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## WHOLESALE BEER DISTRIBUTORS OF TEXAS

November 14, 2018

To: Sunset Advisory Commission  
From: Tom Spilman, Executive Vice President, Wholesale Beer Distributors of Texas  
Re: Comments of the Wholesale Beer Distributors of Texas ("WBDT") on Sunset Staff Recommendations for the Texas Alcoholic Beverage Commission ("TABC")

### Introduction

The WBDT strongly supports the continuation of the TABC. The TABC provides critical oversight of an industry subject to well established regulations which effectively mitigate the negative aspects of the sale and use of alcoholic beverages. Most importantly, the TABC's dedicated regulatory commitment is vital in preventing the anti-competitive monopolistic tendencies in the Texas marketplace that are endemic to the unregulated alcohol markets found throughout the world.

WBDT believes the current administration and leadership of the TABC has brought effective management and reforms to an agency that is functioning at an extremely high level to serve and protect our state. Many of the concerns raised by Sunset staff are being effectively addressed by the new administration and can be fully addressed if the TABC is fully funded. WBDT believes that restoring the revenue collected from the industry back to the TABC would be most helpful in this regard.

WBDT has always supported strict, uniform, fair and impartial enforcement of the laws and regulations governing the malt beverage business. We are keenly aware that this is a customer service-oriented business, which exists only through public approval and acceptance. It therefore must be controlled and operated under a system with the public interest and welfare in mind. WBDT supports and defends Texas's beer cash law and other three-tier regulations.

The Sunset Commission staff report wastes little time in diving straight into the turbulent intra-industry policy debates buried in the nuances of the Alcoholic Beverage Code. Using naïve language and cliché characterizations like "antiquated" and "byzantine," the staff report picks winners and losers based upon one-sided analysis that holds almost no regard for the extra-ordinarily competitive malt beverage industry in Texas.

The WBDT strongly disagrees with several recommendations of the Sunset Commission Staff which threaten to undermine the fabric of a well-functioning regulatory system and seem to reflect a policy preference to treat alcohol more similarly to other, non-intoxicating commodities.

## Comments on Issues

### WBDT Issue 1 – Recommendation on cash law would undermine the competitive and healthy Texas beer market.

Sunset Recommendation 3.2: Make cash payments optional by applying the existing credit law restrictions to beer transactions between retailers and distributors.

WBDT Response: Unlike the credit law which is applicable to wine and spirits, the cash law carries no administrative burden to the TABC and is vital to protecting a beer marketplace that is far healthier and more competitive than its industry counterparts where credit is allowed. Modification of the cash law should be removed from the Sunset recommendations for the following reasons:

- Contrary to Sunset Staff assertions, TABC does not “monitor daily transactions” between malt beverage distributors/wholesalers and retailers. Nor is the agency in “the business of collecting unpaid bills for the alcohol industry.”
- The sale of beer through the currently prescribed cash law system ensures that the excise taxes are paid promptly to the state by the distributor.
- There is virtually no administrative burden to the TABC to enforce Section 102.31 of the Texas Alcoholic Beverage Code (“Cash law”). Violations are self-reported by industry on a web portal, not to TABC law enforcement, field personnel, or auditors. Violators receive a computer-generated letter on their first 6 violations (within a 12-month period). See 16 TAC 45.131, and accompanying Marketing Practices Bulletin—MPB035 December 28, 2009. The simplicity of the cash requirement makes the cash law an almost zero administrative burden to the TABC. In contrast, the credit law requires constant staff attention by maintaining delinquency lists and issuing enforcement notices.
- The cash law is a critical public policy issue vital to maintaining the integrity of the three-tier system. The cash law prevents the anti-competitive practices associated with leveraging concessions and favorable product treatment from retailers in debt to a distributor.
- The current Texas beer market is more competitive than most any other retail commodity, with dozens of brand options in the typical supermarket aisle. The healthy market relies, in part on prohibitions against improper benefits or “payola” being offered to retailers for shelf space or exclusive product placement. Introducing credit would destroy those free market protections. Selective offering or extending favorable credit terms would be used to bring all the anti-competitive evils the market has thus far avoided.

**WBDT Issue 2: Repealing the ability of pay a fine in lieu of suspension is a policy issue unrelated to the functioning of the agency and would have a significant impact on capital investment in Texas businesses.**

Staff Recommendation 5.2: Remove the requirement that TABC offer licensees a choice between a suspension or fine, and instead authorize TABC to determine the appropriate penalty for each violation.

WBDT Response: WBDT believes the TABC currently has the necessary tools to shut down industry members who pose a threat to the public welfare. Section 11.64 of the Texas Alcoholic Beverage Code gives the TABC broad authority, including rulemaking authority, to ensure it can shut down bad actors who pose a threat to public health and welfare.

Eliminating the code provision allowing payment of a fine in lieu of suspension (only recently adopted by the Legislature) jeopardizes contracts between industry members and would have a chilling impact on investment and lending decisions to provide capital critical to the continued success of the industry in Texas.

Banks, investors and creditors would be much more circumspect about investing in Texas businesses if operations could be shut down based upon the unpredictable decisions of a revolving set of staff and commissioners. Sunset staff offers no evidence that current enforcement and penalty options are in any way deficient to protect the public safety and welfare.

**WBDT Issue 3: The TABC functions very well with three commissioners.**

Staff recommendation 1.2: Expand the Alcoholic Beverage Commission from three to five members.

WBDT Position: The TABC functions very well with three highly qualified commissioners who find consensus on most issues. Given the appropriate and high conflict of interest standards, it would be difficult to maintain the very high quality of commissioners if forced to find additional candidates. Furthermore, additional commissioners would only expand the necessary bureaucratic support for the members, decreasing efficiency and diverting staff resources from the core functions of the agency.

Transferring every-day decision-making from the Executive Director to the volunteer, part time, Governor-appointed Commissioners would be cumbersome, time consuming and counter-productive to reducing bureaucratic delay. Requiring volunteer commissioners to engage in such a micro-managing level of oversight makes it more difficult to find high quality volunteers and risks creating a perception that enforcement decisions are subject to political influence. The Commissioners have broad authority under current law to review and reverse staff decisions, and sunset staff has not identified any specific deficiencies in that process.

**WBDT Issue 4: The distinction between beer and ale serves an important public policy purpose and should not be eliminated.**

Staff recommendation 2.2: Modernize Texas' regulation of malt beverages by eliminating distinctions between beer and ale.

WBDT Position: The staff recommendations reflect a general attitude throughout the TABC analysis that alcohol be treated like any other commodity. The proposal to eliminate the distinction between ale and beer is a policy position which should be rejected as it is at odds with positions taken by the Legislature since prohibition and through the 2017 legislative session. In fact, the Legislature explicitly rejected this concept last session (S.B. 2169, by Sen. Huffines, left pending in Senate Business and Commerce Committee).

The staff recommendation does not fully disclose the dramatic code rewrite necessary to eliminate the local option zoning and election issues with eliminating the distinction between beer and ale in Texas law. There are important reasons Texas law, like many other states, differentiates between beer and stronger ale, taxes them differently, and there are constitutional protections to the authority of local jurisdictions to authorize one and not the other.

*History*

In Texas, the sale and consumption of beer became legal again in 1933, so long as its alcohol content was less than 3.2 percent. Ale followed. It was not legal until the repeal of the 18th amendment by the ratification of the 21st amendment to the U.S. Constitution, and the adoption of the Texas Liquor Control Act, which became effective November 15, 1935.

The emphasis in Texas to delineate between beer and the higher alcohol content ale mirrored the approach of most other States and reflected the strong public policy reasoning to regulate stronger malt beverages differently than lesser intoxicating "beer." In 1933 Raymond Fosdick and Albert Scott published a treatise "Toward Liquor Control" which made recommendations to States regarding sound alcohol regulation as the end of prohibition approached. The treatise served as the model for regulation throughout the country and advocated the three-tier system which is still the standard of regulation throughout the country. Importantly, the book emphasizes the need to delineate between "strong" and "light" beer. *Toward Liquor Control*, Chapter Three: Light wines and Beer vs. Spirits (Harper and Brothers Publishers, 1933).

The treatise advocates that regulation be tailored to different beverages based on alcohol content, stating that "American liquor legislation in the past has, as we have seen, been guided more by emotion than by reason or experience. In the stumbling search for a law to cure the drink evil, legislators seldom paused to inquire what drinks should be the main target of attack." (Id. at 28). The treatise explains, "If light beers and wines were the only alcoholic beverages consumed, the social implications of the liquor trade would present but few difficulties. It is, primarily, the distilled liquors and, secondarily, the heavier beers and wines that create the real problems." (Id. at 35).

The history of delineating between stronger beers is instructive, precisely because it serves as the public policy justification for the labeling distinctions in this state.

### *Implications*

Texas has always treated “beer” and “ale/malt liquor” differently. They are considered different products and require different permits, and they are taxed at different rates. The current tax on beer is \$6.00 per 31-gallon barrel. The tax on ale and malt liquor is \$0.198 per gallon or \$6.138 per 31 gallons.

Furthermore, the wet-dry laws of the state were written to authorize the citizens to determine if they only wanted a lower alcoholic beverage, beer, or whether they wanted to authorize higher alcoholic content beverages such as ale, malt liquor and wine, and finally if they wanted to allow distilled spirits which was a separate category.

Now more than ever before a distinction between beer and ale/malt liquor needs to be maintained in the code because of the explosion of the craft beer industry. There are more malt beverage products on the shelf with alcohol content ranging between 3% to 15% than there have ever been in Texas.

### **WBDT ISSUE 5: The proposal to streamline TABC label approval would jeopardize the health and welfare of Texas consumers.**

Staff recommendation 3.1: Streamline TABC’s process for approving alcoholic beverages for sale in Texas.

WBDT Response: The Sunset Commission should reject the staff recommendation to eliminate the label approval process at the TABC. Again, this proposal reflects a broader theme in the report to make policy determinations to deregulate the oversight of how alcoholic beverages are handled and sold in Texas. The current label approval process and testing of malt beverages is vital to ensuring safe products are sold in Texas and labels correctly identify the alcohol volume of the beverage. As evidenced by the loosely regulated roll out of legalized marijuana in other states, consumers can experience significant harm when labels do not clearly and reliably indicate the potency of intoxicating commodities.

The Federal government does not evaluate labels for wine and beer produced and sold only in the state of Texas. Removing label approval requirements would leave a great number of products of Texas startups unregulated and untested. As the alcohol volume of ales continues to climb, now is not the time to abdicate the state’s responsibility to ensure the products sold to consumers are safe for public consumption.

**WBDT Issue 6: Eliminating the State's tax on imported alcohol only serves to help foreign interests at the disadvantage of Texas.**

Staff Recommendation 6.1: Repeal the state's inefficient tax on alcohol imported for personal use and eliminate TABC's ports of entry tax collection program.

WBDT Response: Allowing imports to go untaxed would serve to unfairly punish local businesses to the advantage of their cross-border competitors. The TABC should enact cost saving efficiencies to maintain its current tax collection efforts at ports of entry which would make the program profitable for the State. The staff recommendation also fails to account for the substantial revenue collected by the TABC in the port of entry program related to tobacco imports which would otherwise go untaxed.

**WBDT ISSUE 7: The Legislature should not expand three-tier exceptions to authorize package stores to sell beer to other retailers.**

Staff Recommendation 2.2(i): Package stores and wine-only package stores would have authority to purchase and sell all malt beverages with one permit instead of two, which is consistent with most other retailers in Texas. This recommendation also would codify an informal TABC policy, in place for several decades, allowing package stores with a local distributor's permit to purchase beer from distributors and distribute it to bars, restaurants, and private clubs.

WBDT response: This recommendation again fundamentally misunderstands the constitutionally protected right of local jurisdictions to determine which types of products can be locally sold. Package stores are different from other retailers in that distinct permits are needed for the broad spectrum of products they sell to reflect the different wet/dry decisions made by jurisdictions throughout the state.

Currently package store licensing is under direct attack by multi-national entities seeking to bring ubiquitous access and cheap liquor to Texas markets. Now is not the time to create new authorization for sales to other retailers which are inconsistent with the policy goals to the Texas system.

**WBDT Issue 8: The Sunset bill should not be a vehicle to pass legislation related to the storage of high-volume malt beverages which has failed in past sessions.**

Staff recommendation 2.2(e): The current authority for beer manufacturers to store beer anywhere in the state should apply to all malt beverages. Currently, ale manufacturers may only store their products in the county where the permitted manufacturing facility is located.

WBDT response: This recommendation is a replica of proposals that the Legislature has rejected in previous sessions. By authorizing "blind" warehousing for high volume malt beverages, the state

oversight over the distribution of the products becomes more difficult. Going forward, the WBDT would support making the regulations applicable to ale apply to beer.

**WBDT ISSUE 9: The Legislature should not eliminate the agent licenses which are critical to TABC oversight of how malt beverages are sold and promoted to the public.**

Staff recommendation 2.1(b): Eliminate agent licenses and permits. State law would no longer individually regulate agent employees of manufacturers and distributors, but would still govern what the agents can do. This change would remove a substantial burden on TABC by eliminating one-quarter of the licenses and permits it currently processes. Since employers are responsible for their agents' actions, licensing these employees is duplicative and provides no public benefit. This recommendation would require businesses to retain agent employees' employment records for a minimum of four years in the event TABC receives a complaint.

WBDT Response: While WBDT agrees that there are a high number of agent licenses in Texas, WBDT strongly disagrees that the licensing places an administrative burden to the TABC and in fact streamlines the ability to provide necessary oversight regarding the way malt beverages are promoted and sold to the public. Eliminating the licenses would make it more difficult for the TABC and employers to identify bad actors and act against those engaged in illegal practices in coordination with retailers responsible for the ultimate sale to consumers.

\*See Attached TABC Marketing Practices Bulletin dated December 28, 2009