initiative by reducing time spent on licensing overall, and freeing officers to spend more time on enforcement.

In developing the plan, the agency should consider conducting an analysis of its enforcement staffing in each office to determine the cost-effectiveness of reorganizational alternatives, using input from the regions and the agency's internal auditor. Specifically, the agency should examine ways to reduce the need for enforcement agents in remote offices to spend up to 50 percent of their time on licensing activities.

2.8 Direct TABC to update its enforcement policies and procedures manual.

This recommendation would direct TABC to incorporate all of its current enforcement policies and procedural directives, communicated either verbally or through emails and memoranda, into its enforcement manual by March 1, 2006.

Impact

Overall, these recommendations would significantly strengthen TABC's enforcement functions. They would ensure that the agency is taking more consistent and appropriate disciplinary actions against establishments by updating its standard penalty chart and analyzing information on the disposition of complaints and violations detected. Conducting enforcement activities and addressing complaints according to risk would ensure that the agency places its limited enforcement resources where they are needed most. Tracking enforcement activities and setting goals would allow the agency to measure its performance and better oversee its regions. Using a checklist when inspecting establishments for compliance with basic regulatory requirements would ensure consistent and thorough inspections.

Fiscal Implication

The statutory recommendations in this issue would not have a fiscal impact to the State. However, the management recommendation directing TABC to develop a plan to increase the time its agents spend on enforcement activities could have a fiscal impact to the State, depending on how the agency approaches the problem. The agency should develop and implement the plan according to its available resources or whatever additional resources the Legislature appropriates for this purpose. The intent of this recommendation is to allow agents to spend more of their time on enforcement activities, while using less expensive non-commissioned staff to perform more routine licensing and inspection activities. This should also reduce the need for additional resources for law enforcement agents.

While this recommendation simply directs the agency to develop a plan, to implement this plan, the agency may need additional staff. For example, hiring five licensing staff, who could process 1,500 applications annually, and six compliance staff, who could perform about 25 percent of the agency's routine inspections each year, would cost $353,000 for salaries and benefits per year.

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1 The agency bases its penalty decisions for many of its minor-related offenses on a 1977 provision of the Alcoholic Beverage Code that limits the penalty to a suspension of 60 days or more or cancellation on the third violation. However, a more recent amendment to the Code authorizes stronger penalties by allowing TABC to suspend a license for up to 90 days for a first violation, up to six months for a second violation, and up to 12 months for a third violation. The agency may also choose to cancel a license on the second offense.

2 Stings usually require two or more teams: one team that enters a licensee's premises with the minor to ensure the minor's safety, and another team that enters the premises after the sting to issue a criminal citation if a sale was made. Currently, the first team would count its activity as a sting while the second team may count it either as a sting or a routine inspection.

3 The State Auditor's Office defines a full-time equivalent employee as an employee working 2,088 hours per year.

4 Salaries for TABC's enforcement agents start at $36,400, and go up to more than $57,000 for Captains. TABC also supplies its agents with vehicles, portable radios, firearms, and other equipment, and provides additional benefits, such as hazardous duty pay and laundry allowances. The initial cost of the equipment is approximately $29,000, with annual operating costs of $840 per agent. In contrast, the starting salary for a non-commissioned accounts examiner, who performs licensing work for the agency, is $23,052 and more than $35,100 for more experienced employees, with no additional costs, such as for firearms or hazardous duty pay.

5 Texas Alcoholic Beverage Code, Section 11.641.

6 Texas Alcoholic Beverage Code, Section 106.13.

Issue 3

Over-Regulation of Certain Business Practices Serves No Consumer Interest, Imposes Unnecessary Costs on the Industry, and Creates Excessive Burdens for the Agency.

Summary

Key Recommendations

- Eliminate restrictions on the size of beer containers that can legally be sold in Texas.
- Eliminate label approval and testing for liquor and wine, and instead authorize TABC to register federal certificates of approval for these products.
- Allow distributors to report retailers who are delinquent in making payments for liquor and wine by electronic mail or other means, and work towards phasing out the paper-based delinquency list.

Key Findings

- Restricting the size of beer containers sold in Texas serves no clear consumer or state interest, and imposes unnecessary costs and limitations on the industry.
- TABC's liquor and wine approval process duplicates federal processes, serves no clear public health purpose, and creates unnecessary delays in getting products to market.
- TABC's oversight of payments for alcoholic beverages between liquor and wine distributors and retailers is inefficient.

Conclusion

Sunset examined a broad range of regulations that TABC enforces regarding the production, approval, and distribution of alcoholic beverages. Sunset staff applied statutory criteria for determining if less burdensome alternatives to current regulation exist that would still be protective of the public's safety and consumer interests. Sunset staff found that eliminating or streamlining several of the requirements would improve TABC's oversight of the industry by eliminating over-regulation that is duplicative, unnecessarily burdensome for the agency, and not clearly tied to public safety or consumer interests.

Support

TABC regulates the business practices of the alcoholic beverage industry to protect consumers and prevent undue influence of manufacturers and distributors over retailers.

- TABC's statute requires the agency to regulate and enforce certain industry business practices to protect consumers from unsafe or misrepresented products, to ensure against marketing that might encourage excessive consumption, and to prevent manufacturers and distributors from monopolizing retail sales. The law directs TABC to ensure that manufacturers and distributors do not control retailers through unlimited inducements or the extension of credit that would provide an unfair advantage to one retailer over another. The textbox, *Key TABC Business Practices Regulations*, summarizes some of these key regulations.

> ***Key TABC Business Practices Regulations***
>
> TABC accomplishes its oversight of alcoholic beverage industry business practices through the following regulations.
>
> **Beer Container Sizes**
> Beer sold in Texas must be packaged in 7, 8, 12, 16, 24 or 32 ounce containers, or 3.8, 7.75, 15.5, or 31 gallon kegs.
>
> **New Alcoholic Beverage Approval**
> TABC staff approves new products to ensure that labels accurately represent the content and perform chemical analysis to ensure product quality, alcohol content, and that the container holds the stated amount.
>
> **Credit Law - Liquor and Wine**
> Prohibits distributors from extending credit to retailers beyond 25 days. Distributors must report any delinquent retailers to TABC. The agency maintains a delinquency list of those retailers that do not pay on time, and distributors cannot deliver products to retailers who owe money.

TABC tested 1,300 products and approved 12,000 labels in FY 2003.

- TABC administers and enforces business practices regulations primarily through its Marketing Practices Division, with three staff. This Division approves alcoholic beverage labels, and conducts product testing. In fiscal year 2003, TABC tested approximately 1,300 products and approved more than 12,000 liquor, wine, and beer labels, collecting more than $300,000 in fees, primarily from wine labels. The Division also provides guidance to the industry on acceptable promotional practices, which are addressed in more detail in Issue 4 of this report.
- In addition, 37 of the Compliance Division's staff ensure manufacturers, distributors, and retailers comply with business practices regulations by enforcing credit payment requirements. Staff monitor compliance with credit laws when conducting excise tax audits. In fiscal year 2003, TABC conducted 112 on-site audits, representing about 20 percent of all Texas distributors.

The Legislature has shown an interest in reducing unnecessary regulatory burdens on business.

- The Legislature has directed agencies to review regulatory requirements that create unnecessary burdens and costs on private businesses. For example, the Sunset Act charges the Sunset Commission and its staff, when conducting agency reviews, to assess ways that an agency's regulation could be less burdensome for the agency and business, and still adequately protect the public.

Most other states place no restrictions on the size of beer containers sold.

Restricting the size of beer containers sold in Texas serves no clear consumer or state interest, and imposes unnecessary costs and limitations on the industry.

- Mandating the size of beer containers in state law does not clearly relate to any public health or safety concern. Texas law only allows beer to be sold if it is bottled in one of six bottle sizes or four keg sizes. However, 43 other states place no restrictions on the size of beer containers sold in their states. Of the six other states besides Texas that do specify beer container sizes in law, five states only set a minimum or maximum size, otherwise allowing a full range of sizes. In addition, Texas does not limit the size of liquor containers, and only sets a maximum limit of 4.9 gallons for wine containers. Sunset staff found no indications of any health or safety problems from not regulating this aspect of the industry.

- If a product does not meet Texas' container size restrictions, brewers can spend millions of dollars in additional costs to participate in the Texas market because the brewer must separately bottle product lines for Texas. The textbox, *Costs Associated with Texas' Regulation of Beer Containers*, shows examples of some of these costs to business.

- Texas' beer container size restrictions also function as a barrier to entering the market, potentially limiting consumers' choices of products in retail locations. For example, many foreign brewers use metric-sized containers that do not conform to Texas requirements. For example, Texas' restrictions eliminate common metric sizes such as 345 ml., or 11.65 ounces. While this container is very close to the permitted 12 ounce size, it cannot be marketed in Texas. As a result, consumers lack access to a range of products bottled in metric sizes from countries such as Canada, Holland, Belgium, New Zealand, and Japan, which can be purchased in almost all other states.

- In researching the reason for these restrictions, industry members indicated that regulating the size of beer containers provides distributors with some certainty regarding the number and size of different products they have to store and deliver to retailers. However, this does not seem to be a matter of state concern. In addition, distributors manage to store, for

Costs Associated with Texas' Regulation of Beer Containers[1]

Texas' restriction of beer container sizes can cost brewers millions of dollars in additional costs to produce containers to comply with Texas law. For example:

- One domestic brewer estimated that creating a separate product package for Texas cost the business almost \$600,000 annually.
- One foreign brewer estimated that producing a product in a Texas-specific container costs them an additional \$60,000 per year.
- A domestic producer of flavored malt beverages estimated additional costs of \$200,000 for producing container sizes specific to Texas.
- Another foreign brewer reported having to maintain an entire inventory of Texas-specific 15.5 gallon keg sizes because Texas does not allow its 13.2 gallon beer kegs, as other states do.

export to other states, beer labeled or packaged in a variety of container sizes, even though they cannot legally be sold in Texas.

When other states have repealed their container size restrictions, as occurred in Florida in 2001, many brewers and distributors initially opposed the change. However, they now indicate that the distribution network has adapted, and retailers can effectively meet consumer demands, and even increase sales. For example, one importer of Mexican beers reported sales increased by an average of 300,000 cases annually after introducing a container size in Florida that was previously prohibited.[2]

TABC's liquor and wine approval process duplicates federal processes, serves no clear public health purpose, and creates unnecessary delays in getting products to market.

Federal oversight ensures new liquor and wine products meet standards for public health and safety.

- In fiscal year 2003, TABC expended resources to examine and approve about 9,800 wine labels, more than 1,100 liquor labels, and conduct chemical analysis of approximately 1,300 new alcohol products. However, Sunset staff concluded that TABC's approval and testing processes for liquor and wine unnecessarily duplicates the federal Alcohol and Tobacco Tax and Trade Bureau's (TTB) alcohol approval and testing activities. The textbox, *Federal Tax and Trade Bureau Approval of New Alcoholic Beverages*, summarizes TTB's key regulations and activities related to approving new products for the market to protect public health and consumer interests.

Federal Tax and Trade Bureau Approval of New Alcoholic Beverages

The Tax and Trade Bureau (TTB) regulates alcoholic beverage manufacturers and importers to ensure that imported and domestically produced alcoholic beverages meet quality standards to protect public health and safety. This regulation includes the following activities.

Pre-approval of Alcoholic Beverages

In advance of gaining TTB approval to market a product, manufacturers must provide TTB with statements of product formula and production, which the agency uses to determine if the products contain any prohibited ingredients and are properly classified.

Chemical Analysis of Alcoholic Beverages

TTB may require manufacturers to submit a sample of some products, primarily certain liquors, to the agency to test for purity and alcohol content. In addition, TTB conducts inspections of domestic manufacturers and tests samples taken during inspections.

Certificate of Label Approval

After receiving pre-approval documentation, and conducting any needed testing, TTB reviews the product label. This review protects consumers by ensuring proper product representation. Upon approval, TTB issues a Certificate of Label Approval, which allows that product to be marketed in the United States.

Product Sampling and Investigations

TTB conducts random testing of alcoholic beverages after they go to market to ensure products are safe, and conducts investigations to ensure proper classification and representation of products to protect consumer interests.

- Only Texas and two other states, Virginia and Connecticut, conduct chemical analysis of all new alcoholic beverage products. In contrast, the vast majority of other states and the federal government find no need to test all products to ensure protection of public health and safety. While TABC conducts chemical analysis of all new liquor and wine products, these activities have not resulted in the agency denying products due to impurities that would threaten public health and safety. In the last fiscal year, TABC approved 96 percent of all liquor and wine tested, and did not deny approval of any products due to impurities, even approving a liquor with a whole scorpion in the bottle, which TTB also approved. Of the 4 percent of products denied, the majority were for the label's alcohol content not matching the tested content, with a small variance of only 2/10ths of one percent outside of the permissible alcohol content.

The vast majority of other states do not find a need to test new products like Texas does.

- The majority of other states also do not require any type of label approval for liquor and wine. Of the 22 states that do regulate labels, they only require registration of the federal certificate, which is less burdensome than conducting a second state-level approval. Although TTB requires all domestic and foreign manufacturers to submit their labels to TTB to ensure proper product representation, manufacturers must still submit a separate application to TABC with their federal Certificate of Label Approval, a sample label, and a container for each product size.

  Federal label approval takes approximately one month, and because manufacturers must submit the federal certificate with the Texas application, TABC's process only creates additional delays. While TABC's goal is to process these approvals in one week, in some cases it takes more than four weeks if a manufacturer must re-submit a revised label, or failed to provide every bottle size for the product.

  In addition, the Alcoholic Beverage Code does not specifically require TABC to approve wine labels, however the agency requires approval as a practice. In contrast, the Code specifically requires label approval for liquor. The current label approval process for wine creates unnecessary delays for wineries of two to three weeks in getting their products to market, since the most common reason for label denials is for the vintage year on the application not matching the label. However, TABC requires wineries to show the vintage year on the label based on a TABC rule, not a state or federal law.

Although not specified by law, TABC requires wineries to obtain approval of labels for each new vintage year.

Fixing the fee amount for TABC's approval of new alcoholic beverage products in statute reduces the agency's flexibility to adjust the fee to adapt to changing circumstances.

- TABC's statute requires manufacturers to submit a $25 fee with products sent to the agency for label approval and testing, generating more than $300,000 annually in revenues to cover the costs of these activities. The Legislature has established a practice in many programs of eliminating set or capped fee amounts in statute and allowing agencies to set fees by rule. This allows for greater administrative flexibility and is consistent with a provision in the General Appropriations Act that requires agencies to set fee amounts necessary to recover the cost of regulation. While TABC has the flexibility to adjust surcharges on its licensing fees, the agency lacks this flexibility to adjust the fee for approving alcoholic beverage products.

TABC's oversight of payments for alcoholic beverages between liquor and wine distributors and retailers is inefficient.

- TABC's administration of the credit law, which governs payments between liquor and wine distributors and retailers, is highly paper intensive. TABC maintains the delinquency list to track which retailers are behind in their payments. Distributors use this list to keep track of retailers to which they cannot sell or deliver products. TABC maintains a paper-based delinquency list, as well as an on-line list available on the agency's Web site.

  TABC sends the list twice per month to almost 900 distributors, or more than 200,000 lists annually. Out of these distributors, only 51 receive it by e-mail, with the remaining distributors still getting paper-based lists in the mail. In addition, TABC processes about 80,000 documents a year related to maintaining the list, including 50,000 delinquency notices sent by distributors and 30,000 release letters sent to retailers. Statutory requirements for distributors to report delinquent retailers in writing to TABC also contribute to this administrative burden for the agency.

Currently only 51 out of 900 distributors take advantage of e-mail to receive notice of delinquent retailers.

- Some retailers may be unfairly penalized and prevented from accepting deliveries even though they have paid their debt because the paper-based list is almost always out of date compared to the Web-based list. While TABC places a later effective date on the paper-based list to allow for delays in printing and mailing, it is still out of date compared to the Web-based list that staff update on an hourly basis.

Recommendations

Change in Statute

3.1 Eliminate restrictions on the size of beer containers that can legally be sold in Texas.

This recommendation would eliminate the requirements that beer only be sold in specific container sizes. The State would instead allow the sale of beer in any container size. This change would allow the industry to decide which beers to sell in Texas based on consumer preference, without having to consider if the container size meets state requirements.

3.2 Eliminate label approval and testing for liquor and wine, and instead authorize TABC to register federal certificates of approval for these products.

This recommendation would authorize the agency to implement a label registration program to accept federal Certificates of Label Approval for liquor and wine. This recommendation would eliminate statutory requirements for state approval of liquor labels, and clearly authorize TABC to implement a process to accept federal approvals for liquor and wine instead. TABC should clarify in rules that wineries would not re-submit labels for approval each time the vintage changes. In addition, this recommendation would eliminate the state requirement for chemical analysis of liquor and wine under 7 percent alcohol by volume, which would no longer be required when accepting federal product approvals. This recommendation would not change TABCs current label approval and testing requirements for beer. While all beer sold in Texas must be federally approved, the State's current approval process is needed because Texas has additional requirements for beers to qualify to be sold in Texas.

3.3 Eliminate fees set in statute for the approval of new alcoholic beverage products.

This recommendation would remove the $25 dollar fee set in statute for the approval of liquor and wine, and add language that the fee should be set to cover the costs of regulation, including implementing a label registration program. This recommendation would also eliminate the fee set in statute for the testing and approval of beer, and the agency would also set this fee to cover the cost of these activities.

3.4 Allow distributors to report retailers who are delinquent in making payments for liquor and wine by electronic mail or other means authorized by the agency.

This recommendation would modify requirements for liquor and wine distributors to report in writing delinquent retailers who have not paid within two days of the maximum 25 days allowed for credit, and allow for alternative means, such as e-mail or fax, for providing this information to the agency.

Management Action

3.5 TABC should work toward phasing out the paper-based delinquency list.

The Commission should move toward reducing the use, and mailing, of the paper-based delinquency list used for administration of credit law. The agency currently provides the list to a few distributors by e-mail, and the agency should try to expand these efforts. Under this recommendation, after March 2006, distributors would receive the list by e-mail, or access the current list maintained on the agency's Web site to ensure that they do not make deliveries to delinquent retailers. After this date, the agency should provide the paper-based list only on a distributor's request, and charge a fee to recover the costs of providing the list by mail. Distributors could also obtain this information by calling TABC.

Impact

Overall, these recommendations would improve TABC's ability to effectively regulate business practices by eliminating regulations that are duplicative or not clearly tied to public safety or consumer interests. Removing restrictions on the size of beer containers would result in savings to business because they would not have to produce products sized only for the Texas market, possibly providing consumers with more choices. Allowing the agency to accept federal certificates of approval for liquor and wine would reduce delays to business in getting products to market. Eliminating statutory caps on fees for product approval would give the agency the flexibility to set fees at the level necessary to recover liquor and wine registration, and beer testing program costs as conditions change. Reducing the use of the paper-based delinquency list, and allowing other means for reporting delinquent retailers, would allow the agency to more efficiently administer the credit law and eliminate potential unfairness to the industry resulting from the out-of-date paper-based list.

Fiscal Implication

These recommendations will not result in a significant fiscal impact to the State. Removing container size restrictions could increase fee revenue tied to the approval of new beer products for sale in Texas, with a corresponding cost associated with the approval of new containers. However, this increase could not be estimated as it would depend on how the market responds to this change. Removing the need to approve wine labels for each new vintage year could reduce fee revenue, and the agency would need to adjust the fee levels to ensure that its costs are fully covered. In addition, the agency could realize a small savings from phasing out the paper-based delinquency list, which costs the agency approximately $12,000 per year to produce and mail.

[1] Information provided by industry members to Sunset staff.

[2] Ibid.

Issue 4

TABC Lacks an Effective Approach for Resolving Key Marketing Practices Regulatory Issues, Resulting in Inconsistent Enforcement and Unnecessary Costs to the Industry.

Summary

Key Recommendation

- Require TABC to develop a formal process for making policy decisions regarding marketing practices regulations, and for communicating these decisions to agency staff and the industry.

Key Findings

- The agency faces difficulties in consistently and reliably interpreting regulations governing the promotion and marketing of alcoholic beverages.
- TABC lacks an effective means for deciding and communicating interpretations of law, or changes in policy, regarding restrictions on the marketing of alcohol.
- TABC's inconsistent approach to addressing marketing practices issues results in regulatory problems going unresolved for many years.
- The agency's lack of consistency in providing the industry with regulatory guidance results in unnecessary costs to the industry and unfair enforcement.

Conclusion

Sunset examined a range of regulations that TABC enforces regarding the marketing and promotion of alcoholic beverages, and found that TABC struggles to formulate, and communicate to the industry, important regulatory policies. Sunset staff's recommendation would improve TABC's decisionmaking processes for interpreting these regulations and improve the agency's ability to more consistently enforce these laws. In addition, this recommendation would provide the industry with better quality information on regulatory policies to assist with compliance, and provide more regulatory certainty for the industry.

Support

TABC regulates the marketing practices of the alcoholic beverage industry to protect consumers and prevent undue influence of manufacturers and distributors over retailers.

State law strictly limits inducements that manufacturers and distributors can give retailers.

- TABC's statute directs the agency to protect consumers from misrepresented products or deceptive advertising, and ensure against marketing that might encourage excessive consumption. The law also requires the agency to regulate and enforce certain industry marketing practices to prevent manufacturers and distributors from monopolizing retail sales.
- TABC administers and enforces these regulations through its Marketing Practices Division, with approximately three staff located at Headquarters. This Division monitors the alcoholic beverage marketplace, providing industry members technical assistance and guidance on regulations governing the marketing and promotion of alcoholic beverages, and approves the representation and packaging of alcoholic beverages. Staff also enforce restrictions on inducements manufacturers and distributors can provide to retailers, including:
  - limitations on the value of consumer novelties, promotional materials, and goods or services, and
  - limitations on marketing activities including advertising, sweepstakes, promotional events, and beverage sampling.

  In addition, 37 of the Compliance Division's staff ensure manufacturers, distributors, and retailers comply with marketing practices regulations by auditing financial records, inspecting licensed premises, investigating promotional events, and issuing administrative violations if necessary.

The agency faces difficulties in consistently and reliably interpreting regulations governing the promotion and marketing of alcoholic beverages.

Laws governing the marketing of liquor, beer, and wine vary significantly.

- To accomplish fair regulation, TABC must be able to provide consistent and reliable interpretations of state law to agency staff who enforce these laws, and to industry members who must comply. However, TABC staff often have difficulty interpreting marketing practices laws because they vary according to the type of alcohol - liquor, beer, and wine - and because the degree to which these laws apply to new technologies and marketing innovations is not always clear. The chart, *Statutory Restrictions on Marketing Practices that Require TABC Interpretation*, summarizes key regulations that are difficult for TABC to interpret and consistently enforce.

Statutory Restrictions on Marketing Practices that Require TABC Interpretation

Statutory Restriction	Interpretation by TABC
Providing Inducements to Retailers Industry members may not provide any equipment, money, service, or other things of value to retailers. However, industry members may provide courtesy inducements to retailers such as food, beverages, and entertainment valued at up to $500 per person, per event, as long as the industry members providing the benefit are present.	TABC must decide if: • providing a particular item or service is a "thing of value" that would result in an unfair competitive advantage to one retailer over other retailers; • sponsoring an event would result in more people attending the event than without sponsorship, thus providing an unfair advantage to one retailer over other retailers; and • a new technology provided to retailers qualifies as "equipment" or serves a function similar to one already approved.
Conducting Promotional Events Promotional events must not be advertised in advance or encourage excessive consumption. Promotional events for liquor may be arranged in advance, however events involving beer may not.	TABC must decide if: • a promotional event encourages "excessive consumption," or for beer to what extent an event was "pre-arranged" between the distributor and retailer.
Providing Novelties or Advertising Items For liquor, consumer novelty items of limited value may be provided to customers. For beer, these items must be worth less than one dollar. For liquor, industry members may provide advertising items worth up to $101 per brand, location, and year.* For beer, these items have no limit on the dollar value.	TABC must decide if: • novelty items provided by liquor manufacturers or distributors are of "limited" value, and that beer items actually cost less than one dollar to produce; and • for liquor, if advertising items provided to retailers are actually worth less than $101,* and for beer if items were actually given to the retailer without influencing the retailer.
Advertising Content For beer, by law industry members may not produce any type of advertisement that disparages a competitor's product, deceives the consumer, or creates a misleading impression. For liquor and wine these restrictions are by rule, and are not statutory.	TABC must decide if: • the packaging, labeling, or promotion of a product is "deceptive" to a consumer or "disparaging" of a competitor's product.

* TABC statute sets the amount for advertising items for liquor at $78, however the agency has authority to increase this amount in rule by 6 percent annually, based on the consumer price index.

TABC lacks an effective means for deciding and communicating interpretations of law, or changes in policy, regarding restrictions on the marketing of alcohol.

- While the agency has made recent efforts to provide interpretations of law to the industry, TABC lacks a clear structure or process for making marketing practices interpretations and consistently communicating them to the industry and TABC staff. Currently, selected executive staff, and staff from the Marketing Practices, Enforcement, and Compliance Divisions, and the General Counsel make these decisions solely on a case-by-case basis, with little input from the regulated industry. In fiscal year 2002, the agency created an informal staff committee to discuss these regulatory issues and publish advisories to guide regional enforcement efforts. However, this committee failed to meet regularly, did not keep consistent documentation, and did not effectively communicate its decisions to industry members. As a result, the agency continues to have no consistent approach to providing both the industry and its staff with clear guidance on acceptable marketing practices.

Industry members have difficulty getting useful guidance from TABC on allowable marketing activities.

- In some instances, even when industry members contact TABC in advance to determine if a promotional event is legal, the agency is unable to provide a clear response. According to TABC letters sent to two distributors, dated November 2002, the agency stated "We are not prepared to say this promotion is unlawful...we will continue to review the statutes, and further reserve the right to ask you to discontinue the promotion if and when we deem necessary." While TABC should appropriately reserve the right to take any needed enforcement actions, these types of responses do not provide the industry with reasonable and reliable guidance to help ensure compliance with regulations.

TABC's inconsistent approach to addressing marketing practices issues results in regulatory problems going unresolved for many years.

- Because TABC does not have an adequate process for making these regulatory decisions, potential problems can escape staff's attention. As a result, these problems do not receive needed attention early on, creating larger future problems for the agency and the industry.

  For example, a long standing industry practice is for smaller companies to contract with larger brewers to produce and bottle their beer, known as contract brewing. However, for more than a year TABC has questioned the legality of this practice. During this time the agency attempted to apply to the contract brewing concern a different, but related, 1998 Attorney General's opinion prohibiting more than one manufacturer from using a single brewery. However, the agency has yet to clarify this contract brewing issue for the regulated community by seeking a new Attorney General's opinion, proposing a legislative change, or bringing an enforcement case. As a result, the industry continues to operate under regulatory uncertainty while the agency investigates bringing administrative cases against many brewers.

Significant regulatory concerns can remain unresolved at TABC for long periods of time.

In another example, TABC allowed a manufacturer to legally market different formulations of a flavored malt beverage as a "flavored beer" and a "cordial" for more than nine years. During this period, TABC repeatedly approved samples of both versions of the product. However, TABC recently informed the manufacture that the agency's approval was an "oversight" and the manufacturer would have to remove one of the products from the market on the basis that the labeling of the two similar products was "deceptive" to consumers.

The agency's lack of consistency in providing the industry with regulatory guidance results in unnecessary costs to the industry and unfair enforcement.

- TABC's lack of an effective decisionmaking structure also results in the agency being unable to ensure consistent regulation or fair enforcement, creating unnecessary costs for the industry. For example, TABC authorized the provision of certain equipment to improve the quality of draft beer, only to reverse its approval four months later based on a new interpretation of the law, costing a brewer $20,000 for equipment already provided to distributors that could not be used. Also, in many instances industry members have relied on oral approvals from TABC's Headquarters to carry out certain promotional activities. However, agency regional staff who were unaware of Headquarter's decisions at times reversed these decisions, and issued violations against industry members as a result.

Other Texas state agencies have formal processes for gathering input from regulated industries to ensure sound decisionmaking when interpreting the law or making policy changes.

- The Texas Commission on Environmental Quality seeks input from its numerous advisory committees and stakeholder groups on implementation of legislation, development of rules, and changes in policies and procedures. For example, several small business advisory committees, composed of regulated businesses, industry associations, and environmental consultants, advise the agency on proposed rules and policies, program operations, voluntary compliance efforts, and enforcement issues that affect small businesses.

  The Public Utility Commission also solicits input from the regulated community by appointing negotiating committees, composed of industry representatives, consumer groups, and other stakeholders. These committees serve as a resource for Commission decisionmaking by commenting on proposed rules and policies. As a result of these formal mechanisms for gathering input from the regulated community, these agencies are better able to ensure full deliberation of regulatory decisions, and the reliable dissemination of these decisions to regulated entities.

Other Texas agencies could serve as a model for improving TABC's communication with the industry.

Recommendation

Change in Statute

4.1 Require TABC to develop a formal process for making policy decisions regarding marketing practices regulations, and for communicating these decisions to agency staff and the industry.

This recommendation would require the agency to develop a process to improve both its overall decisionmaking processes for marketing practices regulatory issues, and how the agency communicates these decisions to its staff and to the regulated community. In implementing this recommendation, the agency should consider assembling an ad-hoc working group composed of equal representation from the manufacturer, distributor, and retail tiers of the industry for liquor, beer, and wine. On an as-needed basis, TABC staff could convene the group to discuss marketing practices regulatory issues and to provide input for the drafting of marketing practice policies.

As part of this recommendation, the agency should document its decisions by using a precedents manual, or drafting formal advisories, and making these documents available to regional staff, as well as to industry members, though the agency's Web site, electronic mail, and agency publications. In implementing this recommendation, TABC could look to the practices of other state agencies, such as the Texas Commission on Environmental Quality and the Public Utility Commission, for guidance on establishing advisory groups and communicating policy decisions to the industry.

Impact

This recommendation would improve TABC's ability to effectively regulate marketing practices by providing better information to the regulated community. Requiring the agency to consult with an industry working group on marketing practices issues, and making advisory opinions available to the industry and regional staff, will provide agency staff with clearer guidance on how to enforce state law and provide industry would greater regulatory certainty.

Fiscal Implication

This recommendation would not result in a fiscal impact to the State. The agency should implement this recommendation with existing resources.

Issue 5

TABC Lacks a Consistent and Formal Approach to Investigating and Resolving Complaints Against Its Employees.

Summary

Key Recommendations

- Require TABC to maintain an internal affairs function to ensure fair, effective, and impartial investigations of alleged misconduct by law enforcement officers and other employees.
- Require the agency to track and report complaint information to the Administrator and the Commission on a regular basis.

Key Findings

- Despite the importance of a well-defined internal affairs function, TABC's laws, rules, and policies do not provide adequate guidance regarding its handling of personnel complaints.
- TABC does not track, analyze, or report statistical information on complaints that could help the agency identify and correct problems.

Conclusion

As a law enforcement agency, TABC must ensure that its employees maintain high standards of conduct by quickly and impartially investigating any complaints that allege misconduct on the part of an employee. Although a standard for law enforcement entities, neither the Alcoholic Beverage Code nor the Commission's rules require the agency to have an internal affairs function to oversee the investigation of personnel complaints. In response to severe corruption problems among TABC employees in the late 1980's, the agency created an internal affairs function. However, having no statutory or other formal basis for existence, and no written policies and procedures, that function has come and gone over the years according to the management style of the agency's administrators. These recommendations seek to solidify TABC's recent efforts to establish an internal affairs function by creating a requirement for it in statute; and requiring the agency to adopt policies and procedures, which include best practices for the effective handling of personnel complaints.

Support

TABC investigates allegations of misconduct by its staff through its recently created Office of Professional Responsibility.

- Created in the late 1980's to combat widespread allegations of corruption among officers for exchanging favors with the regulated industry, TABC recently raised the profile of its internal affairs function and renamed it the Office of Professional Responsibility. Due to the law enforcement nature of its work and a high level of interaction with the public, TABC must maintain high standards of conduct and respond quickly and effectively to any complaints against its employees.

  The agency employs about 236 commissioned peace officers across Texas who carry weapons and can make arrests, search licensed premises without a warrant, file criminal and administrative cases and execute other police powers. In addition, more than 100 ports of entry staff handle about $3 million annually in cash from personal importation taxes on tobacco and alcohol collected at the Texas-Mexico border. Other TABC staff answer questions from licensees and conduct audits and inspections at licensed locations.

- The public, as well as TABC employees, may submit complaints over the Internet, through the mail, or through the agency's toll-free phone number. The table, *Personnel Complaints*, shows the type of complaints received and how they were resolved in the first six months of 2004 when the agency started compiling this information.

- The Office of Professional Responsibility (the Office) is composed of one employee who collects information on all personnel complaints and investigates, or assigns to the appropriate regional supervisor, complaints of a serious nature, including discharge of firearms, excessive force, or corruption. Lesser complaints, such as tardiness, are handled by the employee's immediate supervisor and reviewed by the Human Resources Department with notification to the Office before action is taken. Both the Office and Human Resources may investigate sexual harassment complaints and often conduct them jointly.

The agency began compiling personnel complaint information in 2004.

Personnel Complaints 2004, 1st and 2nd Quarters

Allegations	
Rudeness or unprofessional conduct	13
Conflict of interest	9
Harassment	8
Excessive force	6
Employment issues, such as abuse of sick leave and dual employment	4
Dispute of a citation	3
Theft	3
Unlawful search	3
Failure to file seizure report	2
Failure to investigate	2
Off-duty conduct	2
Other	6
Total	61
Disposition	
Closed due to insufficient information	22
Unfounded	21
Pending	10
Counseling	4
Suspension	2
Employee resigned	1
Reprimand	1
Total	61

Division directors determine the appropriate disciplinary action for all complaints of a more serious nature, while an employee's supervisor may resolve other complaints. Human Resources and the agency's General Counsel review all involuntary terminations before the agency notifies the employee. Employees may appeal all disciplinary decisions to the Administrator.

Despite the importance of a well-defined internal affairs function, TABC's laws, rules, and policies do not provide adequate guidance regarding its handling of personnel complaints.

Until recently, regional supervisors investigated and disposed of personnel complaints with little to no oversight from Headquarters.

- Given that half of TABC's workforce has authority over life and liberty issues, TABC must ensure that its staff maintain high standards of conduct and act in accordance with the agency's policies. Failure to do so could cost the agency its public trust and expose it to litigation. Despite this liability, neither state law nor rules require TABC to have a formalized process for investigating complaints or allegations of misconduct by its employees.

  Without such statutory or regulatory guidance, various administrators have chosen to use the internal affairs function differently over the years, according to their individual management style. Until the new Administrator implemented a policy in April 2004 requiring all complaints to be reported to the Office of Professional Responsibility, regional supervisors investigated and disposed of personnel complaints with little to no oversight from Headquarters.

  As a result, Headquarters was often not involved in how individual regions disciplined their employees. For example, according to agency files, in September 2000, the shooting of a minor by a TABC agent was resolved at the local level without involvement from Headquarters. Although not as serious, the agency also needs a formal process to deal with complaints against non-commissioned staff.

- Although the current Administrator has made it a priority to establish a centralized internal affairs function, the agency has yet to develop consistent and adequate policies and procedures to guide the complaint process. Currently, the employee manual contains a small section on personnel complaints, but it lacks information needed by employees, such as instructions for filing a complaint; clearly defined steps in the investigation process; types of disciplinary actions an employee could face; and the process for appealing disciplinary action.

  In addition, information provided in the employee manual is not entirely consistent with a memorandum recently sent to division directors on how to handle complaints. Sunset staff interviews with TABC employees revealed that staff have no clear understanding of the steps involved in handling personnel complaints. Because no clear, detailed, and readily available policies and procedures exist, employees may not be aware of their due process rights in the event they face a disciplinary action based on a complaint.

- TABC has no established standards for the type of disciplinary action appropriate for various types of employee misconduct. Without such standards, TABC cannot ensure any level of consistency among regions and divisions in taking disciplinary action, or informing employees about the potential consequences of their misconduct.

- TABC does not make standard forms easily available to facilitate its complaint process. TABC's standard complaint form is not available to the public on the agency's Web site. Instead, the public is invited to submit an email or contact the agency by mail or phone. Lack of a readily available personnel complaint form is likely to result in missing information early on in the process that can create unnecessary follow-up with the complainant.

  The agency also does not provide information to the public about what to expect once they have filed a complaint, such as what steps the agency will take to address the complaint and how long the process should take. Further, the agency has not developed any standard notification forms to keep complainants and respondents updated of a complaint's status. The agency also does not have a standard reporting form to ensure regional supervisors follow all steps in the investigation process and collect necessary information in a timely and consistent manner.

TABC does not track, analyze, or report statistical information on complaints that could help the agency identify and correct problems.

Analyzing complaint trends could help solve problems with policy, training, and supervision.

- The Office of Professional Responsibility recently started to report quarterly statistics to the Administrator on the type and number of allegations and their disposition. However, the Office does not provide useful long-term analysis on an annual basis that would show particular trends or problem areas over the years. In addition, the Office does not report information on complaints or its activities to the Commission. Lack of analysis of personnel complaints affects the Administrator's and the Commission's ability to effectively oversee the agency and identify potential problems with agency policy, training, or supervision. Lack of information on internal affairs activities, such as the number of investigations performed by the Office as opposed to field offices or Human Resources, and average complaint resolution time, hinder effective oversight by the Commission.

- Although the Office's Director updates the Administrator weekly on the status of complaints, the Director does not forward this information to the division directors who have responsibility over the employees involved in the complaints. Additionally, division directors and Human Resources do not currently benefit from updates on patterns of complaints that could show employees and units of employees that have had more than one complaint. This type of analysis could help the agency prevent further complaints before they occur and be used as an additional tool to oversee field offices.

Recommendations

Change in Statute

5.1 Require TABC to maintain an internal affairs function to ensure fair, effective, and impartial investigations of alleged misconduct by law enforcement officers and other employees.

This recommendation would establish TABC's internal affairs function in statute, with original jurisdiction over all personnel complaints. The internal affairs staff would coordinate and be the central reporting point for, but need not conduct, all employee investigations. The staff may initiate complaint investigations independently, but would require the approval of the Administrator to investigate an employee if no complaint had been made. The Commission, by rule, should outline general guidelines to inform the public of how to file a complaint and what steps the agency will take to address that complaint. The Administrator should appoint and directly oversee the head of internal affairs.

5.2 Require the agency to track and report complaint information to the Administrator and the Commission on a regular basis.

This recommendation would require the internal affairs staff to report at least monthly to the Administrator information about the nature and status of each complaint. It would also require the staff to report to the Commission quarterly a summary of information relating to investigations, including analysis of the number, type, and outcome of investigations, trend information, and recommendations to avoid future complaints.

Management Action

5.3 TABC should develop policies and procedures to guide its internal affairs process.

This recommendation would direct TABC to develop policies and procedures governing its internal affairs process that follow guidelines laid out by the Commission. The procedures should include information on each step of the process with timeframes from receipt of complaints, investigation, disciplinary action, and appeal. In addition, the agency would need to develop a schedule of sanctions to guide supervisors in more consistently disciplining employees according to the type and severity of the misconduct. TABC should publish all of this information in its employee handbook so it is available to the entire staff. TABC would also need to develop standard reporting forms as appropriate to guide its internal affairs process, including a standard letter to complainants and respondents, and a standard reporting form that ensures complaint investigators go through each step of the process outlined in the employee manual in a timely manner. The agency should also make its personnel complaint form available on its Web site and in its employee manual.

As part of this recommendation, the agency should establish an early warning system to keep division directors informed about personnel complaints in writing. The internal affairs staff should analyze complaints at least annually to identify individual employees or units that have multiple complaints filed against them. Based on this information, the supervisor should work with executive management to design a plan for corrective action, such as specialized training, to address the problems. Additionally, the internal affairs staff should update division directors on the status of complaints affecting their employees in writing at least monthly to keep them informed and to ensure investigations are conducted in a timely manner.

Impact

These recommendations would ensure that, as a law enforcement agency, TABC has an appropriate structure in place and follows standard procedures for complaint investigations to ensure that the agency fairly and effectively addresses any valid concerns raised. The recommendations would also ensure that the internal affairs staff is able to perform its work with an appropriate degree of independence while reporting necessary information to the Commission, the Administrator, division directors and other appropriate personnel that can be used to help facilitate good management and policy decisions. Overall, these changes would result in a more consistent handling of complaints against agency employees within and across administrations, and would help ensure due process for employees who have complaints filed against them.

Fiscal Implication

These recommendations would not have a fiscal impact to the State. They would require the agency to devote additional resources to establish internal affairs policies and procedures, including the potential need for a computerized tracking system, but this could be achieved with existing resources.

Issue 6

Texas Has a Continuing Need for the Texas Alcoholic Beverage Commission.

Summary

Key Recommendation

- Continue the Texas Alcoholic Beverage Commission for 12 years.

Key Findings

- Texas has a clear and continuing interest in regulating the alcoholic beverage industry.
- TABC is the most appropriate agency to regulate the alcoholic beverage industry.
- The Legislature needs to make significant improvements to the Alcoholic Beverage Code and to the agency's operations.
- While organizational structures vary, all states regulate the production, distribution, and sale of alcoholic beverages.

Conclusion

The Texas Alcoholic Beverage Commission's responsibilities - regulating the production, distribution, and sale of alcoholic beverages, enforcing state laws regarding alcohol, and collecting taxes - are important to the State. The Sunset review evaluated the continuing need for a single, independent agency to perform these functions. Sunset staff assessed whether the agency's responsibilities could be successfully transferred to other agencies, and looked at how other states regulate the alcoholic beverage industry. Sunset staff found that while other state agencies could perform TABC's current functions, the benefits of transferring the functions are not sufficient to justify significant change. While other recommendations in this report identify needed improvements to the agency's operations, the Legislature should continue TABC.

Support

The Texas Alcoholic Beverage Commission's mission is to regulate every aspect of the alcoholic beverage industry.

- The Legislature created the Texas Liquor Control Board in 1935, two years after the repeal of Prohibition. In 1970, the Legislature changed the name of the agency to the Texas Alcoholic Beverage Commission, but its functions have stayed essentially the same over the years. The agency's mission is to supervise and regulate all phases of the alcoholic beverage industry to ensure the protection of the welfare, health, peace, temperance, and safety of the people of Texas. The agency also works to facilitate fairness, balanced competition, and responsible behavior within the industry through voluntary compliance.

- To accomplish its mission, TABC licenses manufacturers, wholesalers, and sellers of alcoholic beverages; enforces the Alcoholic Beverage Code; collects taxes on alcoholic beverages; and provides educational programs to address issues such as underage drinking. A three-member, part-time Board oversees the agency, with its 565 employees and $30 million annual budget in fiscal year 2004. Licensing fees and surcharges cover the cost of the agency's budget.

Texas has a clear and continuing interest in regulating the alcoholic beverage industry.

- The Legislature originally created the agency to prevent corruption within the alcoholic beverage industry. After the repeal of Prohibition in 1935, each state created a regulatory structure that prohibited close ties between the three tiers of the industry - manufacturers, wholesalers, and retailers - as described in the textbox, *The Three Tiers*. No ties, familial or financial, can exist among the three tiers, to prevent "tied houses" where one tier unduly influences another and where corruption and organized crime can dominate the alcoholic beverage industry.

  This structure was intended to protect citizens from the unregulated, unaccountable, and anonymous sale of alcohol. Today, some federal guidelines exist for regulating the interactions among the three tiers of the industry, but for the most part, each state supervises and controls the industry according to its own laws. As such, TABC ensures the alcoholic beverage industry operates within the bounds of the state's alcohol laws.

> ***The Three Tiers***
>
> *Manufacturer*
>
> Upper tier. Licenced to produce and sell alcoholic beverages to wholesalers.
>
> *Wholesaler*
>
> Middle tier. Licensed to purchase alcoholic beverages from manufacturers and sell to retailers. Referred to as wholesalers for liquor and wine products, and as distributors for beer products.
>
> *Retailer*
>
> Lower tier. Licensed to sell alcohol to consumers. Includes package stores, grocery stores, convenience stores, restaurants, and bars.

- Even more important than maintaining the separation of the three tiers, Texas has a continuing interest in protecting the public from the illegal and irresponsible consumption of alcohol. Problems such as underage drinking, over consumption, and drinking and driving, continue to be important public safety issues for Texans. Since the Legislature raised the legal drinking age to 21 in 1986, TABC has focused a great deal of its enforcement effort on finding and preventing violations of this law.

The agency issues citations to minors in possession of alcohol and to adults who provide alcohol to minors; conducts sting operations of retailers to uncover businesses who are selling alcohol to minors; and provides educational programs to children, college students, parents, and others on the dangers of underage drinking.

TABC also plays a role in reducing the number of traffic accidents related to alcohol consumption through its educational programs for those who sell and serve alcohol, investigations of the sources of alcohol involved in fatal crashes, and other activities. The textbox, *Drinking and Driving in Texas*, illustrates the seriousness of this public safety issue.

> ***Drinking and Driving in Texas***
>
> *Fatalities*
>
> Forty-seven percent of all traffic fatalities in Texas in 2002 were attributed to alcohol use. This figure is down from 66 percent in 1982. Statewide, 1,745 traffic fatalities involved alcohol. Five counties - Bexar, Dallas, Harris, Tarrant, and Travis - each had 55 or more traffic fatalities involving alcohol.[1]
>
> *Injuries*
>
> Alcohol-related crashes caused 25,142 injuries in 2002.[2]
>
> *DUI*
>
> The number of people arrested for driving under the influence of alcohol or drugs in 2003 totaled 91,429. Of all DUI arrests, 10,674 or 12 percent, were persons under the legal age to purchase alcohol.[3]

- To ensure compliance with the Alcoholic Beverage Code, the agency performs many important functions. For example, through its licensing function, the agency ensures all members of the alcoholic beverage industry meet certain qualifications. The agency also performs traditional law enforcement activities such as inspections and complaint investigations, audits excise tax returns, and monitors the industry's marketing activities. Through these activities, the agency finds and takes action on administrative and criminal violations. The agency tries to prevent violations through its various educational programs.

  In fiscal year 2003, the agency issued or renewed more than 96,000 licenses, responded to more than 5,600 complaints, performed more than 111,000 inspections, found more than 33,000 administrative and criminal violations, collected $2.8 million in fines, collected nearly $166 million in taxes, and provided educational programs to more than 410,000 people.

- The alcoholic beverage industry is large and the laws regulating it are complex. TABC licenses approximately 36,500 restaurants, bars, grocery stores, and other retailers to sell alcohol in Texas. More than 1,700 businesses are licensed to manufacture and distribute alcohol in the state. The agency ensures that all of these licensees meet and maintain the numerous qualifications for licensure. For example, the agency must investigate whether an applicant has any financial ties whatsoever to another licensee. The alcoholic beverage industry is highly competitive and continually developing new and sophisticated ways of marketing its product. This constant change presents a challenge for TABC, which must monitor the industry to prevent and take enforcement action when necessary against illegal promotional activities.

TABC found more than 33,000 violations of alcohol laws and rules in FY 2003.

- As a result of legislation passed in 2003 easing requirements for communities to hold elections on the legalization of alcohol sales, numerous communities have either held local option elections or are in

In fiscal year 2004, 36 communities voted to legalize the sale of alcoholic beverages.

the process of collecting signatures to bring the issue to a vote. In fiscal year 2004, 36 communities voted to legalize the sale of alcoholic beverages. As of August 2004, 19 communities are scheduled to hold elections on the legalization of alcohol. Allowing alcohol sales in many new communities will result in a significant number of new retailers applying to TABC for licensure and requiring regulation by the agency.

TABC is the most appropriate agency to regulate the alcoholic beverage industry.

- Although other state and local agencies in Texas perform a variety of similar licensing, enforcement, and tax collections functions, TABC is unique in that all its efforts focus solely on the regulation of the alcoholic beverage industry, and it has specialized expertise in the state's complex alcoholic beverage laws. Sunset staff examined several organizational options for the regulation of the alcoholic beverage industry. While other agencies could perform these functions, Sunset staff did not find sufficient benefit to the State to warrant transfer of any or all of TABC's functions. The material below discusses these options.

- TABC performs a variety of traditional law enforcement functions that are similar to those performed by the Department of Public Safety (DPS) and local police and sheriff's departments. For example, both local and state police enforce criminal laws related to alcohol use, such as driving while intoxicated, public intoxication, and selling alcohol to a minor. In addition, on a statewide level, DPS conducts investigations to detect illegal activity, performs inspections to ensure compliance with the law, provides education programs on a variety of public safety issues, and manages a large volume of criminal history data and statistics, among other law enforcement activities.

  While DPS has a great deal of law enforcement tools at its disposal, it also has a number of current responsibilities. Staff was concerned that DPS would be pressed to focus significant attention on the enforcement of alcohol related laws or regulation of the alcoholic beverage industry, as does TABC. Further, local law enforcement agencies do not have the resources or statewide reach to effectively deter and detect violations of alcoholic beverage laws.

DPS would be pressed to focus significant attention on the enforcement of alcohol related laws.

- TABC's extensive licensing function could be performed by the Department of Licensing and Regulation (TDLR) or DPS. TDLR performs a variety of standard licensing functions through its regulation of 20 professions. The agency issues licenses, conducts inspections, investigates complaints, assesses penalties, and sets rules and standards, all similar to TABC's licensing functions. DPS also has experience in licensing. In addition to its driver licensing program, the Legislature gave DPS the responsibility of licensing private investigators and private security agents in 2003. These functions are similar to TABC's in that DPS must ensure applicants meet and maintain all licensing qualifications. DPS also has experience with the administrative hearings process used to revoke driver licenses, a process similar to that used by TABC to take administrative action against its licensees.

While TDLR or DPS could take over TABC's licensing functions, alcoholic beverage law places many more complex requirements on licensees than most standard occupational regulations. TABC has the expertise necessary to ensure these requirements are met before issuing licenses.

- While TABC collects several alcoholic beverage taxes, the Comptroller of Public Accounts collects the bulk of all state taxes, including other alcohol taxes. In addition to the sales tax, the Comptroller also collects the mixed beverage gross receipts tax from bars and restaurants that serve mixed drinks. The Comptroller has sophisticated systems in place to ensure businesses are paying the proper amount of taxes to the State, including automated payment processing, risk-based auditing, and wide-reaching collection authority.

  Although the Comptroller could perform TABC's current tax collection functions, no significant benefit would result from such a transfer. TABC is adequately performing these functions. Further, when TABC audits its tax payers, the agency has the opportunity to find other violations of the Alcoholic Beverage Code that may not have become apparent otherwise.

TABC tax audits give the agency an opportunity to find other violations.

The Legislature needs to make significant improvements to the Alcoholic Beverage Code and to the agency's operations.

- TABC effectively performs many functions. For example, as a result of the agency's sting operations, 80 percent of retailers comply with laws prohibiting the sale of alcohol to minors today versus 30 to 40 percent when the agency started the operations in the early 1990s. TABC also works closely with local law enforcement agencies and with colleges and universities to combat underage drinking. In addition, the agency is working diligently to automate its licensing and enforcement systems, with the intent of eliminating the vast amount of paper files held by the agency, making its information more accessible to agency staff, and streamlining the application and renewal process for licensees.

- Despite its successes, the agency has several significant problems that can be attributed to both the complexity of alcoholic beverage laws and to the agency's management over the years. These problems are addressed specifically in the other issues in this report. The overall goal of this report is to modernize the agency's regulation of the alcoholic beverage industry and to focus its resources more squarely on public safety issues involving the sale and consumption of alcoholic beverages. With the changes recommended in this report, the agency should be positioned to operate more effectively and efficiently over the next 12 years.

With the changes recommended in this report, TABC should be better positioned to operate over the next 12 years.

While organizational structures vary, all states regulate the production, distribution, and sale of alcoholic beverages.

- Among the states, a variety of organizational structures exist for regulating the alcoholic beverage industry. Eighteen states, known as "control states," control the distribution of alcohol by owning and operating the wholesale tier. Some of these states also choose to own and operate package stores in order to further control the sale of alcohol to consumers. The other 31 states, like Texas, license private companies to distribute and sell alcohol. How these states organize their enforcement, licensing, and tax collection functions varies greatly. Some states, like Texas, have independent agencies that are solely responsible for all aspects of alcoholic beverage regulation. In other states, these functions are administered by agencies responsible for public safety, revenue collection, or business and professional licensing.

Recommendation

Change in Statute

6.1 Continue the Texas Alcoholic Beverage Commission for 12 years.

Impact

This recommendation would continue TABC as an independent agency, responsible for regulating the alcoholic beverage industry.

Fiscal Implication

If the Legislature continues the current functions of the Texas Alcoholic Beverage Commission, using the existing organizational structure, the agency's annual appropriation of approximately $30 million would continue to be required for its operation. Licensing fees and surcharges the agency collects from the alcoholic beverage industry more than cover TABC's entire appropriation.

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[1] National Highway Traffic Safety Administration, *State Traffic Safety Information, Texas - Toll of Motor Vehicle Crashes, 2002*, www.nhtsa.dot.gov/STSI/. Accessed: October 8, 2004.

[2] Texas Department of Transportation, *Save a Life, Don't Drink & Drive*, www.TexasDWI.org. Accessed: October 8, 2004.

[3] Texas Department of Public Safety, *2003 Crime in Texas*, ch. 8, "2003 Texas Arrest Data" (Austin, Texas). Online. Available: www.txdps.state.tx.us/crimereports/citindex.htm. Accessed: October 8, 2004.

Across-the-Board Recommendations

Texas Alcoholic Beverage Commission	
Recommendations	**Across-the-Board Provisions**
Do Not Apply	1. Require public membership on the agency's policymaking body.
Update	2. Require provisions relating to conflicts of interest.
Update	3. Require unbiased appointments to the agency's policymaking body.
Update	4. Provide that the Governor designate the presiding officer of the policymaking body.
Update	5. Specify grounds for removal of a member of the policymaking body.
Apply	6. Require training for members of the policymaking body.
Apply	7. Require separation of policymaking and agency staff functions.
Already in Statute	8. Provide for public testimony at meetings of the policymaking body.
Modify	9. Require information to be maintained on complaints.
Apply	10. Require the agency to use technology to increase public access.
Apply	11. Develop and use appropriate alternative rulemaking and dispute resolution procedures.

Agency Information

Agency Information

Agency at a Glance

The Texas Alcoholic Beverage Commission (TABC) regulates all phases of the alcoholic beverage industry to ensure the protection of the welfare, health, peace, temperance, and safety of the people of Texas. The Legislature created the agency, originally called the Liquor Control Board, in 1935, in response to the repeal of Prohibition. Today, the agency endeavors to protect the people of Texas while facilitating fairness, balanced competition, and responsible behavior in the alcoholic beverage industry through voluntary compliance. To accomplish its mission, the Commission:

On the Internet: Information about the agency is available at www.tabc.state.tx.us.

- licenses alcoholic beverage manufacturers, wholesalers, and retailers;
- enforces administrative and criminal laws in the Alcoholic Beverage Code;
- collects taxes on alcoholic beverages; and
- provides educational programs to address issues such as underage drinking.

Key Findings

- **Funding.** The agency spent more than $25.2 million for its operations in fiscal year 2003 - all of which came from licensing fees and surcharges.
- **Staffing.** In fiscal year 2003, the agency had 515 employees, including 214 commissioned law enforcement officers. About a quarter of these employees are located at the Headquarters in Austin, and the rest work in the agency's many field offices around the state and ports of entry along the Mexico border.
- **Licensing.** The agency issued or renewed more than 96,000 licenses in fiscal year 2003, including more than 65,600 retailer, 860 wholesaler, and 1,600 manufacturer licenses. Some businesses require more than one license to operate, and so the agency actually licensed approximately 38,700 locations that year.
- **Enforcement.** In fiscal year 2003, the agency resolved 16,483 administrative violations from all divisions and issued citations for 17,389 criminal violations. As a result, the agency collected $2.8 million in fines, temporarily suspended licenses for 3,326 violations, and cancelled licenses for 201 violations, among other enforcement actions. The agency also received 5,719 complaints and resolved 5,689.
- **Tax Collection.** In fiscal year 2003, TABC collected nearly $166 million in excise, personal importation, airline and passenger train taxes, and associated fees on alcoholic beverages.

- **Education.** The agency presented its educational programs to more than 410,000 people in fiscal year 2003, including school children, college students, local law enforcement personnel, civic and community group members and licensed businesses. In that same year, the agency received $422,000 in federal grants for educational programs, most of which it passed through to local law enforcement, advocacy, and university groups.

Major Events in Agency History

1836 The Republic of Texas imposed the first taxes on distilled spirits and malt beverages.

1920 Prohibition began following the ratification of the 18th Amendment to the U.S. Constitution.

1933 Prohibition ended following the ratification of the 21st Amendment to the U.S. Constitution, allowing individual states to regulate alcoholic beverages.

1935 The Legislature created the Texas Liquor Control Board to regulate all phases of the alcoholic beverage industry. Individual communities were authorized to hold local option elections to determine what kind of alcohol, if any, could be sold in their areas.

1970 The Legislature changed the name of the agency to the Texas Alcoholic Beverage Commission.

1971 The Legislature created a mixed beverage permit to allow the sale of liquor by the drink.

1986 In response to possible federal highway fund sanctions, the Legislature raised the legal age limit for alcoholic beverage consumption to 21. In pursuing years, the agency developed several enforcement and educational programs to deter and detect violations involving underage drinking.

1994 Following TABC's Sunset review, the Legislature transferred two TABC functions to other agencies. Collection of the mixed beverage gross receipts tax was transferred to the Comptroller of Public Accounts and bingo regulation, which TABC had administered since 1990, moved to the Texas Lottery Commission.

Organization

Policy Body

Texas Alcoholic Beverage Commission Policy Body

Member	Residence	Term Expiration
John T. Steen, Chair	San Antonio	2007
Gail Madden	Dallas	2005
Vacant Position		

The Commission is composed of three members appointed by the Governor with advice and consent of the Senate to serve staggered six-year terms. The chart, *Texas Alcoholic Beverage Commission Policy Body*, contains information on current members. As of September 2004, one position was vacant.

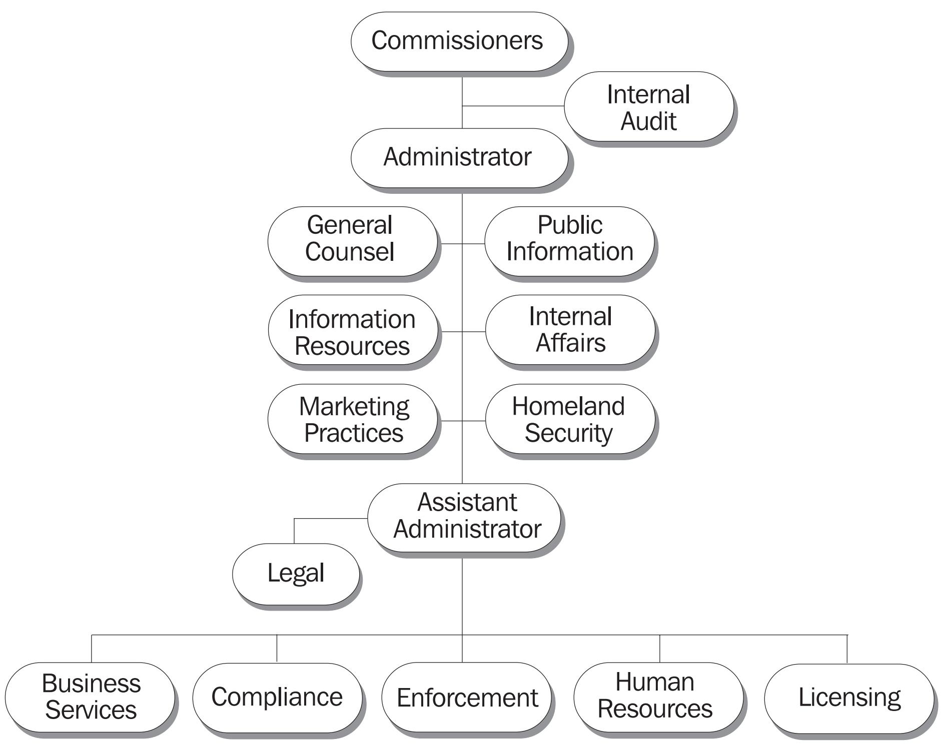
To be appointed to the Commission, an individual must have been a Texas resident for at least five consecutive years immediately before appointment and have no ties to the alcoholic beverage industry.

The Commission sets policies and adopts rules to carry out the provisions of the Alcoholic Beverage Code. The Commission also selects the agency's Administrator and Internal Auditor and approves the strategic plan and legislative appropriations request. The Commission has delegated to the Administrator its jurisdiction to grant, refuse, suspend, and cancel licenses and permits. The Commission generally meets once a month in Austin.

Staff

The Administrator manages the day-to-day activities of the agency, with the help of an Assistant Administrator. The agency is organized into three main divisions - Licensing, Enforcement, and Compliance - with several other divisions providing support services. The chart, *Texas Alcoholic Beverage Commission Organizational Chart*, depicts the agency's organization.

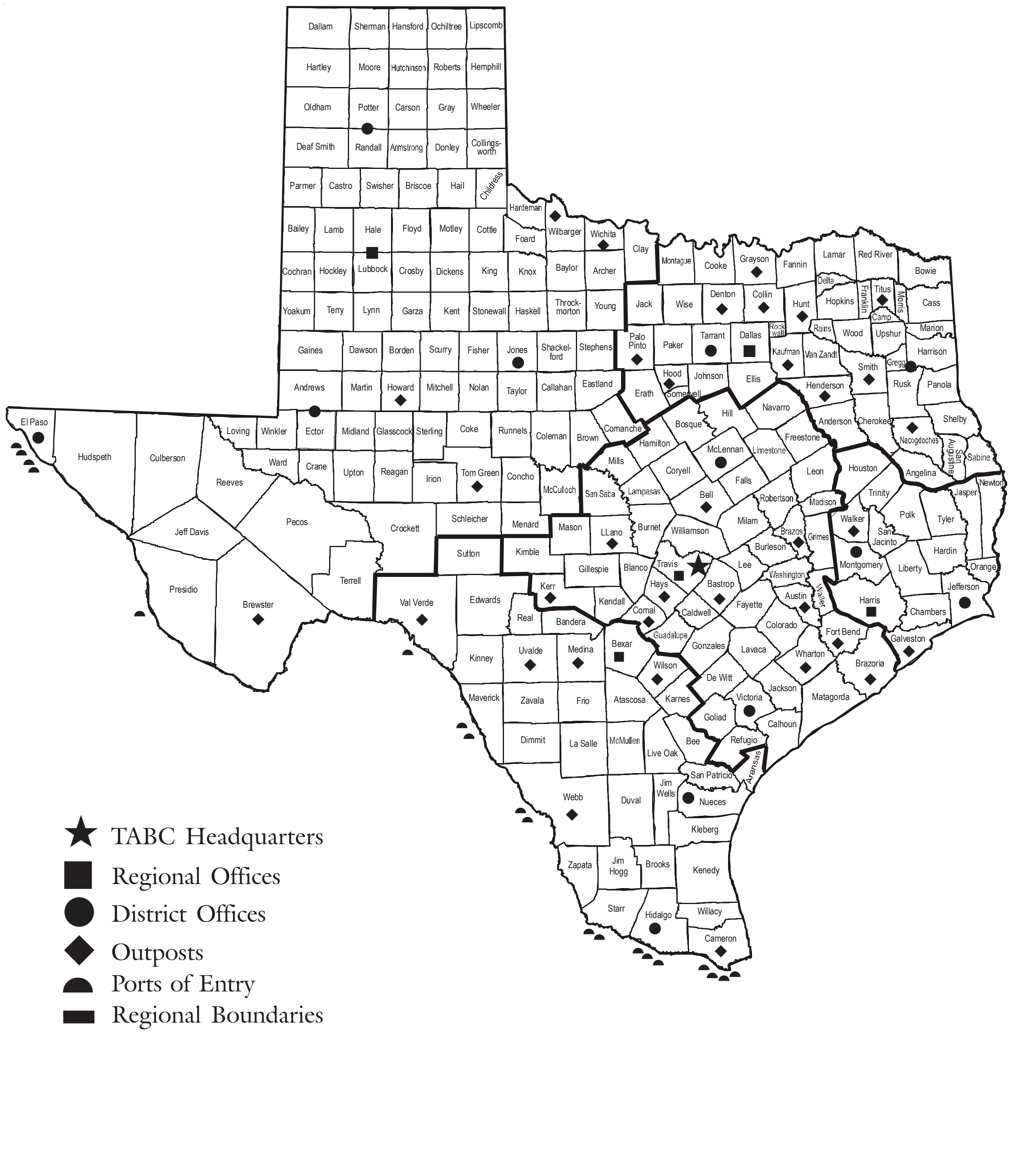
Texas Alcoholic Beverage Commission Organizational Chart



Most of the agency's employees work in the agency's 52 field offices.

In fiscal year 2003, the agency had 515 employees. About a quarter of these employees are located at the Headquarters in Austin. The rest work in the agency's 52 field offices. The agency has divided the state into five enforcement regions, with a main regional office in each. The regional offices oversee smaller district offices as well as several outposts, some of which house only one employee. The agency also has staff at 19 ports of entry located along the Mexico border. The map, *Office Locations*, shows the location of these offices.

Texas Alcoholic Beverage Commission Office Locations



Most of the agency's personnel in its field offices are commissioned law enforcement officers. Other field personnel include compliance auditors, tax collectors at the ports of entry, and administrative support staff. In addition to their enforcement and auditing duties, many field personnel also perform licensing functions for the agency. Specifically, they help applicants fill out the proper paperwork and inspect new locations to ensure they meet licensing requirements.

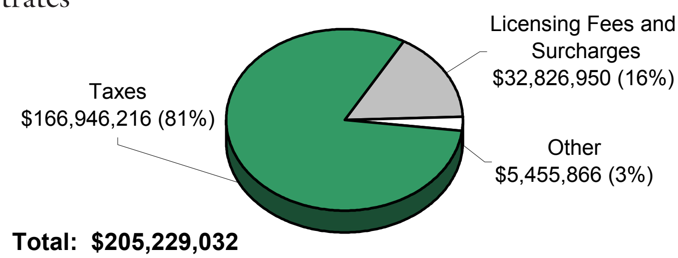
A comparison of the agency's workforce composition to the minority civilian labor force over the past four years is shown in Appendix B, *Equal Employment Opportunity Statistics*. TABC met or exceeded the statewide civilian labor force percentages for most job categories, but fell short in a few categories.

Funding

Revenues

In fiscal year 2003, the Alcoholic Beverage Commission collected more than $205 million in revenue from its regulation of the alcoholic beverage industry. This revenue came from licensing fees and surcharges, taxes, penalties, and various other fees, all of which was deposited in the General Revenue Fund. The chart, *Revenue Collected by TABC*, illustrates how much money in each category the agency collected for the State in fiscal year 2003. The "Taxes" category in the chart represents excise taxes collected from wholesalers and from individuals bringing alcoholic beverages across the Mexico border, cigarette taxes collected on behalf of the Comptroller of Public Accounts, and other taxes and associated fees collected by the agency. The "Other" category represents fines, administrative fees for various agency functions, the sale of confiscated liquor, and other miscellaneous revenue collected by the agency.

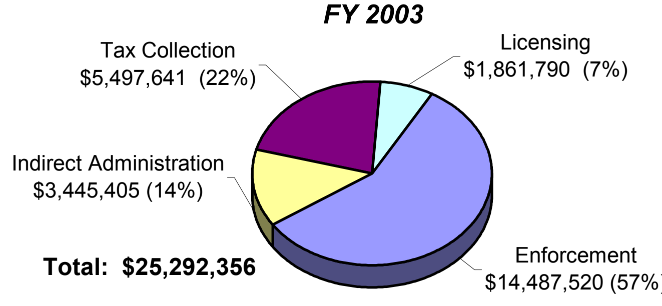
Revenue Collected by TABC
FY 2003



Expenditures

In fiscal year 2003, the Commission spent more than $25.2 million in four main areas: enforcement, licensing, tax collection, and administration. The chart, *Expenditures by Strategy*, provides a break down of the agency's expenditures in the previous fiscal year. The largest portion of the agency's budget went toward its enforcement function, which includes traditional law enforcement activities and several educational programs.

Expenditures by Strategy
FY 2003



Appendix C describes the Commission's use of Historically Underutilized Businesses (HUBs) in purchasing goods and services for fiscal years 2000 to 2003. In fiscal year 2003, TABC exceeded the statewide goals for building construction and special trade, but fell short of the goals for professional services, other services, and commodities.

Agency Operations

After the repeal of Prohibition in 1935, the Legislature created, as did all other states, a regulatory structure that prohibited close ties between alcoholic beverage manufacturers and retailers. The states required a wholesale buffer between the manufacturer and retailer, in effect creating three regulatory tiers. Known as the three-tier system, this structure was intended to protect citizens from the unregulated, unaccountable, and anonymous sale of alcohol. No ties, familial or financial, could exist between manufacturers and retailers to prevent "tied houses" where one tier unduly influences another and where corruption and organized crime dominate the alcoholic beverage industry. The textbox, *The Three Tiers*, describes the functions of each tier.

The three-tier system of regulation began after the repeal of Prohibition.

The Three Tiers

Manufacturer	Upper tier. Licenced to produce and sell alcoholic beverages to wholesalers.
Wholesaler	Middle tier. Licensed to purchase alcoholic beverages from manufacturers and sell to retailers. Referred to as wholesalers for liquor and wine products, and as distributors for beer products.
Retailer	Lower tier. Licensed to sell alcohol to consumers. Includes package stores, grocery stores, convenience stores, restaurants, and bars.

Local government also plays an important role in how alcohol is sold in all areas of the state and whether it can be sold at all. The textbox, *The Role of Local Government*, describes local option elections

The regulatory structure that the Texas Alcoholic Beverage Commission oversees today continues to operate under the same three-tier system established at the end of Prohibition. The agency licenses businesses in each tier and enforces alcoholic beverage laws. The agency also collects alcoholic beverage taxes and administers educational programs to help prevent violations of the law, including the sale of alcohol to minors and intoxicated persons.

The Role of Local Government

The Texas Constitution permits areas of the state to hold local option elections designating what types of alcohol, if any, can be sold and how it can be sold. A city, county, or justice of the peace precinct can vote to be completely dry or to allow alcohol to be sold under a variety of circumstances, ranging from only allowing beer and wine in restaurants to allowing package stores. Even in areas that are completely dry, an organization, such as a country club or fraternal organization, may apply for a private club license to serve alcohol to its members.

TABC relies on localities to maintain the information on what areas are wet or dry. With 254 counties, nearly 850 precincts, and numerous cities, the lines between wet and dry areas can be difficult to track. Also, the boundaries of a locality can change, as with census shifts and incorporations, but the wet or dry status remains within the original voting boundaries, further complicating wet and dry tracking. Currently, approximately 89 percent of Texas counties are at least partially dry.

Licensing

Following the three-tier structure, the agency licenses manufacturers, wholesalers, and retailers of alcoholic beverages. Licensing ensures that only qualified businesses are allowed to produce, distribute, or sell alcohol in Texas. In addition, licensing qualifications ensure separation between the three tiers by prohibiting a licensee in one tier from having any financial ties to a licensee in another tier.

General License Types

Primary License	The main license to sell or produce alcoholic beverages. Examples include an on-premise mixed beverage permit for a bar or restaurant, or an off-premise beer license for a grocery or convenience store that only sells beer.
Subordinate License	Licenses that allow a primary license holder to engage in another activity related to their business, such as a package store that provides wine tastings or a bar that wishes to stay open past midnight, in accordance with local ordinances.

The agency issues 64 different kinds of licenses and some businesses require more than one license to operate. These 64 licenses fall into two general categories, as described in the chart, *General License Types*. In fiscal year 2003, the agency issued or renewed more than 96,000 licenses, which represents approximately 38,700 licensed locations. The table, *Number of Licenses and Licensed Locations*, shows the number of licenses in each tier in fiscal year 2003. In addition to businesses, the agency licenses individuals, known as agents, who work for wholesalers and manufacturers. The "Other" category in the table includes licenses for hotel minibars and airplane alcohol sales, among others. The agency also issues temporary licenses to allow alcohol sales at special events, such as the State Fair.

Number of Licenses and Licensed Locations – FY 2003

Type	Number of Licenses	Number of Licensed Locations
Manufacturers	1,623	1,490
Manufacturer Agents	613	
Wholesalers	868	262
Wholesaler Agents	21,981	
Retailers	65,687	36,500
Temporary Licenses	4,878	
Other	524	516
Total	**96,174**	**38,768**

The process for obtaining each type of license shares some similarities across tiers, such as criminal and financial background checks, and all licensees are subject to local ordinances and protests by the public. However, each tier has some application differences, for example, the types of bonds needed and licensing fees vary greatly. In addition, the process for obtaining a beer, wine, or liquor license varies as well. The complexity of obtaining a license, and the associated fees, generally increase with the percentage of alcohol in the beverage sold. Less than $300 will cover licensing fees to sell beer in a bar or restaurant, whereas the same location would have to pay an additional $3,000 to sell mixed drinks. The fees for licensure also tend to be higher for locations where customers consume alcohol on-premise.

An applicant begins the process of obtaining a license with the local TABC office. Staff interview applicants, instructing them on how to get and maintain a license, provide applicants with all necessary signs to be posted in their business, perform background checks and any other investigations that the enforcement agents deem necessary, and review applications for completeness. For a new license, the process takes approximately two

Licensing Requirements

Depending on the type of license needed, an applicant must meet the following requirements.

Notify the public through:

- 60 day posting at the location or in two issues of the newspaper, and
- written notice to residences within 300 feet.

Receive local authorization through:

- certification from city secretary,
- certification from county clerk, and
- hearing or waiver by county judge.

Pay fees to:

- TABC, and
- the county tax assessor collector.

Secure bonds to ensure:

- future compliance with the law, and
- future payment of taxes.

Provide detailed information regarding the personal history and financial holdings of each owner, partner, corporate officer, majority stockholder, and manager. The agency also conducts criminal history background checks.

Submit to an inspection of the location to be licensed.

months from the filing of an application to receipt of a license. The textbox, *Licensing Requirements*, lists various requirements an applicant may have to fulfill, depending on the type of license. Once an application is complete, local TABC staff forward it to Austin for final processing and issuance of the license.

All licenses must be renewed each year. The agency automatically renews a license if the licensee has not experienced location, ownership, or management changes, is up-to-date on taxes, remains free of criminal convictions and local protests, and pays all necessary renewal fees.

Retailer Licenses

Because retailers sell alcoholic beverages directly to consumers, a retail license is the most complex to obtain and requires the most number of steps of all TABC licenses. In fiscal year 2003, TABC licensed approximately 36,500 retail locations. Retailers fall into two main categories: on-premise locations such as bars and restaurants, and off-premise locations such as grocery and convenience stores. Private clubs are also in the retail tier. These clubs operate in dry areas and are only allowed to serve alcohol to their members. The greatest amount of turn over occurs in the retail tier, with the average licensee staying in business for only two years. The textbox, *Two Retail Licensing Scenarios*, shows examples of what licenses a retail applicant may need and the cost in fees and surcharges required to go into business.

Two Retail Licensing Scenarios

Liquor Store: Off-Premise License

A retail store planning to sell beer, wine, and liquor for off-premise consumption would need one license for beer and another for liquor and wine. If the store wants to sell to other retail establishments, such as private clubs, they would need a local distributor's permit. If the store has another retail location, the owner would need a cartage license to transport products between locations. To offer product tastings would require another license.

Licensing fees: $1,223

Brewpub Restaurant: On-Premise License

A brewpub restaurant planning to sell beer, wine, and mixed drinks for on-premise consumption would need one license for beer, wine, and mixed drinks, a subordinate license to brew his product on-premises, and another subordinate license to stay open until 2 a.m. if local ordinances allow.

Licensing fees: $4,014

Wholesaler and Manufacturer Licenses

TABC licenses businesses that produce and distribute alcohol to ensure they have no ties to other sectors of the alcoholic beverage industry, most importantly retailers. TABC also ensures that licensed manufacturers and wholesalers comply with laws on properly marketing and advertising their products in Texas. In fiscal year 2003, TABC licensed 262 wholesalers and 1,490 manufacturers. In addition to the licensure of these businesses, TABC licenses certain individual agents who represent licensed wholesalers and manufacturers and work directly with retailers to sell their products. In fiscal year 2003, the agency licensed nearly 22,600 agents.

Enforcement

TABC enforces both administrative and criminal laws contained in the Texas Alcoholic Beverage Code, primarily through the work of its 237 law enforcement agents located throughout the state. The textbox, *Law Enforcement Activities*, provides examples of the activities TABC agents perform in enforcing the law.

Law Enforcement Activities

- Investigating complaints submitted by the public, licensees, local officials, and others.
- Monitoring bars and clubs for sales of alcohol to minors or intoxicated people.
- Investigating the source of alcoholic beverages involved in fatal traffic accidents.
- Conducting sweeps of entertainment districts to check for use of false identification.
- Conducting minor sting operations to check for retail sales of alcohol to minors.
- Inspecting retailers for valid licenses and for compliance with other requirements under the law and rules.
- Inspecting unlicensed locations such as residences, parks, or gatherings for illegal use of alcohol.
- Monitoring special events such as spring break celebrations and the State Fair.
- Conducting undercover operations in licensed premises to detect narcotics, lewd conduct, prostitution, and gambling.
- Conducting surveillance of suspects for bootlegging and other illegal activities.

Agents regularly inspect both licensed establishments, such as bars and restaurants, and non-licensed locations, such as private residences or outdoor public gatherings, to ensure compliance with the law. In fiscal year 2003, TABC's enforcement agents conducted more than 111,000 inspections of licensed and non-licensed locations. On an annual basis, TABC agents inspect about 80 percent of all licensed locations.

Agents also investigate complaints from the public, licensees, TABC employees, and other state and local agencies. The agency receives complaints through its toll-free complaint line, calls placed to local field offices, e-mail, and by direct contact with the public. In fiscal year 2003, TABC received 5,719 complaints and resolved 5,689, as shown in the chart, *Complaints*.

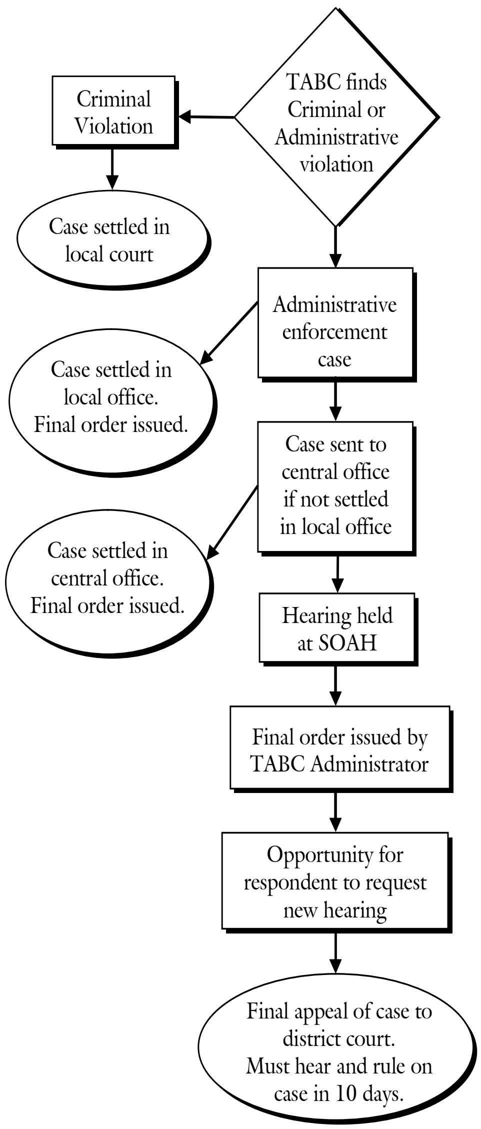
Complaints – FY 2003

Total complaints received	5,719
Complaint disposition*	
No violation	3,165
Administrative charges	1,025
Administrative warnings	658
Criminal charges	615
Verbal warnings	522
Criminal warnings	63
Other dispositions including application protest, nuisance abatement suite, and referral to another agency	120
Total complaints resolved	5,689

*A complaint investigation may find more than one violation, resulting in more than one type of disposition.

TABC also works in conjunction with local law enforcement officials on joint operations, such as providing additional agents to assist local police departments on South Padre Island during spring break. In addition, agents may provide back up assistance for other local law enforcement efforts on cases involving alcohol. For example, TABC agents will investigate the source of alcohol involved in a traffic fatality. TABC agents also work with police departments to conduct minor sting operations at bars, convenience stores, and other retailers.

Enforcement Process



Agents may take three types of action in response to a violation. Agents may file an administrative case if it involves a licensee who violates TABC law or rule; write a criminal citation against an individual who commits a misdemeanor or felony offense; or give a verbal or written warning. Other agency employees may also find administrative violations, such as through compliance audits. The flow chart, *Enforcement Process*, shows how the agency handles administrative and criminal cases.

Administrative Violations

In fiscal year 2003, TABC resolved more than 16,000 administrative violations. The chart, *Administrative Violations Resolved*, shows the different types and number of administrative violations TABC resolved in fiscal year 2003.

When TABC files an administrative case, a licensee may choose to settle the case by paying a fine or having their license suspended. If TABC cannot resolve an administrative case at the regional office, the agency prepares the case for a hearing before an administrative law judge with the State Office of Administrative Hearings (SOAH). In fiscal year 2003, TABC could not resolve 1,319 administrative cases at the regional level. Most of those cases were settled by TABC's legal staff in Austin before they were heard by a SOAH judge. Only 405 cases were actually settled through a SOAH hearing. In fiscal year 2003, TABC collected $2.8 million in fines, temporarily suspended licenses for 3,326 violations, and cancelled licenses for 201 violations. The chart, *Resolution of Administrative Violations*, shows the results of the administrative charges filed by the agency in fiscal year 2003.

Resolution of Administrative Violations – FY 2003

Method of Resolution	Number of Violations
Warning issued	11,776
Civil penalty paid	2,271
Temporary suspension served	1,055
Violation dismissed	669
Granted safe harbor due to participation in seller/server training program	430
License cancelled	201
Other disposition	81
Total	**16,483**

Administrative Violations Resolved – FY 2003		
Type of Violation	**Number of Violations**	**Percent of All Violations**
Failure to pay for beer by cash or check on delivery	2,766	16.8
Sale of alcohol to a minor	1,220	7.4
Possession of alcohol that is unfit for human consumption	1,049	6.4
Failure to conduct business in a place or manner that complies with the law, including allowing gambling, prostitution, or other illegal activity	912	5.5
Failure to comply with outdoor advertising restrictions	617	3.7
Mishandling of tax stamps	391	2.4
Subterfuge or applying for a license for the benefit of another person	354	2.1
Permitted or failed to report a breach of the peace on licensed premises	318	1.9
Failure to pay for liquor deliveries according to credit terms	291	1.8
Failure to file monthly excise tax report on time	246	1.5
Sale of alcohol to intoxicated person	239	1.5
Violations classified as "Miscellaneous" by the agency	4,149	25.2
Other (includes different types of violations with less than 200 incidents each)	3,931	23.8
Total	**16,483**	**100**

Criminal Violations

In fiscal year 2003, the agency filed more than 17,000 criminal citations. Of these criminal citations, 48 percent, were for persons under the age of 21 possessing alcohol. The chart, *Criminal Citations Filed*, shows the type and number of citations issued by the agency in fiscal year 2003. Local courts adjudicate criminal charges in the same manner as other charges brought by law enforcement agencies. Some criminal charges are arrestable offenses, in which case TABC agents will transport a suspect to the local police department or sheriff's office for processing.

Criminal Citations Filed – FY 2003		
Type of Violation	**Number of Citations**	**Percent of All Citations**
Possession of alcohol by person under age 21	8,363	48.1
Public intoxication	1,728	9.9
Open container of alcohol	1,316	7.6
Sell, serve, or make available alcohol to person under age 21	1,130	6.5
Other misdemeanor offenses	676	3.9
Consumption of alcohol during prohibited hours	582	3.4
Driving while intoxicated, driving under the influence, and other traffic offenses	542	3.1
Execution of warrants on behalf of other agencies	505	2.9
Drug-related offenses	453	2.6
Other (includes different types of violations with less than 300 incidents each)	2,094	12.0
Total	**17,389**	**100**

Resolution of Criminal Cases – FY 2003	
Cases pending	12,322
Convictions resulting in: deferred adjudication .... 802 jail term .... 206 probation .... 65 pre-trial diversion .... 2 other penalty, including payment of a fine 3,270	
Total convictions	4,345
Dismissals	342
Juveniles - information is limited and restricted	280
Acquittals	59
Prosecuting attorney refuses to accept the case	41
Total	**17,899**

The vast majority of criminal charges filed by TABC in fiscal year 2003 were still pending in the courts at the end of the fiscal year. The chart, *Resolution of Criminal Cases*, shows the results of criminal charges filed by the agency.

Compliance

In addition to enforcement, TABC performs a variety of monitoring functions to ensure licensees pay their taxes and stay in compliance with the law and agency rules. One of TABC's largest compliance functions involves collecting alcoholic beverage taxes and auditing tax payers. Both the state and federal governments levy taxes on alcoholic beverages, as described in the textbox, *Alcoholic Beverage Taxes*. At the state level, TABC and the Comptroller of Public Accounts collect five different types of alcoholic beverage taxes. The Comptroller collects the sales tax and mixed beverage tax, and TABC collects all other alcohol-related taxes. Most of the tax revenue goes to the General Revenue Fund, with the exception of a portion of the sales and mixed beverage taxes, which goes to local units of government. Excluding sales tax, the State collected about $572 million from alcoholic

Alcoholic Beverage Taxes

TABC collects the following taxes on alcohol.

- **Excise tax:** levied on the sale of alcohol from wholesalers to retailers. The tax has a fixed rate according to the type of alcohol that ranges from $0.19/gallon for beer to $2.40/gallon for distilled spirits. TABC collected $162,903,306 in fiscal year 2003 from this tax and associated fees.
- **Personal importation tax:** levied against individuals importing alcohol from outside the state for personal consumption. TABC collected $2,358,448 in fiscal year 2003 from this tax and associated fees.
- **Airline and passenger train beverage tax:** assessed on drinks served to passengers of airplanes flying in Texas airspace or trains traveling within Texas borders, at a rate of 5 cents per drink. TABC collected $418,581 in fiscal year 2003.

The Comptroller of Public Accounts collects the following taxes on alcohol.

- **Mixed beverage tax:** assessed on mixed drinks, beer, and wine served to consumers. Licensed establishments pay the mixed beverage tax that is assessed as a percentage of a drink's sales price, currently set at 14 percent. Twenty-one percent of this tax is allocated to the counties and cities in which the tax is collected. The Comptroller collected $405,080,599 in fiscal year 2003.
- **Sales tax:** assessed on all alcoholic beverages that are not subject to the mixed beverage tax, such as beer and wine sold at a convenience store. The sales tax rate varies between 6.25 percent and 8.25 percent depending on the local tax rate. The Comptroller cannot determine what percentage of the total sales tax collected came from alcoholic beverage sales.

In addition to state taxes, the federal Alcohol and Tobacco Tax and Trade Bureau collects the following taxes.

- **Federal excise tax:** assessed on top of each state's excise tax on the sale of alcohol from wholesalers to retailers. The tax rate varies according to the type and amount of alcoholic beverage.
- **Occupation tax:** assessed annually in the amount of $250 for retailers, $500 for wholesalers, and $1,000 for manufacturers nationwide.

beverages taxes in fiscal year 2003, 30 percent of which was collected by TABC.

Compliance Audits

TABC performs numerous audits to ensure proper payment of excise taxes and compliance with other laws. TABC auditors review monthly tax returns and perform on-site audits of wholesalers who pay the tax. In fiscal year 2003, TABC conducted 112 on-site audits, which represented about 20 percent of all wholesalers in Texas. These reviews and audits also allow the agency to monitor compliance with cash and credit laws, which require retailers to pay wholesalers for their product according to certain restrictions. The agency's auditors also perform audits to ensure compliance with laws governing the operation of private clubs and requirements for food and beverage permit holders. In fiscal year 2003, TABC conducted 1,245 food and beverage analyses, representing 32 percent of all restaurants serving alcohol, and 453 private club analyses, representing 41 percent of all private clubs.

Ports of Entry

To ensure proper payment of the personal importation tax on alcohol, TABC operates 19 tax collection booths on the most heavily traveled international crossings along the Mexico border. TABC also collects taxes on cigarettes on behalf of the Comptroller of Public Accounts at these border crossings. Texas residents may bring no more than one quart of liquor, 24 twelve-ounce containers of beer, and three gallons of wine into the state within a 30-day period.

TABC operates 19 tax collection booths along the Mexico border.

TABC port personnel cannot conduct searches and therefore rely on individuals to voluntarily declare the purchase of alcoholic beverages and cigarettes. Staff confiscate alcoholic beverages over the importation limits or in the possession of minors and intoxicated people. TABC staff will also confiscate cigarettes in the possession of persons under the age of 18. TABC destroys all confiscated alcohol and cigarettes. In fiscal year 2003, staff confiscated almost 6,700 containers of alcohol and 6,000 containers of cigarettes.

Marketing Practices

TABC oversees the marketing and advertising practices of alcoholic beverage manufacturers and wholesalers to ensure compliance with laws governing these activities. Staff provide technical assistance to the alcoholic beverage industry on allowable advertising, promotion, and marketing practices for alcoholic beverages. In addition, staff investigate and monitor business relationships between the manufacturing, wholesale, and retail tiers of the industry to prevent undue influence of one tier over another. Staff also ensure the quality and accurate classification of alcoholic beverages by testing new products submitted by manufacturers for alcohol content and bottle fill, as well as approving beverage labels. In fiscal year 2003, TABC analyzed almost 1,300 products for introduction to the Texas market, and approved almost 12,000 beverage labels, collecting $300,000 in fee revenue for these approvals.

Seller/Server Training

In 1987, the Legislature created a training program for sellers and servers of alcohol in the hopes of reducing sales to minors and intoxicated people. TABC administers this program, which teaches retail employees how to identify minors and intoxicated people and what the consequences are for selling alcohol to them. Sellers and servers who successfully complete a four-hour training course and pass the required test are certified for two years. In fiscal year 2003, TABC certified approximately 343,000 sellers and servers, or 38 percent of all alcoholic beverage retail employees. Alcoholic beverage retailers that require their employees to be certified may claim a legal defense against administrative action if one of their employees is caught selling alcohol to a minor or intoxicated person.

Seller/Server training is designed to reduce sales to minors and intoxicated people.

TABC does not provide the training itself. Instead, the agency certifies 148 privately operated training schools, their curriculum, and their teachers to ensure they provide the proper information to sellers and servers. TABC staff monitor training classes around the state to ensure compliance with minimum course requirements.

Educational Programs

TABC conducts educational activities to raise awareness about state laws, underage drinking, driving while intoxicated, and other issues involving the use of alcohol. These programs target a variety of groups, including school children, college students, community groups, licensed businesses, and local law enforcement. The textbox, *Educational Programs*, describes the agency's key underage drinking and alcohol awareness programs.

The agency also administers several federal grants that support educational programs. In fiscal year 2003, TABC received more than $360,000 from the federal Department of Justice for programs to reduce underage drinking and $62,000 from the federal Department of Transportation for programs to target drunk driving. TABC used this funding for its own educational campaigns and also awarded grants to various councils of government, local law enforcement agencies, advocacy groups, and university-based programs.

Educational Programs

Project SAVE (Stop Alcohol Violations Early) - TABC enforcement agents conduct presentations to promote compliance with state laws and help prevent underage drinking. In fiscal year 2003, the agency presented Project SAVE to more than 278,500 people.

Shattered Dreams - Community groups sponsor these events with grant funding and other support from TABC. High school students and local law enforcement officials act out dramatizations of alcohol-related car accidents to illustrate the consequences of underage drinking and driving and to help prevent these types of accidents. More than 131,500 students participated in this program in fiscal year 2003.

Safe Prom/Safe Graduation - TABC agents visit high schools to promote safe, alcohol-free prom and graduation parties; and monitor hotels and motels, where students are celebrating, for underage drinking violations.

APPENDICES

Three-Tier System Requirements in Texas

In conducting the review of the Texas Alcoholic Beverage Commission, Sunset staff identified concerns about maintaining such strict regulation of the three tiers of the alcoholic beverage industry – manufacturers, distributors, and retailers. While all 50 states continue to use the three-tier system, many groups are beginning to question the justification for this level of regulation in today's modern commercial environment, and believe that it deserves serious reassessment.[1]

Sunset staff felt further discussion on the topic was needed. While the system was certainly appropriate at one point in time, it now seems to be focused on protecting the interests of the various industry segments and not on public safety. However, staff deemed this issue to be outside its review scope, and therefore did not make any recommendations that specifically addressed changing the three-tier system. However, this appendix highlights some particularly restrictive requirements in Texas, some less restrictive approaches used in other states and at the federal level, and some of the recent legal challenges to the system.

Selected Three-Tier System Restrictions in Texas

Requirements for Exclusive Territorial Agreements for Beer Distributors

The Alcoholic Beverage Code requires beer distributors to sign exclusive territorial agreements with brewers to distribute the brewer's products, and file them with TABC. The Code governs the general terms of these agreements, which define the business relationships between brewers and distributors. The specifics of individual agreements may include:

- granting an exclusive territory to the distributor, and requiring the distributor to aggressively sell and promote the brewer's products over any other products;
- requiring the manager of the distributorship to own a percentage of equity in the business, and requiring the brewer's approval for changes in management; and
- providing the brewer an option to purchase the distributorship, and requiring the brewer's approval for the sale of the business, or any transfer of interest in the business.

Texas law states that these agreements promote the public interest in the competitive distribution of beer and assure product quality. However, Texas law does not require liquor and wine manufacturers and distributors to have similar exclusive territorial contracts. In fact, in 1995, Governor Bush vetoed a bill that would have set up similar requirements for the liquor industry, finding such regulations to be overly restrictive and an unjustified government intervention in the distribution system.[2]

Restrictions Against Distributors Extending Credit to Retailers

To ensure against undue influence across the tiers, the Alcoholic Beverage Code restricts distributors from extending credit to retailers for purchases of alcoholic beverages. For beer, no credit is allowed, and retailers must pay by cash, check, or electronic funds transfer on delivery; and beer distributors must report to TABC retailers that write checks returned for non-sufficient funds. In fiscal year 2003, TABC wrote citations for almost 2,800 bounced checks. For liquor and wine, the Code allows for credit of up to 25 days; but distributors must report to TABC any liquor and wine retailers that do not pay within 25 days. TABC maintains a delinquency list of liquor retailers that have not paid their distributor as prescribed. All distributors are prohibited from selling to those retailers until the retailer pays the amount owed. In fiscal year 2003, TABC wrote citations for 344 credit law violations. While the purpose of these laws is to prohibit undue influence across the tiers, the reality is that they place the State in the position of going after retailers for bounced checks and overdue credit to ensure full payment to distributors.

Requirement that Restaurants and Bars Purchase Liquor Only From Package Stores

The Code requires holders of mixed beverage permits, such as restaurants and bars, to purchase liquor only from retail package stores, rather than directly from a distributor. These package stores must hold distributor's licenses authorizing them to purchase liquor from general distributors, to then resell to restaurants and bars. As a result, these package stores act as an additional middleman or fourth tier, adding extra cost to the liquor that bar and restaurant owners purchase.

Licensure of Distributor Sales Representatives

TABC licenses about 22,000 liquor, beer, and wine distributor sales representatives to ensure that only authorized individuals solicit retailers. These representatives are employed by distributing companies that are already licensed by the State. In the last five years, TABC has only written, on average, about 28 administrative citations annually against these sales agents, primarily for selling to unlicensed establishments. More than half of other states do not license distributor sales representatives. Other states simply require these agents to carry identification issued by their employers.

Less Restrictive Federal and State Approaches

All states use the three-tier system to regulate the alcoholic beverage industry, with varying levels of restrictions on interactions and inducements allowed between the tiers. Overall, regulations by the federal Alcohol and Tobacco Tax and Trade Bureau (TTB) allow for greater flexibility between the tiers than Texas and several other states. The majority of other states use TTB's laws regulating manufacturers and distributors as a baseline for their state's regulations. The textbox, *Federal Tax and Trade Bureau Regulation to Ensure Retailer Independence,* summarizes TTB's general approach to ensuring manufacturers and distributors do not exert control over retail sales. The following compares Texas' more restrictive regulation to other states with laws modeled after TTB regulations.

Federal Tax and Trade Bureau Regulation to Ensure Retailer Independence

TTB regulates anti-competitive practices in the alcoholic beverage industry to the extent that inducements from upper tier members prevent or hinder free trade by excluding a competitor's product from the market. Such inducements include having an interest in a retailer's establishment, furnishing items of value to retailers, extending credit to retailers, and commercial bribery.

When interpreting the extent that upper tier members can provide inducements to retailers, TTB takes into consideration protection of public health, the value of the items, and established trade practices that do not harm public interests. TTB regulations on inducements apply to liquor and wine, but only apply to beer to the extent that a state has its own, similar laws in place.

Appendix A

Three-Tier System Requirements in Texas

Allowing Higher Value Promotional Items and Advertising

Texas inconsistently limits the value of promotional displays and other advertising items that distributors can provide retailers. For liquor, the limit is $101 per brand, per location, per year; but for beer, the law places no dollar limit on the value. In addition, Texas prohibits upper tier members from purchasing advertising for retailers. In contrast, TTB regulations do not place a dollar limit on the value of promotional items, allow product displays up to $300, and allow manufacturers to purchase advertising for retailers.

Instead of placing specific restrictions on the industry, TTB monitors the industry to ensure the upper tiers do not unfairly influence the retail sector, for example by providing inducements that would result in a retailer excluding a specific manufacturer's product from the market. Most states prohibit the purchasing of advertising, but some states allow it if multiple retailers are included in the advertising. Thirty-one other states have adopted the less restrictive TTB regulations for promotional items, advertising, and other allowable inducements.

Allowing Manufacturers to Provide Product Samplings

Texas prohibits manufacturers from carrying bottles that actually contain liquor, and only allows a manufacturer to provide a sample if the establishment has never purchased the product before. In addition, Texas limits the size of the sample to smaller sizes than allowed under TTB regulations. For example, Texas limits beer sample sizes to one six pack, while TTB allows up to three gallons. In addition, Texas law prohibits manufacturers from paying for, and conducting, sampling events, and only allows manufacturers to solicit retailers in the presence of distributors' sales agents.

In contrast, TTB regulations allow manufacturers to provide alcoholic beverages, as well as conduct consumer tastings at retail establishments, and do not require manufacturers to be accompanied by distributors. The majority of other states allow manufacturers representatives to visit accounts without distributors being present.

Allowing Consumer Contests and Coupons

Texas is the only state that requires a sweepstakes promotion to be conducted in 30 other states before being allowed in Texas. In addition, Texas does not allow coupons redeemable for discounts on alcoholic beverages, and only allows limited consumer contests.

TTB regulations allow consumer contests and coupons as along as all retailers can participate. The vast majority of other states allow consumer contests generally, with some requiring prior approval from the state regulatory agency, and most all other states allow consumer coupons.

Recent Court Challenges to the Direct Shipment of Wine

Increasing numbers of wineries are selling directly to consumers through the Internet, which about half of the states permit. For example, California has allowed wineries to opt out of the distributor network and sell wine over the Internet to consumers living in states that have reciprocity agreements with California. In addition, certain large retailers are demanding the ability to negotiate volume discounts directly from manufacturers, by-passing the distributor tier.

Appendix A

Three-Tier System Requirements in Texas

In 2004, the nation's largest wine retailer, Costco, sued the State of Washington challenging its prohibition against out-of-state wineries shipping directly to Washington retailers. Costco contends this prohibition violates the Commerce Clause of the U.S. Constitution, because the state allows direct shipments from its in-state wineries to other states. Costco's ultimate goal is to be able to purchase wine directly from the manufacturer.

The Federal Trade Commission (FTC) and the U.S. Supreme Court have also taken an interest in interstate direct shipment of wine. In July 2003, FTC staff found that state bans on interstate direct shipping are the largest barrier to expanded e-commerce in wine, and contribute to higher prices and reduced choices for consumers.[3] Later this year, the Supreme Court is set to hear a case examining the constitutionality of several states' authority to ban interstate shipments of wine directly to consumers.

In Texas, a federal district court found in August 2002 that Texas' prohibition against shipments from out-of-state wineries to consumers in Texas was unconstitutional, and as a result, shipments to wet areas of the state are currently allowed. However, Texas wineries can only ship directly to consumers located in Texas, or outside of Texas, if the purchase was made on the winery's premise. TABC did not seek a Supreme Court review of the federal district court's decision, but the agency has requested an opinion from the Attorney General's Office to clarify if TABC has the authority to require out-of-state wineries to route deliveries through Texas distributors.

[1] Erik D. Price, "Time to Untie the House?", *Washington State Bar News* (June 2004). Online. Available: www.wsba.org/media/publications/barnews/2004/price.htm. Accessed: October 12, 2004.

[2] George W. Bush, Governor of the State of Texas, Veto Proclamation for House Bill 2732 (1995). Online. Available: www.lrl.state.tx/scanned/vetoes/74/hb2732.pdf. Accessed: October 13, 2004.

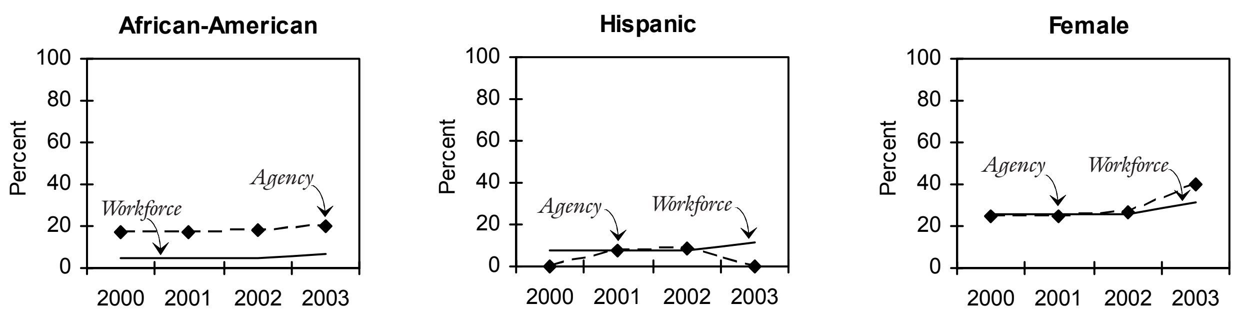
[3] Federal Trade Commission, *Possible Anti-Competitive Barriers to E-Commerce: Wine* (July 2003). Online. Available: www.ftc.gov/os/2003/07/winereport2.pdf. Accessed: October 12, 2004.

Equal Employment Opportunity Statistics

2000 to 2003

In accordance with the requirements of the Sunset Act, the following material shows trend information for the Texas Alcoholic Beverage Commission's employment of minorities and females in all applicable categories.[1] The agency maintains and reports this information under guidelines established by the Texas Commission on Human Rights.[2] In the charts, the solid lines represent the percentages of the statewide civilian workforce for African-Americans, Hispanics, and females in each job category. These percentages provide a yardstick for measuring agencies' performance in employing persons in each of these groups. The diamond-dashed lines represent the agency's actual employment percentages in each job category from 2000 to 2003. The agency does not employ persons in the service/maintenance job category.

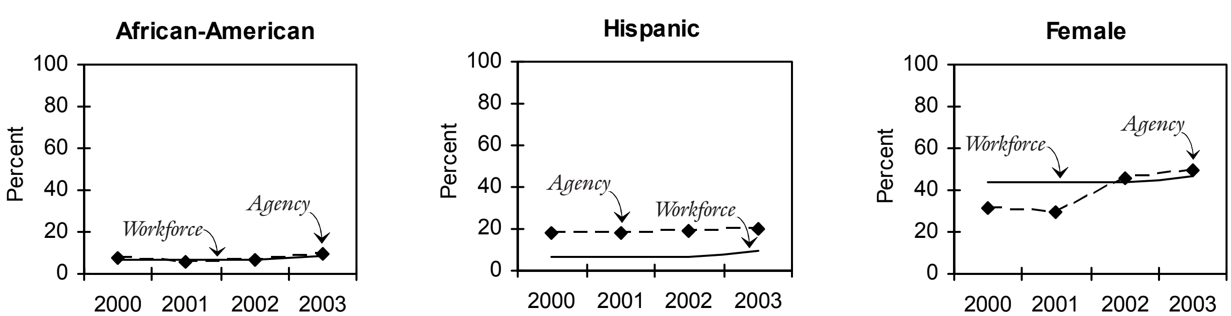
Administration



Positions: 12 12 11 10 | 12 12 11 10 | 12 12 11 10

TABC exceeded the civilian workforce percentages for African-Americans and females in this category, but fell short for Hispanic representation in 2003.

Professional



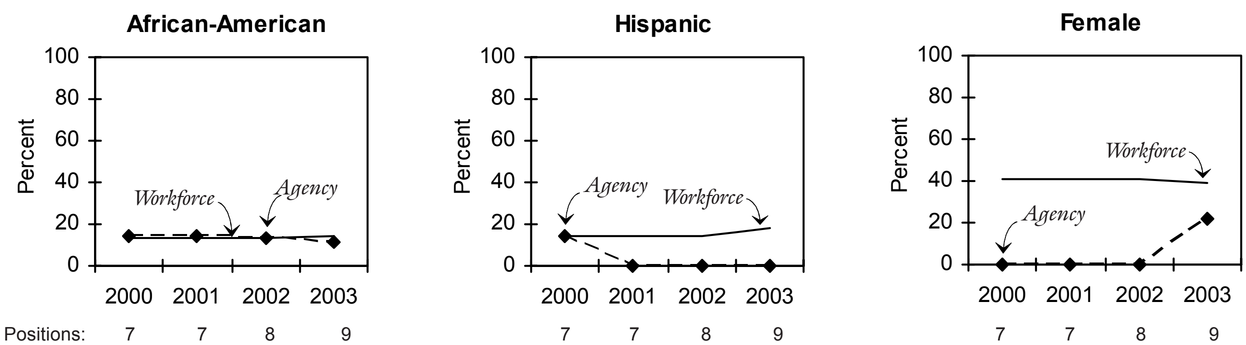
Positions: 86 89 114 119 | 86 89 114 119 | 86 89 114 119

TABC has generally met or exceeded the percentages in this category.

Appendix B

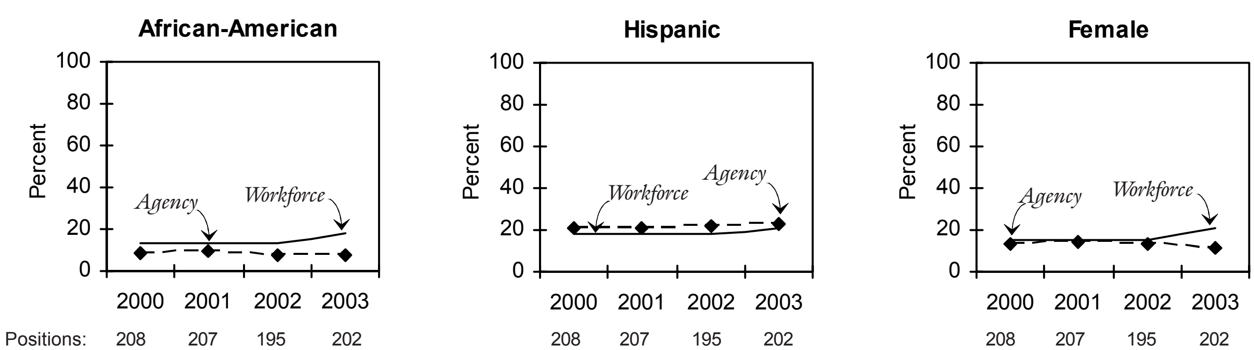
Equal Employment Opportunity Statistics

Technical



TABC has met the percentage for African-Americans in this category, but has fallen short for Hispanic and female representation.

Protective Services

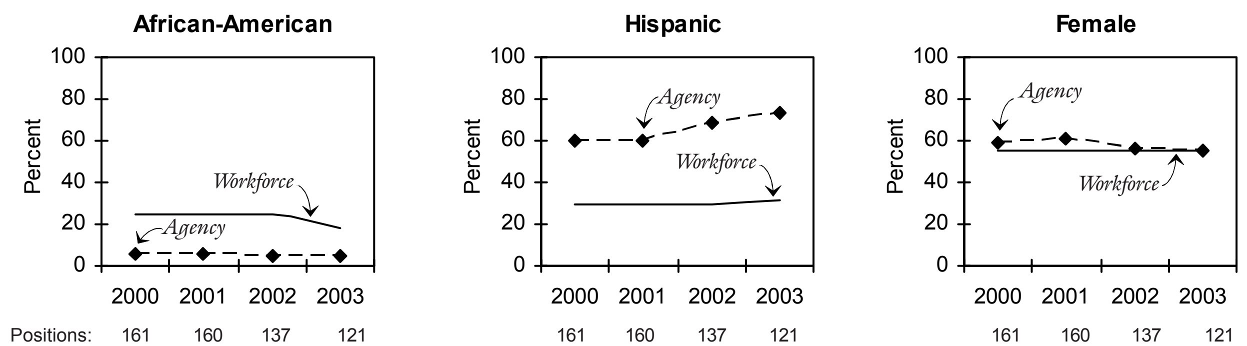


TABC exceeded the percentage for Hispanics in this category, but fell short for African-American and female representation.

Appendix B

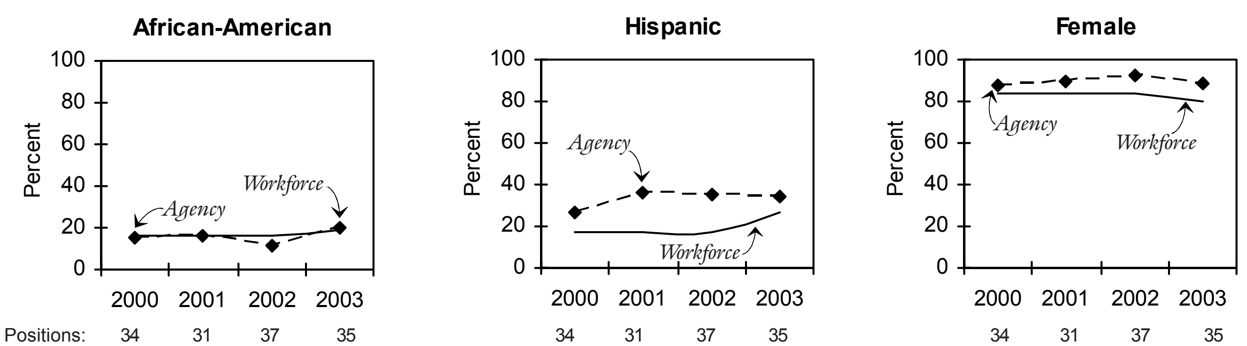
Equal Employment Opportunity Statistics

Para-Professionals



TABC has fallen short of the percentage for African-Americans in this category, but exceeded the percentages for Hispanics and females.

Administrative Support

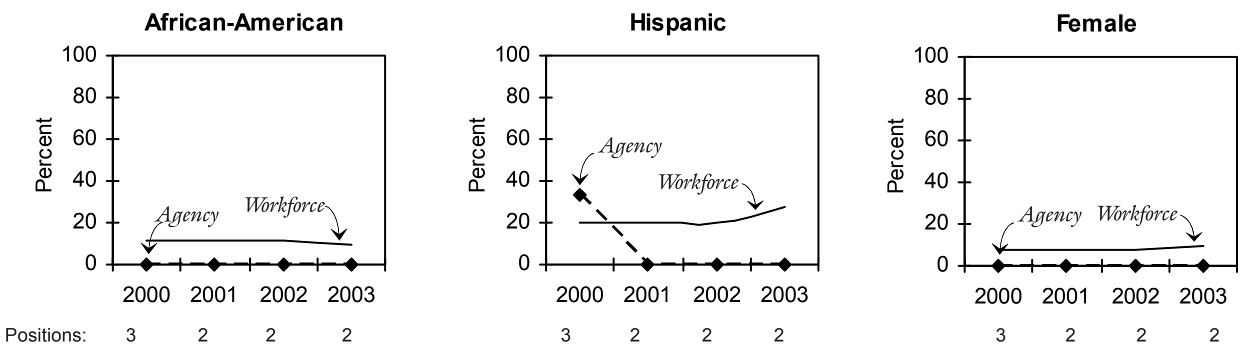


TABC has met or exceeded the percentages for all groups in this category.

Appendix B

Equal Employment Opportunity Statistics

Skilled Craft



TABC has failed to meet the percentages for skilled craft, but it has few employees in this category.

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1 Texas Government Code, sec. 325.011(9)(A).

2 Texas Labor Code, sec. 21.501. The Texas Human Rights Commission (HRC) has been the agency responsible for collecting and distributing EEO data. During the 2003 Session, the Legislature passed HB 2933 transferring the functions of HRC to a new civil rights division within the Texas Workforce Commission (TWC). The legislation is to take effect upon certification of the TWC civil rights division by the appropriate federal agency; no specific date has yet been established.

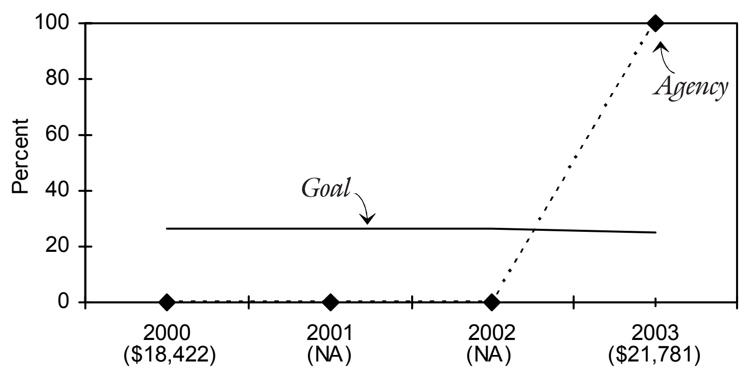
Historically Underutilized Businesses Statistics

2000 to 2003

The Legislature has encouraged state agencies to increase their use of Historically Underutilized Businesses (HUBs) to promote full and equal opportunities for all businesses in state procurement. The Legislature also requires the Sunset Commission to consider agencies' compliance with laws and rules regarding HUB use in its reviews.[1] The review of the Texas Alcoholic Beverage Commission revealed that the agency appears to be complying with state requirements concerning HUB purchasing, but has not adopted its HUB policies in rule.

The following material shows trend information for the Texas Alcoholic Beverage Commission's use of HUBs in purchasing goods and services. The agency maintains and reports this information under guidelines in the Texas Building and Procurement Commission's statute.[2] In the charts, the flat lines represent the goal for HUB purchasing in each category, as established by the Texas Building and Procurement Commission. The diamond-dashed lines represent the percentage of agency spending with HUBs in each purchasing category from 2000 to 2003. Finally, the number in parentheses under each year shows the total amount the agency spent in each purchasing category. TABC has generally fallen short of the state goals, but made improvements in fiscal year 2003 in the building construction and special trade categories.

Building Construction

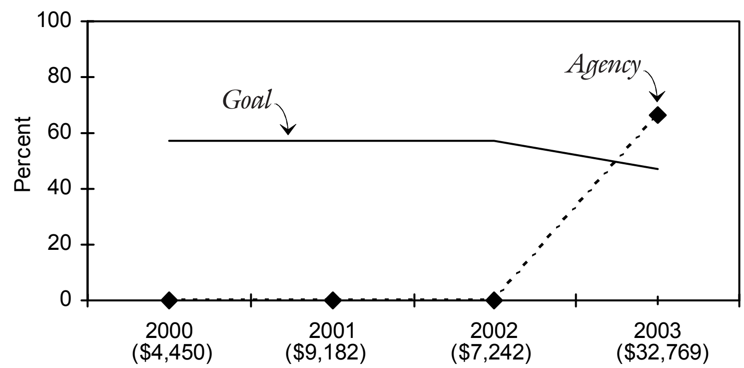


In past years, TABC failed to meet the goal or did not spend money in this category, but in 2003, it far exceeded the goal.

Appendix C

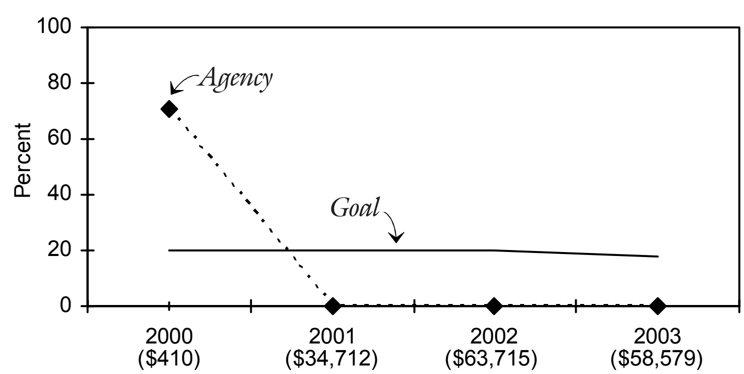
Historically Underutilized Businesses Statistics

Special Trade



In past years, TABC failed to meet the goal in this category, but in 2003, it exceeded the goal.

Professional Services

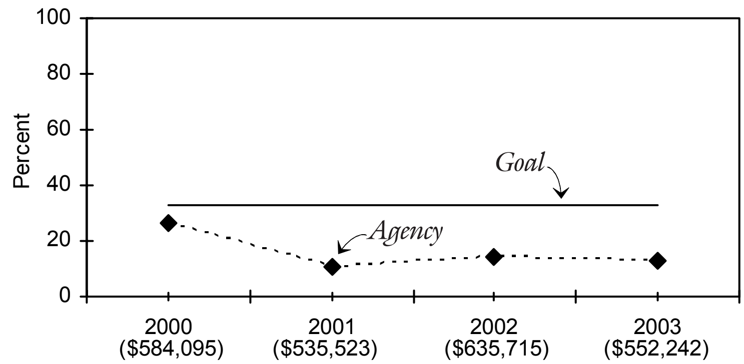


TABC has failed to meet the goal in this category in the past three years.

Appendix C

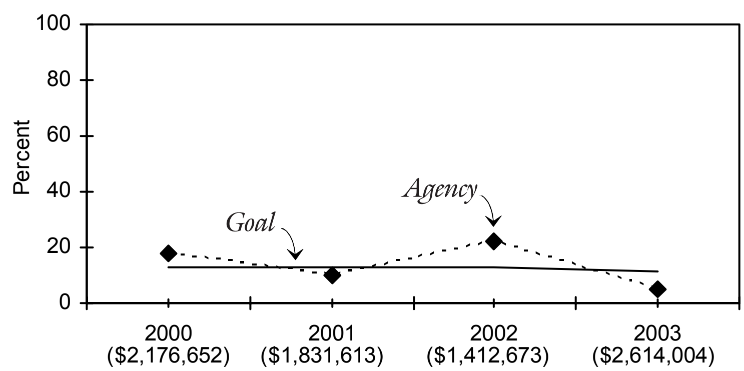
Historically Underutilized Businesses Statistics

Other Services



TABC has failed to meet the goal in this category for the past four years.

Commodities



TABC's spending in this category has been slightly above or below the goal over the past four years.

[1] Texas Government Code, sec. 325.011(9)(B).

[2] Texas Government Code, ch. 2161.

Staff Review Activities

The Sunset staff engaged in the following activities during the review of the Texas Alcoholic Beverage Commission.

- Worked extensively with the Administrator, Assistant Administrator, Division Directors, General Counsel, Internal Auditor, and agency staff at Headquarters and in the field.
- Attended Commission meetings and met individually with Commission members.
- Toured a brewery, winery, and beer and liquor distribution facilities.
- Accompanied Austin and Dallas Regional Office staff on compliance and enforcement activities. Observed compliance staff on inspections of licensed establishments and new locations, and toured the Austin Regional Office's confiscated property room. Accompanied enforcement agents on night activities, including minor stings; complaint investigations; routine inspections of nightclubs, bars, and convenience stores; monitoring establishments for public intoxication and underage drinking; and arresting a bootlegger in conjunction with the Austin Police Department.
- Met with local officials during field visits, including local law enforcement officers, district attorneys, city prosecutors, and city attorneys. Interviewed local district judges by telephone.
- Attended a seller training session with completion of the required test. Attended a continuing education session for seller training school trainers in Austin.
- Met with or interviewed over the phone representatives of interest groups representing domestic and foreign manufacturers, importers, distributors, and retailers; nonprofit organizations interested in public safety issues related to alcohol; and owners and managers of licensed establishments. Conducted interviews and solicited written comments from national, state, and local interest groups.
- Talked with staff of the Governor's, Lt. Governor's, and Speaker's Office; State Auditor's Office; Legislative Budget Board; Department of Public Safety; Parks and Wildlife Department; Comptroller of Public Accounts; and legislative committees with oversight of the agency.
- Reviewed reports by the State Auditor's Office, Legislative Budget Board, Federal Trade Commission, and the agency's Internal Auditor.
- Reviewed agency documents including minutes and transcripts of Commission meetings, agency contracts, reports, licensee complaint files, personnel complaint files, enforcement files, statutes and rules, legislative reports, and previous legislation.
- Performed background and comparative research using the Internet and reviewed literature on alcoholic beverage issues. Researched the functions of alcoholic beverage regulatory agencies in other states, and compared the regulation of alcoholic beverages nationwide. Conducted targeted phone interviews with representatives of the California, Colorado, Florida, New Mexico, and New York alcoholic beverage regulatory agencies. Reviewed federal Alcohol and Tobacco Tax and Trade Bureau regulations and interviewed selected staff of that agency by telephone.
- Attended contested case hearings at the State Office of Administrative Hearings in San Antonio.

Sunset Review of the Texas Alcoholic Beverage Commission

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