

Texas Alcoholic Beverage Commission
Quarterly Update to the Senate Business and Commerce Committee
January 14, 2014

IMPLEMENTATION OF BEER-RELATED LEGISLATION

TABC has implemented, without significant problems or concerns, all beer-related legislation that went into effect following the 83rd Legislative Session.

SB 515 by Eltife authorizes a brewpub to manufacture up to 10,000 barrels a year instead of 5,000. Authorizes brewpubs to sell their own malt beverages to wholesalers and distributors. Authorizes brewpubs holding a BG permit who only sell their own product to sell to retailers (up to 1,000 barrels), and to any qualified person outside of Texas. Effective 6-14-13.

Brewpubs who wish to sell their products to distributors must submit a territorial agreement to TABC and receive label approval on the products. At this time, only one brewpub has submitted a territorial agreement. Six brewpubs have obtained label approval for products, indicating that they expect to sell their product to retailers, distributors, or ship to qualified persons outside of Texas.

Ten new brewpub licenses were issued in 2013, including two that switched from breweries to brewpubs (Jester King and New Braunfels Brewing Company). TABC issued five brewpub licenses in 2012 and nine in 2011. There are now 53 brewpubs in Texas: 31 with Wine and Beer Permits (BGs) and 22 with Mixed Beverage Permits (MBs or RMs).

Two issues have been raised relating to this new legislation which perhaps were not fully understood until the new laws were in place. First, although SB 515 authorizes certain brewpubs to sell directly to retailers, it does not directly give them the authority to transport their product. Because no special permit is required to transport beer (up to 4% ABW), the brewpubs can make those deliveries. However, a permit is required to transport ale (over 4% ABW).

After a careful review of relevant sections of the Alcoholic Beverage Code, TABC has determined that brewpubs who are authorized to sell direct to retailers have two options available to them.

1. Hire a company that holds a Carrier Permit (C) to transport product.
2. Obtain a Private Carrier Permit (O) to transport product. The fee for a two-year Private Carrier Permit is \$60. The surcharge is \$252.

Second, the Alcoholic Beverage Code authorizes brewpubs to sell their own products only at the licensed location. Therefore, if a brewpub obtains a temporary permit or caterer's permit for a special event away from the brewpub, they are not authorized to sell their own beer or ale – only other brewery products. They would have to sell their

own product to a distributor, and then purchase it back, having the distributor deliver the product to the location where the special event is being held.

Training was provided to Texas industry members in August 2013, and a detailed letter explaining the implementation of new laws related to brewpubs is being finalized.

SB 516 and SB 517 by Eltife changed the limits on small brewers and manufacturers selling directly to retailers. Under previous law, a brewer or manufacturer who made less than 75,000 barrels annually could self-distribute any amount. Under SB 516 and SB 517, a brewer or manufacturer who makes less than 125,000 barrels annually can obtain a self-distribution permit or license and sell up to 40,000 barrels to retailers annually. Effective 6-14-13.

Although SB 516 and SB 517 went into effect June 14th, TABC was unable to begin issuing the new permit and license types until a rule was passed establishing a surcharge. In the meantime, those brewers and manufacturers who were already selling direct to retailers were allowed to continue these sales without the new license/permit.

The new rule became effective October 24, 2013, and the agency has been accepting applications and issuing the licenses and permits since that time. Fifteen breweries have obtained their self-distribution licenses/permits.

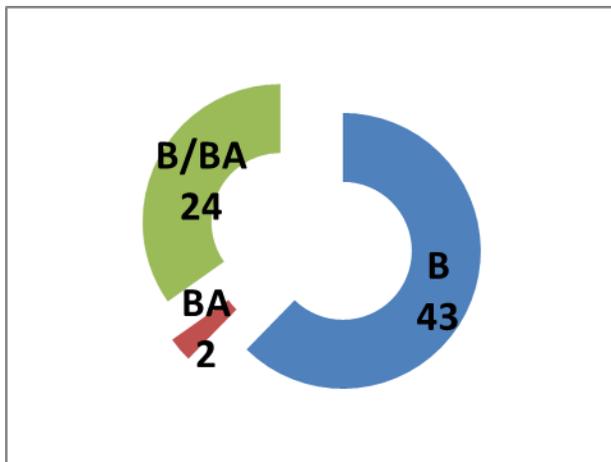
SB 518 by Eltife authorizes manufacturers and brewers who produce less than 225,000 barrels of malt beverages annually to sell up to 5,000 barrels annually of malt beverages produced on the premises to visitors at the brewery for on-premises consumption. Effective 6-14-13.

Brewers and manufacturers who were previously providing free malt beverages to visitors at the brewery are now charging for these drinks. TABC has not been made aware of any problems created by this new authority. However, the agency is in the process of reviewing TABC Administrative Rule 45.103 On-Premise Promotions. Currently, this rule applies to retailers and prohibits happy hour practices and drink specials that can be construed as encouraging excessive consumption. Because all members of the manufacturing level now have the authority to sell direct to consumer, the agency believes the same restrictions should apply to breweries, wineries and distilleries.

Nineteen new breweries in Texas obtained permits in 2013 as compared to 18 in 2012 and 19 in 2011. All but one of these breweries is still active today. There are currently 74 total "packaging" breweries in Texas; 69 are craft brewers and five are very large breweries.

As shown in the chart below, 43 Texas craft brewers hold Brewer's Permits (B) authorizing the production of alt/malt liquor (malt beverages with more than 4% ABW).

Two craft brewers hold Manufacturer's Licenses (BA), authorizing the production of beer (malt beverages with no more than 4% ABW). Twenty-four craft brewers hold both a Brewer's Permit and a Manufacturer's License, authorizing the production of malt beverages above and below 4% ABW.



SB 639 by Carona clarifies the prohibition on reach-back pricing and prohibits a manufacturer from accepting payment for a territorial agreement. Nothing in section 102.75 AB Code shall interfere with the rights of a manufacturer or distributor from entering into contractual agreements that could be construed as governing ordinary business transactions. Nothing in the Code prohibits contractual agreements between members of the same tier who hold the same licenses and permits. Effective 6-14-13.

Although this new legislation has resulted in many discussions about legislative intent and the precise meaning of language in the bill, there have been no complaints filed and no contractual agreements called into question.

HB 3307 by Geren defines alternating brewery proprietorship and contract brewing arrangement and authorizes brewers, nonresident brewers, manufacturers and nonresident manufacturers to engage in these activities, removing the requirement that they have been in business on May 1, 2005. A bond is required for an entity involved in these activities that does not own a fee interest in a brewing facility.

A brewer, nonresident brewer, manufacturer and nonresident manufacturer shall verify to TABC on an annual basis that a brewing or manufacturing facility owned or controlled by the permit or license holder is not used to produce malt beverages primarily for a specific retailer or the retailer's affiliates. Effective 9-1-13.

TABC has issued one permit to a new brewery location in Fort Worth that we believe intends to provide contract brewing services to other entities. There may be others. There are a number of brewery locations outside of Texas that hold TABC permits and will likely participate in contract brewing.

Training was provided to Texas industry members in August 2013, and a detailed letter explaining the implementation of new laws related to malt beverages was distributed to brewers and manufacturers via e-mail, to their lobbyist, and posted on our website in December 2013.

IMPLEMENTATION OF DISTILLERY-RELATED LEGISLATION

SB 828 by Van de Putte created a Distiller's Agent's Permit for employees of a distillery so they can represent the distiller, solicit and take orders from wholesalers and conduct free tastings for consumers at package stores. Effective 9-1-13.

Although SB 828 went into effect September 1st, TABC was unable to begin issuing the new permit type until a rule was passed establishing a surcharge. The new rule went into effect October 24, 2013, and the agency has issued 32 permits since that date.

SB 905 by Van de Putte authorizes a distillery located in a wet area to sell distilled spirits manufactured by the permit holder to the ultimate consumer:

- for consumption on the licensed premises (up to 3,000 gallons annually) and
- for consumption off the premises (up to 3,500 gallons annually)
 - in unbroken packages containing no more than 750 ml
 - no more than two 750 ml bottles or the equivalent to the same consumer in a 30-day period.

Hours of sale are the same as a mixed beverage or package store permit, depending on whether sale is for on- or off-premises consumption. No shipping or delivery or buying for someone else. The bottle must “bear a notice affixed to the bottle that” says the bottle is commemorative, states the month and year the bottle is sold and is signed by an agent/employee of the permit holder. Effective 9-1-13.

We have received several questions about how the wet/dry issue of the location plays into the distillery’s ability to sell for on-premise consumption. However, we have not received any complaints related to the new authority distillers have been granted.

Training was provided to industry members in August 2013. Additional training specific to Texas distillers was provided in October 2013. A detailed letter explaining the implementation of new laws related to distillers was distributed to distillers via e-mail, to their lobbyist, and posted on our website in December 2013.

IMPLEMENTATION OF OTHER LEGISLATION

HB 2806 by Geren states that a retail/winery account is not “delinquent” if the payment is received by the wholesaler not later than the fourth business day after the date payment is due under the credit law system. Effective 6-14-13.

An issue has arisen regarding how to handle payments received after the fourth business day if they are paid by a check that has insufficient funds. In the past, if a payment had not been made by the due date, it would have to be made by cash or cash equivalent to prevent a bounced check after it was too late to add the entity to the delinquent list. Under the new law, because the payment is not delinquent until four days after the due date, it does not provide the additional time necessary to discover a check has bounced and report the retailer to TABC to be placed on the delinquent list. TABC and industry parties are working together to resolve this issue through rulemaking and possibly a change in TABC's reporting system.

HB 2818 by Sheffield changed the statutes regarding the effect of local option elections. Current law states that if a justice precinct (JP) holds an election, the only way to over-ride that election is to hold a subsequent election within the same boundaries of the JP at the time of the first election, even if the boundaries have changed or the precinct no longer exists. HB 2818 authorizes a new election to be held using the current justice precinct boundaries.

HB 2818 also authorizes the issuance of wine and beer retailer (on- and off-premise) permits (BGs), retail dealer's on-premises licenses (BEs), or late hours licenses (BLs), in an area that has approved the sale of mixed beverages (spirits, wine, and beer for on-premises consumption), and approved the sale of wine and beer for off-premises consumption.

Finally, HB 2818 authorizes the issuance of wine and beer retailer (on- and off-premise) permits (BGs), retail dealer's on-premises licenses (BEs), or late hours licenses (BLs), to restaurants that hold a Food and Beverage Certificate in an area that has approved the sale of mixed beverages in a restaurant that holds a Food and Beverage Certificate and approved the sale of wine and beer for off-premises consumption. Effective 9-1-13.

No significant issues have arisen from this legislation.

SB 1035 by Carona was intended to streamline the licensing process by 1) having license applicants pay state fees directly to TABC instead of the county tax assessor-collector; 2) eliminating the requirement of hearings before the county judge in non-contested cases (no protests) but increasing the fee from \$5 to \$25; 3) codifying the practice of TABC giving 5% of the license fee to the county; 4) requiring that notice of application be posted in a newspaper by the applicant instead of the county clerk. Effective 9-1-13.

TABC has been meeting with city and county clerks, judges and tax assessor collectors training employees on the new license process. We are on target to begin collecting fees from beer license applicants on February 1, 2014.

HB 3572 by Rep. Hildebrand

Effective January 1, 2014, a new law went into effect regarding mixed beverage gross receipts taxes. HB 3572 reduced the mixed beverage gross receipts tax from 14% to 6.7%. This tax is included in the drink price and paid by the permit holder. The bill also created a new 8.25% "mixed beverage sales tax" which is charged to the consumer on top of the drink price. As patrons have begun seeing this new tax on receipts, they have contacted TABC asking questions. We are responding with a brief explanation and directing them to the Comptroller's website for a more in-depth explanation.

SIGNIFICANT EVENTS

Agency Revenue

During the FY 12-13 Biennium, TABC met the Biennial Revenue Estimate (BRE) in July – a month ahead of time. For the FY 12-13 biennium, the agency BRE was \$119.80 million, and the agency collected \$140.4 million in revenue. The excess revenue collected stays in General Revenue to fund other state agency programs.

FY12 – BRE \$68.4 million at 8/31/12 actual - \$75.8 million

FY13 – BRE \$51.4 million at 8/31/13 actual – \$64.6 million

As shown below, the first year of the biennium consistently produces more revenue because more two-year permits are renewed during the first year of the biennium.

Galveston Ports of Entry Tax Collection

On January 4, 2014, for the first time, cruise travelers disembarking out of the Port of Galveston were asked to pay a tax for alcoholic beverages and cigarettes that were purchased either on the ship's duty free store or at a foreign port of call. TABC currently operates 20 ports of entry collection facilities along the Texas-Mexico border where the tax is presently collected on alcoholic beverages and cigarettes imported into the state. During the recent legislative session, the agency was appropriated funding to begin tax collection of imported alcoholic beverages and cigarettes from seaport facilities. The Galveston Port facility will be the first seaport location where this tax will be collected with plans to extend to the Houston-Bayport facility in the fall of 2014.

Section 107.07 of the Alcoholic Beverage Code, in effect for over 40 years, requires that each adult (21 years old and over) importing alcoholic beverages into the state for personal consumption pay the state tax and an administrative fee of \$3.00. The law limits personal importation by an adult to once every 30 days with limits of: 1 gallon of distilled spirits, 3 gallons of wine, and 288 ounces of malt beverages (24 12-ounce containers). Persons importing alcoholic beverages must personally accompany the product as it enters the state.

TABC personnel worked in advance with Port of Galveston and cruise line officials to ensure that the tax collection was done efficiently and with limited disruption of port operations and delays to the passengers. Details on the revenue collected during the first three months of operation will be included in the April Quarterly Report.

Label Approval

After receiving feedback from the Texas Craft Brewer's Guild regarding the amount of time the agency was taking to approve new malt beverage products, TABC hired a temporary employee to assist with the paperwork involved. The agency is investigating ways to finance an on-line label approval system which would reduce submission errors and significantly reduce the processing time. Malt beverages cannot be sold in Texas until they receive label approval from both the federal Tax and Trade Bureau and from TABC. The faster the agency can approve new products, the faster they can be sold, businesses can grow, jobs are offered, and taxes are collected.