

**Texas
Sunset
Advisory
Commission**

STAFF EVALUATION

TEXAS ALCOHOLIC BEVERAGE COMMISSION

**A Staff Report
to the
Sunset Advisory Commission**



April 1992

TEXAS ALCOHOLIC BEVERAGE COMMISSION

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SUMMARY

SUMMARY

The Texas Alcoholic Beverage Commission is subject to the Sunset Act and will be automatically abolished unless statutorily continued by the 73rd Legislature in 1993. As required by statute, the review of the agency included a determination of whether the agency fills a real and continuing need; whether there are benefits to be gained by reorganizing the agency; and finally, if current statutory policies should be changed to improve the efficiency and effectiveness of the agency.

Need for the Agency

The review concluded that the Texas Alcoholic Beverage Commission should be continued for a 12-year period and reviewed again in 2005. The primary functions of the commission to license the alcoholic beverage industry and enforce the state's array of alcoholic beverage statutes continue to be needed. This regulatory approach is common to the 32 states that do not directly sell alcoholic beverages to consumers. The 45,000 criminal and 3,600 administrative enforcement actions taken in fiscal year 1991 show a need for continued oversight of the alcoholic beverage industry.

In addition, the commission's responsibility to oversee the operation of bingo as a legal form of gambling continues to be needed. Over \$652 million was spent by patrons on bingo games in fiscal year 1991. The need for oversight of the fair operation of bingo games and the proper use of bingo proceeds for charitable purposes continues in place.

Reorganization Alternatives

As part of the review, various reorganization options were considered to determine if all or part of the agency's functions should be transferred to other agencies. The review showed that savings and a reduction in duplication could be achieved through a transfer of the TABC's tax collection and audit function to the comptroller's office. In general, the state has assigned most of its tax collection and tax audit duties to the state comptroller. The TABC, however, also has a system in place to collect and audit alcoholic beverage and bingo taxes. Over \$2.27 million per year, after the first year of implementation, could be saved by combining alcoholic beverage and bingo tax collection and audit activities with the comptroller's office.

Policymaking Body

- The policymaking structure of the agency should be changed by:
 - increasing the size of the commission to six members; and
 - establishing a citizens advisory committee and a bingo advisory committee.

Overall Administration

- The administration of the agency should be modified by:
 - increasing efforts to recruit, hire and promote minority employees; and
 - requiring the commission to set fees, in rules, to cover the costs of agency operations.

Evaluation of Programs

- The operation of the agency's programs should be improved by:
 - providing straightforward license/permit suspension authority and authorizing the use of administrative penalties;
 - strengthening the agency's ability to enforce statutes relating to the sale of alcoholic beverages to minors;
 - increasing the flexibility of the agency's audit approach and requiring interest to be paid on late tax payments;
 - eliminating the two percent tax discount given to excise taxpayers who pay on time;
 - allowing the distilled spirits and wine industries to make charitable contributions and sponsor events in a manner consistent with the beer industry;
 - transferring the agency's hearings function to the State Office of Administrative Hearings; and
 - increasing opportunities for charities that conduct bingo to boost earnings and providing the agency with a full range of sanctions to use in its bingo regulation efforts.

Fiscal Impact

Preliminary estimates indicate that the transfer of duties from the TABC to the comptroller in conjunction with the other recommendations will produce a net gain to the state of more than \$10 million per year after full implementation.

Fiscal Year	Net Gain to the General Revenue Fund
1994	\$ 601,700
1995	\$ 8,135,700
1996	\$ 9,833,700
1997	\$10,335,700
1998	\$11,378,700

BACKGROUND

CREATION AND POWERS

Following the repeal of Prohibition in 1935, the 44th Texas Legislature created the Texas Liquor Control Board to regulate the manufacture, distribution, storage, and sale of alcoholic beverages in the state. The board's initial responsibilities were to promote temperance, protect the public interest, encourage observance of the Liquor Control Act, collect alcoholic beverage taxes and discourage certain socially undesirable activities such as bootlegging, underage drinking, and organized crime. Texas, along with 31 other states, perform their regulatory functions through a system of licensure of each facet of the alcoholic beverage industry. Eighteen other states have chosen to control the sale of alcoholic beverages through state ownership of portions of the alcoholic beverage industry such as state-operated package stores.

The duties and responsibilities of the state's alcohol regulatory agency have changed and expanded over the last 47 years. In 1970, the TLCB was renamed the Texas Alcoholic Beverage Commission (TABC) and the Liquor Control Act recodified as the Alcoholic Beverage Code (ABC). In 1971, the Texas legislature passed liquor-by-the-drink legislation which allowed voters, by local option election, to determine whether mixed beverages could be sold in restaurants and bars in their area. In addition to passing liquor-by-the-drink legislation and removing the prohibition against the "open saloon", the legislature created a 10 percent gross receipts tax. The gross receipts tax is paid by the seller of mixed beverages on gross receipts from the sale and service of alcoholic beverages. The gross receipts tax was increased to 12 percent in 1984 and to 14 percent in 1990.

In 1989, the 71st Legislature transferred the administration of the Bingo Enabling Act from the Comptroller of Public Accounts to the TABC. Under the Bingo Enabling Act, the TABC is responsible for regulating the bingo industry through the issuance of licenses for charities which conduct bingo games, to individuals which lease bingo premises, and for the manufacturers and distributors of bingo products. The agency is also responsible for collecting and processing bingo taxes and fees and auditing bingo accounts.

The current responsibilities of the TABC reflect the additional tasks that have been assigned to the agency over the years. The TABC regulates the alcoholic beverage industry by controlling all types of alcoholic beverages sold in the state; monitoring the distribution of alcoholic beverages to ensure that there are no illegal business relationships between manufacturers, wholesalers, and retailers; and developing and applying regulatory controls to track the flow of alcoholic beverages from manufacturer to consumer. As mentioned above, the TABC is also responsible for enforcing the Bingo Enabling Act and regulating the bingo industry. In addition, the TABC is responsible for collecting alcoholic beverage and bingo taxes and auditing alcoholic beverage and bingo accounts to determine if the proper amount of taxes have been paid.

POLICYMAKING BODY

The Texas Alcoholic Beverage Commission consists of three members appointed by the governor with the advice and consent of the senate. The members serve staggered six-year terms and one member is designated by the governor to serve as the chairman. The statute requires that members be Texas residents for five years preceding their appointment and be qualified to vote in the state. The statute also forbids members and their spouses from having financial connections with persons in the alcoholic beverage industry, holding stocks or bonds in the industry, or having a pecuniary interest in the industry. No member may receive a commission or profit from, or have an interest in the sale or purchase of alcoholic beverages.

The powers of the commission are related to the regulation of the alcoholic beverage and bingo industries and include the authority to grant or refuse permits and licenses, to supervise and inspect all segments of the industries, to collect taxes and fees, and to investigate violations of the Alcoholic Beverage Code and assist in the prosecution of violators. The statute requires the TABC's headquarters to be located in Austin and authorizes the commission to meet as necessary. In fiscal year 1991, the commission met on 11 occasions. The part-time commission also appoints the administrator of the agency who handles the day-to-day activities of the agency.

FUNDING AND ORGANIZATION

The agency currently utilizes 710 full-time employees (FTE's) to process applications, collect and process taxes, audit accounts, and enforce the Alcoholic Beverage Code and Bingo Enabling Act. In terms of operations performed, 74 or 10 percent of all employees are involved in administration; 32 or 5 percent are in licensing; 170 or 24 percent are in tax reporting and auditing; 314 or 44 percent are in enforcement; 19 or 3 percent are in bingo, and 101 or 14 percent work at the ports of entry stations along the border. Headquarters employees make up 25 percent of the total TABC work force, while 75 percent are employed in field offices located throughout the state. The primary responsibility of the headquarters office is to collect and process taxes, and provide support for agency personnel in the field. Field personnel are responsible for the actual regulation of the alcoholic beverage and bingo industries. Exhibit A depicts how the agency's work force has changed over a five-year period in different categories of employment and how it compares with minority work force goals set in the Appropriations Act. Exhibit B shows the organizational structure of the agency.

Exhibit A
PERCENTAGE OF MINORITIES IN AGENCY'S WORK FORCE
Texas Alcoholic Beverage Commission

Job Category	1987 Total Work Force 678		1991 Total Work Force 714		1992-1993 Appropriations Act Statewide Goal for Minority Work Force Representation
	Total Positions	% Minority	Total Positions	% Minority	
Administrators	24	4.2%	14	14.3%	14%
Professionals	226	17.3%	232	18.5%	18%
Technicians	109	80.7%	132	68.9%	23%
Protective Service	175	21.1%	174	19%	48%
Para-Professional	10	40%	90	25.6%	25%
Administrative Support	132	21.2%	66	39.4%	25%
Skilled Craft	2	50%	6	33.3%	29%
Service/Maintenance	0	0	0	0	52%

The agency is divided into 11 divisions to assist the administrator in performing day-to-day activities: executive division, administrative law division, administrative services division, accounting division, auditing division, bingo division, computer services division, enforcement division, legal division, licenses and permits division, and ports of entry division. The headquarters office in Austin provides basic support services for the agency including human resources, internal accounting, computer services, legal services and coordinates licensing, tax collection, auditing, and enforcement efforts throughout the state.

The district offices serve as the local arm of the TABC and perform enforcement and auditing activities necessary to regulate the alcoholic beverage and bingo industries. The auditing district offices are responsible for inspecting and auditing tax accounts selected by the headquarters office. District audit supervisors may also select additional accounts which are identified by auditors as having possible tax liabilities. The enforcement offices in the districts conduct routine inspections of licensed and permitted businesses, respond to complaints, and take applications for licenses and permits. The enforcement district offices also ensure that taxes are paid by serving suspensions on license and permit accounts which are delinquent in tax payment. To facilitate the enforcement of the Alcoholic Beverage Code and the Bingo Enabling Act and the collection of alcoholic beverage and bingo taxes, agency personnel are located in 21 enforcement districts, 12 auditing districts and nine ports of entry stations located along the Texas-Mexico border. Exhibits C and D show the location of auditing and enforcement offices throughout the state.

Exhibit B
ORGANIZATIONAL CHART
Texas Alcoholic Beverage Commission
FY 1991

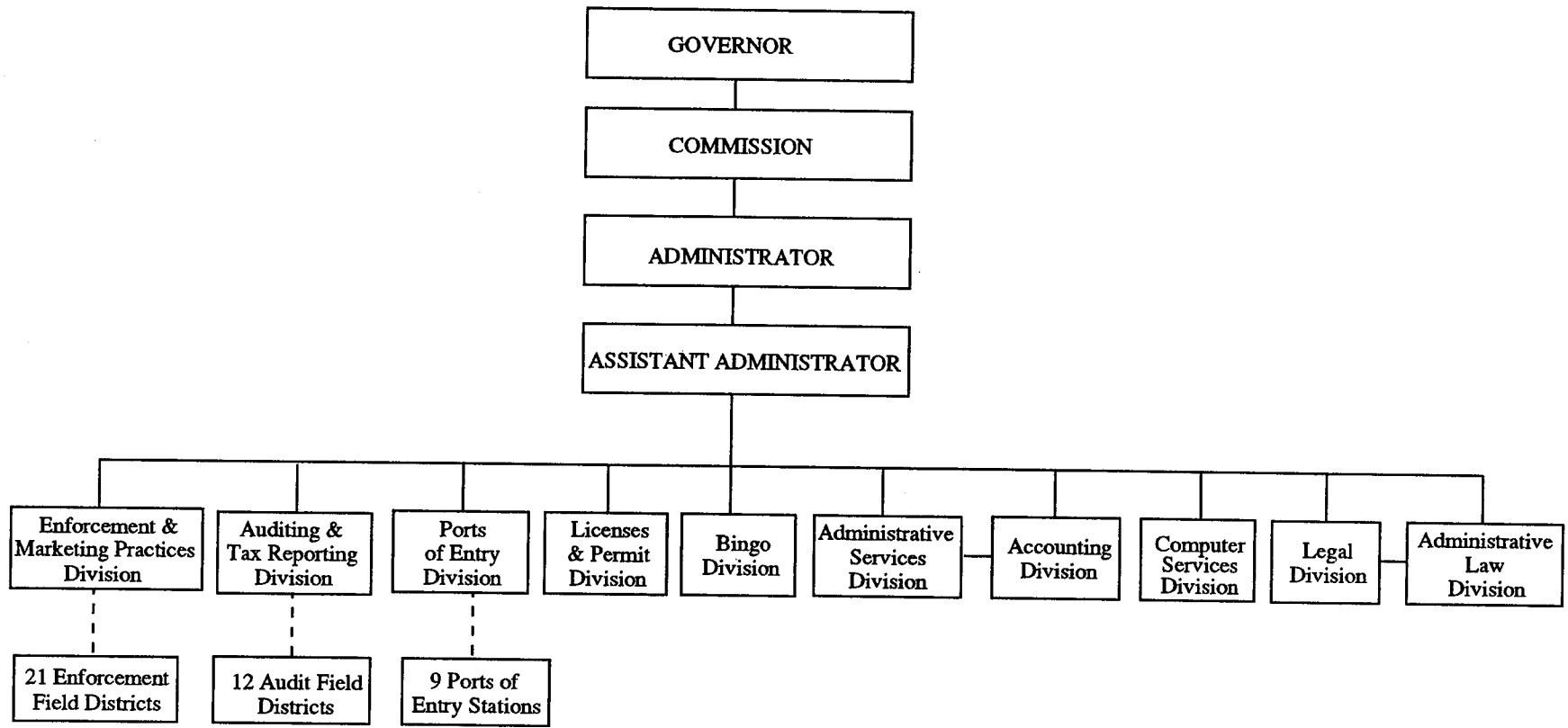
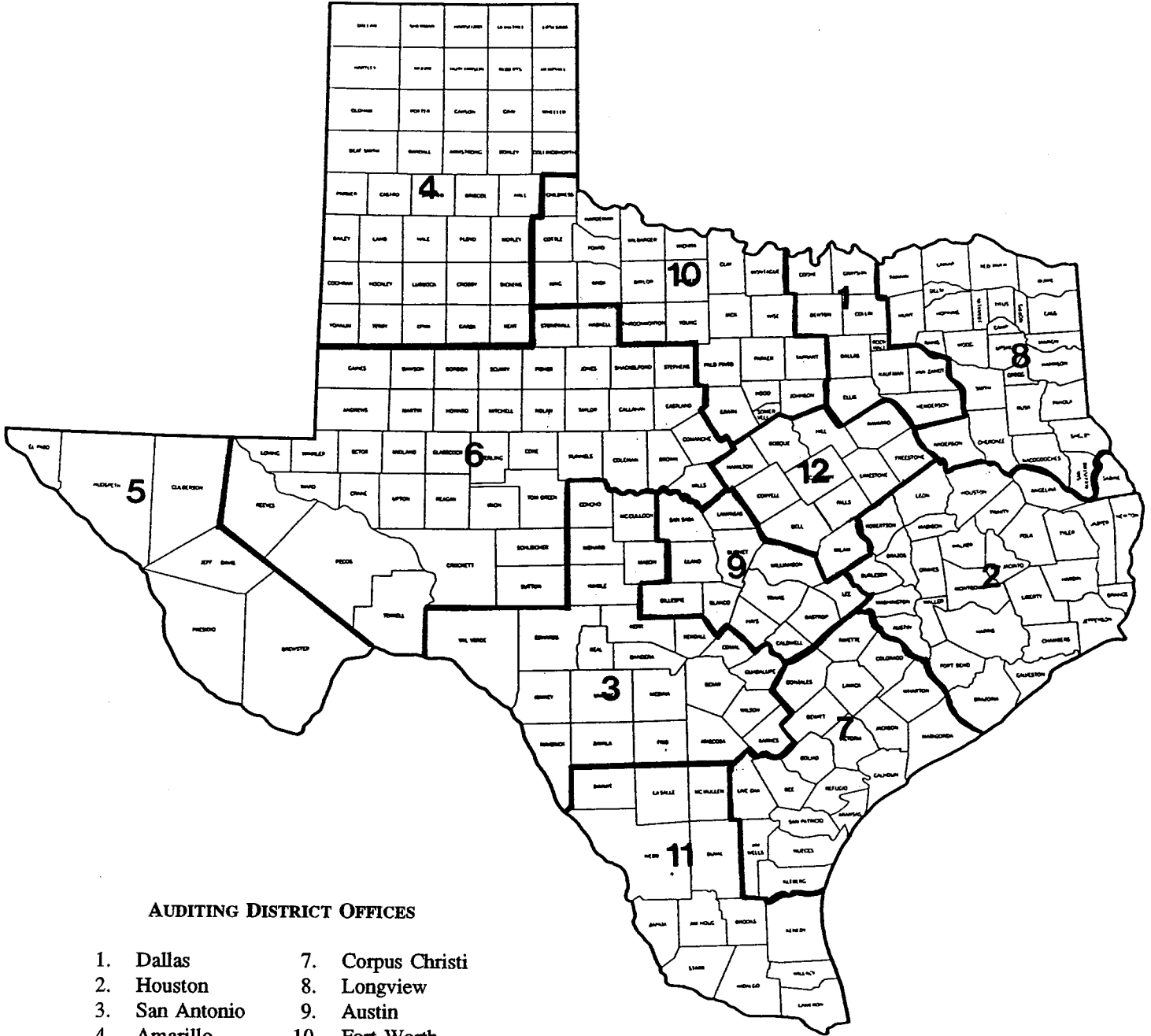


Exhibit C
LOCATION OF AUDITING DISTRICT OFFICES
Texas Alcoholic Beverage Commission



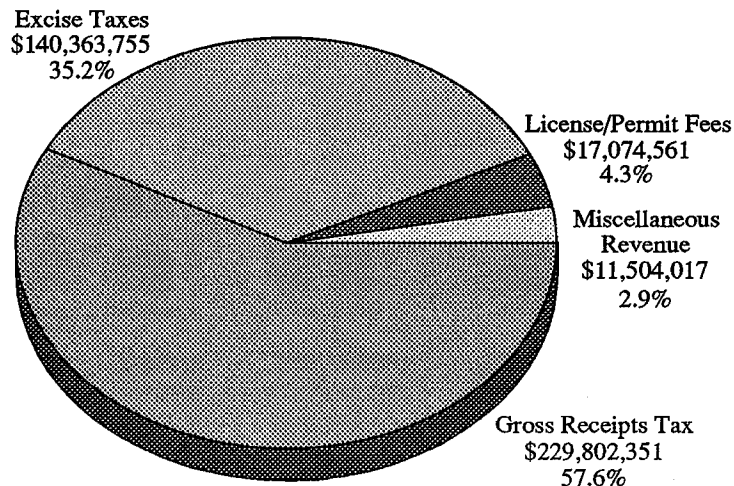
AUDITING DISTRICT OFFICES

- | | |
|----------------|-------------------|
| 1. Dallas | 7. Corpus Christi |
| 2. Houston | 8. Longview |
| 3. San Antonio | 9. Austin |
| 4. Amarillo | 10. Fort Worth |
| 5. El Paso | 11. McAllen |
| 6. Odessa | 12. Waco |

In fiscal year 1991, the TABC collected \$398,744,684 in revenues derived from gross receipts taxes on mixed beverages; excise taxes on beer, wine and distilled liquor; fees from licenses and permits; and revenue collected on alcoholic beverages imported across the Mexican border. The mixed beverage tax, a 14 percent gross receipts tax on the sale of mixed beverages, is the TABC's largest source of revenue totalling more than \$229 million in fiscal year 1991. Revenues from the mixed beverage tax are divided among the state, county and city. Approximately 78.6 percent of mixed beverage tax revenues are deposited in the state treasury, 10.7 percent is paid to the county in which the account is located, and 10.7 percent is paid to the incorporated city or town. Three-fourths of the amount allocated to the state is deposited in the general revenue fund and the remaining one-fourth is allocated to the available school fund.

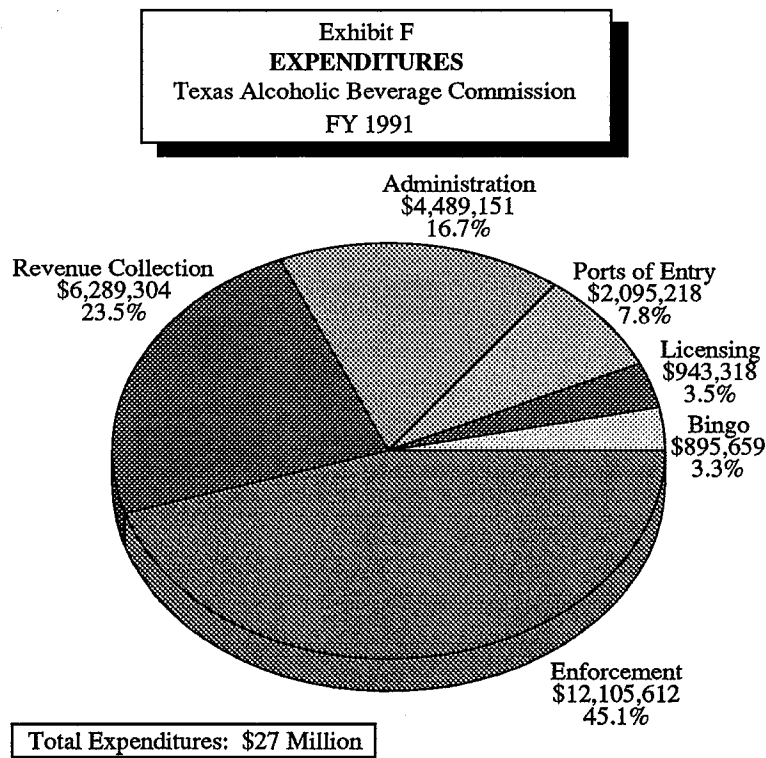
The second largest source of tax revenue is the state excise tax which is paid by liquor wholesalers and beer distributors and is based on the volume of alcoholic beverage that passes through these businesses. The agency collects excise taxes on distilled spirits, wine, malt liquor, and beer. The excise tax generated more than \$140 million in fiscal year 1991. Over \$17 million was generated from license and permit fees for alcoholic beverages. Miscellaneous revenue, consisting of interest, fines, various fees, and gross receipts taxes collected from audits, totalled \$11.5 million in fiscal year 1991. Exhibit E shows revenues collected by the agency in fiscal year 1991. In fiscal year 1991, the TABC also collected \$3.2 million in bingo license and permit fees and generated \$21.2 million from the seven percent gross receipts tax on bingo games. Because of the recent transfer of the regulation of bingo to the TABC, no revenue from bingo was included as a source of revenue for the TABC in 1991.

Exhibit E
SOURCE OF REVENUES
 Texas Alcoholic Beverage Commission
 FY 1991



Total Revenues: \$399 Million

In fiscal year 1991, the TABC received appropriations of \$27.3 million from the general revenue fund and expended about \$27 million to perform the agency's functions. The Texas Alcoholic Beverage Commission expenditures can be divided into six programs: enforcement, tax reporting and auditing, administration, ports-of-entry, bingo, and licensing. The enforcement division was the commission's largest area of expenditure totalling \$12.1 million or 45.1 percent of expenditures. The revenue collection program which includes the tax reporting and auditing divisions was next with expenditures of \$6.3 million or 23.5 percent of expenditures. The agency expended \$4.5 million on the administration program which includes the executive, administrative law, administrative services, computer services, legal and accounting divisions. The agency also expended \$2.1 million on the ports of entry division, \$896,000 on the bingo division and \$943,000 on the licensing division. Exhibit F shows the TABC's expenditures for fiscal year 1991.



PROGRAMS AND FUNCTIONS

As discussed previously, the Texas Alcoholic Beverage Commission is responsible for regulating the alcoholic beverage industry through the issuance of licenses and permits and the inspection of businesses involved in the manufacture, distribution, and sale of alcoholic beverages. The agency also enforces provisions of the Alcoholic Beverage Code, collects and processes gross receipts and excise taxes, and audits alcoholic beverage accounts. In addition to regulating the alcoholic beverage industry, the agency also licenses bingo operators, lessors, and manufacturers and distributors of bingo products, enforces the Bingo Enabling Act, collects

and processes bingo taxes, and audits bingo accounts. The following sections describe how the alcoholic beverage industry is organized in Texas and the United States and how the TABC regulates the alcoholic beverage and bingo industries in the state.

Three-Tiered System

The alcoholic beverage industry in Texas and throughout the United States consists of three distinct levels: manufacturing, wholesale or distribution, and retailers. Provisions in the Texas Alcoholic Beverage Code are designed to prevent "tied house" relationships from developing between the different levels. A tied house relationship, which was legal in the United States before prohibition, is a condition where a manufacturer has overlapping ownership, influence and control of the wholesale and retail levels of the alcoholic beverage industry. In these cases, a manufacturer can require retailers to sell only that manufacturer's brands and products, to the exclusion of other manufacturer's brands and products. Tied house relationships allow a manufacturer to dominate one segment of the marketplace thereby eliminating competition between companies. Tied house relationships can result in fewer brands and products being available in the marketplace and higher prices for the consumer. Tied houses currently exist in England where the brewery owns the retail outlets and requires these outlets to sell the brewery's brands to the exclusion of others, at prices set by the brewery.

As an extension of the tied house prohibitions, provisions of the Alcoholic Beverage Code and the TABC rules are designed to ensure that no level of the industry, specifically the manufacturer, wholesaler or distributor, exerts undue influence on another level, primarily the retailer. For example, no "services" may be provided to the retailer from the wholesaler which would induce the retailer to purchase a particular brand of liquor or beer over those provided by another wholesaler who does not offer such services. By maintaining a distinct three level system, the Alcoholic Beverage Code prevents any intra-industry relationships that could result in undesirable trade practices such as restrictions on trade.

The regulation of bingo also includes this three-tier concept. For example, manufacturers and distributors of bingo supplies may not receive a license as both a manufacturer and distributor. Also, manufacturers and distributors may not be involved in the conduct, administration, and promotion of any game of bingo.

The work of the TABC is aimed at making sure that the balance of the three-tier system is maintained. The agency has six major programs that carry out the day-to-day effort, monitoring the activities of the businesses in each tier. The work of each of the major programs is discussed below.

Major Programs

The following section describes the agency's major programs which include licensing, revenue collection, and enforcement. Generally, the headquarters office in Austin provides overall policy direction, planning and technical assistance where needed, while the field offices provide the actual regulatory functions.

Licensing

In Texas, the alcoholic beverage industry is regulated through a licensing system which controls the flow of alcoholic beverages from manufacture to the consumer. The licensing division processes applications for and issues 55 different types of licenses and permits. Licenses and permits are differentiated by the type of business to which they are issued. Permits are issued to businesses that manufacture, distribute, or sell beer and to establishments that sell liquor by the drink. Licenses are issued to businesses that produce, transport, distribute or sell liquor or wine. Major licenses include the general distributor's license and the manufacturer's license. Major permits include the mixed beverage permit, the private club permit, and the wholesaler's permit.

Licensing and Permit Division. The licensing division is responsible for processing and issuing all alcoholic beverage licenses and permits in the state and ensuring that alcoholic beverage accounts maintain tax security, if necessary. In order to issue a license or permit, the division evaluates each applicant to determine if the applicant is statutorily qualified to hold a license or permit and if the place of business is in adherence with all applicable statutory and regulatory requirements. The division checks applicants to ensure that residency and age requirements are met and performs a background check to determine if the applicant would be precluded from receiving a license or permit based on the applicant's criminal record. The division also requires each applicant to obtain a bond, certificate of deposit, or letter of credit as collateral against any delinquent taxes that may be incurred. For alcoholic beverage licenses and permits, the applicant must also place a public notice in a local newspaper and meet local requirements relating to alcoholic beverage establishments. Barring any discoveries that would disqualify an applicant, the application is generally approved by the licensing division in four to six weeks. In fiscal year 1991, the division issued more than 83,000 new and renewed licenses and permits. During the same year, the licensing division expended \$943,000 and generated \$17.1 million in fee revenue. The licensing division is located in the TABC's Austin headquarters and currently has 32 employees.

Revenue Collection

The Texas Alcoholic Beverage Commission is responsible for collecting taxes and fees due the state from the sale, service and handling of alcoholic beverages by licensees and permittees and for auditing these accounts to ensure that the proper amount of taxes and fees have been remitted to the state. In addition, the agency is responsible for collecting taxes and fees related to bingo, auditing these accounts, and monitoring the income, expenses, and charitable distributions of organizations licensed to conduct bingo games. These responsibilities are divided between the tax reporting division and the auditing division which are included in the revenue collection program. The revenue collection program has 170 employees and expended \$6.3 million in fiscal year 1991.

Tax Reporting Division. The tax reporting division tracks the monthly reports received from licensees and permittees to determine which accounts did not file monthly reports and taxes, which accounts filed reports after the due dates, and which accounts filed incomplete reports. After determining the status of an account, the tax reporting division takes the appropriate action to collect delinquent reports, payments, late penalties, or any information required but not furnished. If the gross receipts tax payments are late, the commission can charge a late penalty and in cases of non-payment can issue an order for summary suspension of the permit. Excise taxes, like the gross receipts taxes, are due on the 15th of each month accompanied by reports documenting purchases and sales. Excise tax accounts receive a two percent discount for paying on time and there is no penalty for late payment. The agency may take administrative action to suspend or cancel licenses or permits for failure to pay excise taxes. If taxes are not paid or are regularly paid late, the tax reporting division can request that the auditing division conduct an audit of the delinquent account. The tax reporting division has 18 employees and expended \$498,528 in fiscal year 1991.

Audit Division. The audit division audits the operating reports and accounting records of licensees and permittees to identify whether or not there are taxes owed to the state, to discourage bootlegging of alcoholic beverages, and to ensure that the proceeds from bingo games are being distributed in a manner consistent with the Bingo Enabling Act. Audits are assigned to the districts each week by the auditing division in the headquarters office and scheduled by the districts based on their risk of delinquency. The agency uses an audit select procedure to identify accounts with the highest risk. The district audit supervisor can also schedule an audit if an account is identified as having a high probability of delinquent taxes. The auditing division conducts several different types of audits based on status of the permit, type of account, risk, and tax liability. Desktop inspections are performed on low risk and low liability (less than \$4,000 in gross receipts per month) accounts. Compliance and record audits are on-site audits which involve an examination of purchase and sales receipts and inventory levels and a trial depletion analysis. These audits are performed on accounts with gross receipts in excess of \$4,000 per month. In fiscal year 1991, the audit division conducted 7,172 audits of various types and identified \$7.78 million in delinquent taxes. The audit division has 15 employees in the headquarters office and 137 employees located in 12 audit districts throughout the state. In fiscal year 1991, the audit division expended \$5.8 million.

Enforcement

The TABC is responsible for enforcing the Alcoholic Beverage Code (ABC) which governs the manufacture, distribution, and sale of alcoholic beverages, as well as the advertising and marketing of alcoholic beverage products in Texas.

Enforcement Division. The enforcement division conducts routine inspections, responds to complaints, and conducts undercover investigations to ensure that all licensed and permitted premises are in compliance with the ABC as well as with other state laws. The division's top priorities are enforcing laws related to the purchase and consumption of alcoholic beverages by minors and intoxicated persons, taxation and tax issues, and the intra-industry relationships. The enforcement division strives to work closely with all segments of the regulated community to

obtain voluntary compliance with the laws and rules. When voluntary compliance cannot be secured, the agency can take administrative action against violators. The agency has the powers to warn, suspend or fine, and to cancel a permit or license. In addition, the agency refers enforcement cases involving criminal violations of the Texas Alcoholic Beverage Code and the Penal Code to local district courts for adjudication.

The marketing practices section within the enforcement division is responsible for enforcing provisions in the ABC related to the promotion and sale of alcoholic beverages in the state. These provisions are designed to ensure that the advertising and promotional activities of the alcoholic beverage industry do not unduly promote the consumption of alcoholic beverages. These laws also guard against circumvention of the three-tiered system by inducing a retail establishment to sell a specific brand or product to the exclusion of other manufacturers' brands or products. The section carries out its responsibility by approving and investigating, when necessary, the advertising practices of the industry including the use of outdoor signs, novelty advertisement, indoor signs and displays in retail establishments, and sponsorship of events by beer manufacturers and wholesalers. In addition, the marketing practices section evaluates bottle labels submitted to the agency for approval based on criteria in code. This section also operates a laboratory to test the chemical makeup and size of products offered for sale in the state to ensure that the products are safe and meet the TABC rules and requirements.

In fiscal year 1991, the enforcement division conducted almost 136,000 inspections of licensed premises, investigated 7,813 complaints, and filed 3,679 administrative and 45,755 criminal cases made under provisions of the Alcoholic Beverage and Penal Codes. The division collected \$1,690,700 in fines which were deposited in the general revenue fund. The division has 314 employees including 244 commissioned peace officers. Twenty-two employees are located in the headquarters office and 292 employees are located in the division's 21 districts. The enforcement division expended \$12,105,612 in fiscal year 1991.

Ports of Entry

The ports of entry program is responsible for ensuring that state excise taxes are paid on all alcoholic beverages imported into the state from Mexico and that all provisions of the Alcoholic Beverage Code pertaining to the importation and possession of alcoholic beverages are followed.

Ports of Entry Division. The ports of entry division collects excise taxes on alcoholic beverage products entering the state from Mexico. The division also collects an importation fee of \$.50 per importation and affixes tax stamps on liquor over the tax-free limit. In cooperation with the state treasurer's office, the division staff also affix tax stamps on cartons of cigarettes. In fiscal year 1991, the TABC confiscated and destroyed 7,137 containers of alcoholic beverages for the following reasons: unlawful size, excessive amounts, intoxicated persons transporting liquor, refusal by persons to pay taxes, smuggling, and possession by persons under the age of 21. In fiscal year 1991, the ports of entry division expended \$2,095,218 and collected \$2,941,704 in revenues (administrative fees and taxes). The agency has 101 employees assigned to nine ports of entry stations located along the Texas/Mexico border from Brownsville to El Paso.

Bingo

In 1981, the legislature passed the Bingo Enabling Act which made bingo legal to raise funds for charitable purposes in Texas, with certain restrictions. Originally the bingo industry was regulated by the comptroller's office, but in 1989 the legislature transferred the enforcement of the Bingo Enabling Act and regulation of the bingo industry from the comptroller's office to the Texas Alcoholic Beverage Commission.

Bingo Division. The bingo division, with the assistance of the enforcement and auditing divisions, is responsible for the enforcement of the Bingo Enabling Act and regulation of the bingo industry. This involves issuing licenses to qualified charities, lessors, and the manufacturers and distributors of bingo products. The division also ensures that funds generated by bingo are appropriately distributed to charities and the state. Similar to the alcoholic beverage industry, applications for charities are taken in the district offices and licenses are issued by the headquarters office in Austin. Bingo taxes and fees are collected and processed by the accounting division and bingo compliance section, and audits of bingo accounts are conducted by the audit division. The bingo division has 19 employees and expended \$895,659 in fiscal year 1991. During the same year, the division collected \$21,219,322 in bingo gross receipts taxes and \$3,282,840 in license fees.

Administration

The agency's administrative activity is composed of the executive division, the administrative services division, the computer services division, and the administrative law and legal divisions. These divisions are responsible for providing the day-to-day support services required to operate the agency, allocating resources such as personnel and equipment, and exercising executive control over agency functions.

Executive Division. The executive division includes the administrator and staff, and activities such as the personnel office, equal employment opportunity coordinator, internal affairs unit and the internal auditor. The internal auditor is responsible for conducting independent reviews and evaluations of agency activities and furnishing the agency with appraisals, recommendations and information on activities reviewed. The Texas Alcoholic Beverage Commission is subject to the state's Internal Audit Act and the internal audit function complies with requirements in the act. The executive division is also responsible for developing a six-year strategic plan for the agency. During the 72nd Regular Session, the legislature passed legislation requiring most state agencies to develop a six-year strategic plan. The strategic plans are the first step in building a long-term statewide budgeting and planning process. The agency is presently working on its strategic plan which is required to be completed by June 1, 1992. The completed plan will be submitted to the governor, lieutenant governor, speaker of the house of representatives and several legislative oversight agencies, including the Sunset Advisory Commission. There are 11 employees in the executive division and in fiscal year 1991, the division expended \$605,023.

Administrative Services Division. The administrative services division includes housekeeping functions such as the print shop, supply room, maintenance of lease and inventory records, and the purchasing of equipment and supplies. Included in the administrative services program is the accounting division which is responsible for depositing all revenue received by the agency in the state treasury, paying the agency's bills, recording and tracking fleet expenses for the agency's 313 vehicles, processing all refunds, accounting for the seizure and disposition of alcoholic beverages by enforcement personnel, and paying all employee travel expenses. The accounting function is also responsible for maintaining accounting records and for preparing all fiscal reports. The revenue collection section of the accounting function processes and deposits tax remittances in the state treasury, and distributes the tax reports which accompany tax payments to the tax reporting division. In fiscal year 1991, the revenue collection section processed more than 122,000 tax and fee transactions valued at more than \$398 million and expended \$1.45 million. There are 29 employees in the administrative services division.

Computer Services Division. The computer services division maintains a database of all licenses and permits which includes records of tax payments, violations, hearings, and ownership interests. The division is also responsible for the printing of all licenses and permits and various agency reports. In fiscal year 1991, the division expended \$1.8 million and currently employs 22 staff.

Administrative Law Division and Legal Division. The hearings process, administered by the administrative law and legal divisions, prepares and adjudicates violations of the agency's statute and rules. The legal division is responsible for preparing and prosecuting administrative cases dealing with violations of the Alcoholic Beverage Code or Bingo Enabling Act. The staff of the administrative law division act as hearings examiners and conducts the hearings. Each examiner makes a written "proposal of decision" regarding the case to the agency administrator for final decision. This decision is appealable to the district court in the county in which the licensee or permittee resides. In fiscal year 1991, the administrative law division and legal division conducted 492 hearings and expended \$468,254. The hearings process for the TABC is currently conducted by 12 employees.

***FINDINGS AND
RECOMMENDATIONS***

OVERALL APPROACH TO REVIEW

OVERALL APPROACH TO THE REVIEW

The Sunset Act requires an assessment of several factors as part of an agency's review. These factors include a determination of the continued need for the functions performed by the agency; a determination if those functions could be better performed by another agency; whether functions performed by another agency could be better performed by the agency under review; and, finally, a determination of the need for any changes in the agency's statute.

In accordance with the Sunset Act, the review of the Texas Alcoholic Beverage Commission included an assessment of the need to continue the functions performed by the agency; whether benefits would be gained by combining any of the functions of the agency with those of another organization; and finally, if the functions are continued in their present form, whether changes are needed to improve the efficiency and effectiveness of the agency.

The need for agency functions focused on whether continued state involvement in the regulation of alcoholic beverages and bingo was necessary. The review then examined whether benefits would result from merging the agency or any particular function of the agency with another state agency. The remainder of the report details changes needed if the agency is maintained in its current form.

To make determinations in each of these review areas the review team was involved in a number of activities over the six month review period. These activities included:

- review of agency documents, legislative reports, other states' reports and statutes, previous evaluations of agency activities, and literature containing background material;
- interviews with key agency staff both in the central office and district enforcement and audit offices;
- attendance at meetings and public hearings of the Texas Alcoholic Beverage Commission;
- phone and personal interviews with individuals involved in many of the differing levels of the alcoholic beverage industry; national alcoholic beverage regulation organizations, federal officials, and other states' alcoholic beverage and bingo regulatory agencies;
- a survey of the agency's employees requesting the identification of problems in the agency as well as potential solutions; and

- interviews and meetings with groups affected by or interested in the activities and policies of the agency including bingo conductors and lessors and groups representing efforts to reduce incidents of driving while intoxicated, school groups, manufacturers, distributors, and retailers of alcoholic beverage products and others.

Out of these activities, the overall focus of the review took shape. A good deal of the organizational and regulatory structure that the agency uses today was developed in the 1930s and 40s. The review focused on the following questions: Does the state's approach to regulating the alcoholic beverage and bingo industries meet modern standards for organization and funding? Does the state have an effective balance of enforcement tools to ensure that alcohol and bingo related businesses operate in a manner consistent with public expectations?

The recommendations included in the report represent only a small percentage of the total number of issues that were raised during the review process. Many of the issues raised were management issues and could not be resolved through a change in statute. This type of issue was left to other legislative oversight agencies to deal with. The policy issues finally selected were based on their relative importance to the statutory structure of the agency and represent a good faith effort to balance the competing interests inherent in the issues surrounding the regulation of the alcoholic beverage and bingo industries.

NEED FOR THE AGENCY

ISSUE 1: The Texas Alcoholic Beverage Commission should be continued for a 12-year period.

BACKGROUND

The Texas Alcoholic Beverage Commission (TABC) was created in 1935 to regulate the manufacture, distribution, storage and sale of alcoholic beverages in the state. Since that time, the agency's duties have expanded to include the responsibility for the regulation of bingo in Texas. While the responsibilities of the agency have expanded over time, the main objectives of the agency have remained essentially the same.

To accomplish its objectives, the agency performs three major functions. First, the agency is responsible for licensing all facets of the alcoholic beverage and bingo industries to ensure that persons involved meet all requirements of the Alcoholic Beverage Code and the Bingo Enabling Act. The second function is the collection and auditing of all alcoholic beverage and bingo taxes. The third major function of the agency is its enforcement efforts to ensure that requirements of the respective statutes are met, with the primary goal being protection of the health, safety and welfare of the citizens of the state.

In fiscal year 1991, the agency was responsible for overseeing the activities of some 83,000 licensees and permittees and collected about \$378 million in alcoholic beverage taxes. A majority of the alcoholic beverage taxpayer accounts were audited during this time period, resulting in the identification of approximately \$7.78 million in deficient taxes in fiscal year 1991. In addition, enforcement efforts in fiscal year 1991 resulted in over 3,000 suspensions of licenses and permits and almost \$1.7 million in fines collected for violations of the Alcoholic Beverage Code.

To justify the continuation of an agency's functions, certain broad conditions should exist. First, a current and continuing need should exist for the state to provide the functions or services. In addition, the functions should not duplicate those currently provided by any other agency. Finally, the potential benefits must outweigh any disadvantages of transferring the agency's functions or services to any other state agency. The evaluation of the need to continue the department's functions led to several findings which are discussed in the following material.

FINDINGS

- ▶ **The primary functions of the agency to regulate all facets of the alcoholic beverage industry and the bingo industry continue to be important state concerns.**

- The agency estimates that in 1990 over 9.3 million gallons of distilled spirits, 26.4 million gallons of wine and 459 million gallons of beer were consumed in Texas. Taxes due on the production and sale of alcoholic beverages total several hundred million dollars annually. The functions of tax collection and audit continue to be needed to ensure the state's proper receipt of taxes due from the alcoholic beverage industry.
 - In fiscal year 1991, the agency's enforcement effort resulted in over 3,600 administrative cases being pursued against licensees and permittees and over 45,000 criminal citations being issued. Some of the violations addressed by these cases included gambling or drug dealing in alcoholic beverage establishments, sale of untaxed liquor, sale of alcoholic beverages to minors, and violations of restrictions on the placement of signs. The number of alcoholic beverage violations that continue to be found indicates that the enforcement function is needed to ensure the safety of the public.
 - One serious problem related to the sale and consumption of alcoholic beverages concerns their use by minors. The TABC reports that almost 27,700 minors were cited by the agency for possession of alcoholic beverages during fiscal year 1991. Driving while intoxicated is also a serious problem in the state. The Department of Public Safety reports that over 40 percent of all traffic fatalities were alcohol-related in 1991. The TABC is the only agency that has the direct responsibility to regulate businesses responsible for the sale of alcoholic beverages to minors and intoxicated persons.
 - The use of bingo as a fundraising activity for charities is a significant financial concern. Over \$652 million was spent by patrons on bingo games in fiscal year 1991. In addition, there were 1,788 charities licensed to conduct bingo games in the state in fiscal year 1991. A need continues to exist for state oversight to ensure that prizes are properly awarded, taxes are fully paid and charities receive their appropriate share of bingo proceeds.
- ▶ **An examination of the agency's major functions, licensing, enforcement, tax collection and auditing led to the conclusion that the tax collection and auditing functions could be combined with another agency.**
- No agency was identified that could perform the TABC licensing functions at a lower cost. Several state agencies perform business licensing functions. For example, the Texas Department of Licensing and Regulation (TDLR) licenses several types of businesses. Transferring the alcoholic beverage and bingo licensing activities to TDLR would not result

in cost savings because a similar number of staff would still be needed to perform the current activities.

- Alcoholic beverage enforcement activities should remain in the TABC. Although counties, cities and the Department of Public Safety (DPS) are authorized to enforce criminal violations related to alcohol, they are not equipped or funded to carry out most of the agency's enforcement functions. In addition, these agencies are not involved in the business regulation aspects of the TABC.
- The TABC's tax collection and auditing activities could be effectively performed by another state agency. The state has developed a policy where one agency, the Office of the State Comptroller, is assigned to perform the majority of the state's tax collection and tax auditing activities. An analysis of the two agencies' tax collection and audit activities showed that the activities are quite similar and could be accomplished at a lower cost at the comptroller's office.

- ▶ **While organizational structures may vary, all states use an agency or department similar to TABC to carry out their alcoholic beverage regulation activities.**

CONCLUSION

The functions currently assigned to the TABC continue to be needed and, with one exception, are appropriately placed in the agency as currently structured. Benefits could be achieved, however, from the transfer of tax collection and audit which is discussed in the next section of this report. No local entities or other state agencies were identified that could assume TABC's remaining functions with increased benefits to the state or at reduced costs.

RECOMMENDATION

- **The Texas Alcoholic Beverage Commission should be continued for a 12-year period.**

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Continuing the functions of the agency would ensure that the regulation of the manufacture, transport, distribution and sale of alcoholic beverages would continue. If the state discontinued these functions, local law enforcement would be left to perform all criminal enforcement activities related to the sale and consumption of alcoholic beverages. The administrative regulation of alcoholic beverage businesses would cease to be in place, as

would any regulation of the bingo industry. In addition, there would be a loss of almost \$400 million in tax and fee revenue collected by the TABC.

FISCAL IMPACT

If the current functions of the TABC are continued using the existing organizational structure, its annual appropriations of \$24.9 million from the general revenue fund would continue to be required.

REORGANIZATION ALTERNATIVES

ISSUE 2: The Texas Alcoholic Beverage Commission's tax administration functions including tax collection and processing, auditing and ports of entry should be transferred to the Office of the Comptroller of Public Accounts.

BACKGROUND

Many of the activities performed by the Texas Alcoholic Beverage Commission (TABC) and the comptroller's office related to tax collection and processing and auditing are similar. Both agencies are responsible for collecting and processing taxes and depositing these taxes in the state treasury. These agencies also audit taxpayer accounts to ensure that taxpayers are in compliance with tax laws and that all tax revenue owed the state is collected. Below is a brief description of how the TABC and the comptroller's office perform their tax administration duties.

TABC Duties. The TABC administers both alcoholic beverage and bingo taxes. Alcoholic beverage taxes are divided into three main categories: the mixed beverage tax, the state excise tax, and service fees. The mixed beverage tax is a 14 percent tax on the gross receipts of a mixed beverage permittee from the sale or service of alcoholic beverages. Excise taxes are paid by liquor wholesalers and beer distributors and are based on the volume (gallonage) of alcoholic beverage that is sold by the wholesaler or distributor to retailers. Service fees of \$.05 per drink are paid by airlines, cruise ships, trains, and limousines and are based on the number of drinks sold while in Texas. The agency also administers the five percent state and two percent local bingo gross receipts tax, the three percent bingo rental tax and the three percent winner's fee. In fiscal year 1991, the agency collected more than \$398 million in taxes and fees related to alcoholic beverages. During the same year, the comptroller's office collected approximately \$24.5 million in taxes and fees related to bingo. Bingo tax and fee collection duties were transferred to the TABC at the beginning of fiscal year 1992.

At the TABC, the revenue processing section of the accounting division collects alcoholic beverage and bingo taxes and fees and deposits this revenue in the state treasury. The reports accompanying the tax payments are also processed and distributed to the appropriate divisions for tracking. The agency maintains a database of all taxpayers and taxpaying accounts. There are seven employees in the revenue processing section and the section expended \$119,756 in fiscal year 1991.

The auditing and tax reporting division monitors monthly tax reports and audits alcoholic beverage and bingo accounts. The tax reporting activity monitors monthly tax reports to determine if taxpayers have completed the reports properly, paid the proper amount of taxes, and remitted payments and reports on time. The tax reporting activity also initiates enforcement action for non-payment or late payment of taxes.

The auditing activity audits alcoholic beverage accounts to ensure that taxpayers comply with all applicable tax laws and that the proper amount of taxes have been reported and paid. The agency uses an audit select procedure to identify those accounts with the highest risk and greatest probability of deficiency, although all mixed beverage accounts are audited at least once during each two-year period. Audits are assigned to the districts each week by the auditing division in the headquarters office and scheduled by the districts based on their risk. The auditing division conducts different types of audits based on the status of the permit, type of account, risk and tax liability. The majority of audits conducted by the TABC are mixed beverage account audits that involve the examination of purchase and sales records and inventory levels, and require that the auditor determine the amount of alcohol served in each mixed drink. The TABC also audits bingo gross receipts tax accounts to ensure that state and local taxes have been paid and that the proper amount of money is distributed to charity. At the end of fiscal year 1991, the tax reporting and audit division employed 177 staff in the headquarters office and in 12 audit districts and had expended \$6.3 million for the fiscal year.

The TABC operates ports of entry stations that perform tax related functions at various points along the Texas-Mexico border. These stations collect taxes and fees on alcoholic beverages imported from Mexico. Under an agreement with the treasurer's office, the TABC also collects cigarette taxes at these stations. In fiscal year 1991, the ports of entry division expended \$2.1 million and employed 105 staff.

Comptroller Duties. While the TABC administers seven taxes, the comptroller's office administers 29 taxes and collected approximately \$15.2 billion in taxes in fiscal year 1991, more than 90 percent of all tax revenue in the state. The sales tax is the largest tax administered by the comptroller's office with more than 500,000 sales tax accounts and remittances in excess of \$8 billion in taxes. The comptroller's office also administers motor fuels taxes which generated more than \$1.5 billion in fiscal year 1991, and the motor vehicle sales and use tax which generated more than \$1 billion during the same year.

Taxes remitted to the comptroller's office are processed by the revenue processing and accounting activity. Tax payments and reports are divided into groups based on the type of tax, entered into the comptroller's office computer system, and deposited in the state treasury. The revenue processing and accounting activity also determines whether taxpayers have remitted tax reports and payments in a timely and accurate manner and initiates steps to collect late or underpaid taxes. There are 165 employees involved in the revenue processing function and the comptroller's office expended \$5.78 million processing tax reports and payments in fiscal year 1991.

The comptroller's auditing division is responsible for auditing taxpayer accounts to identify taxes owed to the state and for promoting voluntary taxpayer compliance. Accounts are selected for audit by an audit select procedure that ensures those taxpayers with the greatest probability of deficiency in each area are audited first. Additional accounts are selected for audit through a random selection procedure that ensures all accounts have some probability of being selected. Audits conducted by the comptroller's office involve examination of the

taxpayers records to determine compliance with tax laws and reporting procedures. Restaurants or bars that sell beer and/or wine are subject to the sales tax instead of the gross receipts tax and are audited by the comptroller's office. Tax deficiencies are determined by the comptroller's office through financial analysis. If proper records and internal controls are not in place, the comptroller's office performs a "gross profit analysis" based on the purchases made by the business and inventory levels. This procedure is similar in some ways to the procedure used by the TABC in its alcoholic beverage gross receipts tax audits. In fiscal year 1991, the comptroller's audit division employed 732 staff and expended \$32.7 million. The comptroller's office has local audit offices located in 16 cities statewide.

While the size and volume of the activities performed by the TABC and the comptroller's office may vary, the activities themselves are very similar. The Texas Sunset Act requires that each review of an agency evaluate the extent to which the programs administered by the agency overlap or duplicate those of other agencies and the extent to which the programs administered by the agency can be consolidated with the programs of other state agencies. The TABC's and the comptroller's office's tax collecting, processing, and auditing functions were analyzed to determine whether any duplication of effort exists and, if so, whether alcoholic beverage tax and bingo tax functions could be more cost effectively performed by the comptroller's office. The approach used in other states to collect alcoholic beverage taxes was also examined. The material in the following findings sets out the results of the analysis.

FINDINGS

- ▶ **The bulk of the state's taxes are collected and audited by the comptroller of public accounts.**
 - The comptroller's office presently collects most of the state's major taxes. Some of these taxes include the state sales tax, the local sales tax, motor fuels taxes, motor vehicle sales and use tax, the oil production tax, and the natural and casinghead gas tax.
 - In terms of the state's revenue stream, the comptroller's office collected more than \$15.2 billion in taxes in fiscal year 1991. Taxes collected by the comptroller's office represented more than 90 percent of all tax revenues collected in the state.
- ▶ **In the majority of other states, the state comptroller or its equivalent collects and processes alcoholic beverage taxes and audits alcoholic beverage accounts. Enforcement of alcoholic beverage laws related to underage drinking, advertising and marketing, and criminal activity is performed by an alcoholic beverage regulatory agency.**

- The alcoholic beverage industry in different states is regulated by either a "control system" or a "license system". In control states, the state itself sells alcoholic beverages to consumers, bars and restaurants. In license states, the industry is regulated through a system of licenses and permits and is characterized by private ownership of wholesalers, distributors and package stores. Currently, there are 32 license states like Texas and 18 control states.
- In 27 of the 32 license states, the alcoholic beverage agency is organized as a licensing and enforcement agency and does not collect taxes. Alcoholic beverage taxes are collected by the Department of Revenue, the Revenue Commissioner, or the Department of Taxation. These agencies perform the same functions and duties as the comptroller's office in Texas. Only five license states impose a gross receipts tax similar to the gross receipts tax in Texas. In three of these states, the comptroller's office or its equivalent collects the gross receipts tax.
- ▶ **The Texas Alcoholic Beverage Commission and the comptroller's office perform many of the same functions related to the collection and processing of taxes.**
 - The TABC collects and processes alcoholic beverage and bingo taxes and deposits tax revenue in the state treasury. In fiscal year 1991, the agency processed approximately 122,000 reports valued at more than \$378 million. Those accounts with tax liabilities in excess of \$500,000 per year are electronically transferred to the state treasury. Taxes which are not electronically transferred to the treasury are processed by the revenue processing section of the accounting division. Tax revenue is delivered to the state treasury on a daily basis.
 - The comptroller's office administers 29 different types of taxes including a gross receipts tax on electric and telephone utilities and the sales tax on all for-profit businesses that operate in the state. The comptroller's office also collects and processes tax revenue. In fiscal year 1991, the comptroller's office processed more than 2.9 million returns and collected more than \$15.2 billion in tax and fee revenue. Like the TABC, accounts with annual liabilities in excess of \$500,000 are electronically transferred to the state treasury. Those returns which are not electronically transferred are processed by the revenue processing division. Tax returns in excess of \$4,000 receive priority status and are quickly routed through the processing function for fast deposit. Tax revenue is delivered to the treasury three to ten times daily based on the volume of returns processed.
- ▶ **Duplication of effort could be eliminated and a more balanced auditing process could be instituted through consolidation of functions.**

- Both the TABC and the comptroller's office have auditing systems composed of supervisory staff, audit staff and support staff located in a central office and in district or regional offices throughout the state. A consolidation of these two audit staffs and the merger of offices located throughout the state would result in the elimination of some supervisory and support positions. Duplicated supervisory and support positions in the central offices could also be eliminated.
- Some current auditor positions could be eliminated by cross training of auditors to perform both alcoholic beverage gross receipts tax audits and the comptroller's office's compliance audits.
- Comptroller staff indicate that, should the transfer occur, they would greatly reduce the percent of accounts audited annually. The TABC currently audits 87 percent of its alcoholic beverage gross receipts tax accounts each year. The comptroller's staff indicates 38 percent annual audit coverage may be sufficient.
- ▶ **Eighty percent of alcoholic beverage businesses must pay taxes to and may be audited by both the TABC and the comptroller's office.**
 - Eighty percent of alcoholic beverage businesses who pay either gross receipts taxes, excise taxes, service fees or membership fees to the TABC also pay sales taxes to the comptroller's office. In addition, these businesses are subject to audits by both the TABC and the comptroller's office. This is an inconvenience that could be rectified through consolidation of tax collection and audit effort.
- ▶ **A comparison of the two agencies' audit procedures did not identify any significant differences that would prevent the comptroller's office from auditing alcoholic beverage and bingo gross receipts tax accounts and alcoholic beverage excise tax accounts.**
 - Both the TABC and the comptroller's office audit a wide variety of tax accounts. The TABC audits alcoholic beverage and bingo gross receipts tax accounts, alcohol excise tax accounts, private club memberships and various types of fees. In fiscal year 1991, the TABC conducted 7,172 alcoholic beverage and bingo tax audits and identified deficiencies in excess of \$7.78 million. In comparison, the comptroller's office is required to audit the accounts of the 29 taxes it administers such as the public utility gross receipts tax, motor fuels taxes and the sales tax. In fiscal year 1991, the comptroller's office conducted 13,875 tax audits and identified deficiencies in excess of \$360 million.

- The majority of audits performed by the comptroller's office are on sales tax accounts and involve a financial audit which requires an analysis of financial statements and records. The comptroller's office does however, perform a "gross profit analysis" on beer and wine establishments that do not have adequate records or internal controls. This audit is similar to the depletion analysis audit performed by the TABC on many alcoholic beverage gross receipts tax accounts.
- Although the TABC's gross receipts tax audit and the comptroller's standard compliance audit on sales tax accounts are different, interviews with comptroller's staff indicated that it would not be difficult to train auditors from the comptroller's office or from the TABC about the different audit techniques. In addition, if the TABC audit function was transferred to the comptroller's office, many of the TABC's audit staff could be transferred to the comptroller's office to perform alcoholic beverage audits, as well as other types of audits conducted by the comptroller's office.
- ▶ **Mechanisms would continue to exist that would allow the TABC to take administrative action against licensees and permittees for failure to pay taxes after the tax collection and auditing function is transferred to the comptroller's office.**
- A system is currently in place through which the TABC is notified by the comptroller's office about beer and wine licensees that have not paid or properly paid sales taxes to the comptroller's office. The TABC then decides whether to take administrative action.
- ▶ **While auditing and enforcement functions do provide mutual support, this support can continue after a transfer if both the comptroller and the TABC want it to work.**
- Audit and enforcement personnel at the TABC share information about the activities that take place in licensed or permitted businesses. Auditors notify enforcement personnel of any illegal activities that might be discovered during an audit such as drugs or gambling. Enforcement personnel contact audit staff if they discover bottles without tax stamps or activities such as refilling bottles. These types of communications could be continued regardless of the agency that performs the activities.
- The TABC and comptroller's office have communications agreements concerning information about sales tax accounts and mixed beverage tax accounts. For example, the TABC notifies the comptroller's office of unreported door charges subject to sales tax and unreported use tax on complimentary beverages.

- Many agencies with related programs currently exchange information through a memorandum of understanding (MOU). The comptroller's office and the TABC could expand existing agreements.

CONCLUSION

The Texas Alcoholic Beverage Commission (TABC) and the comptroller's office perform many of the same functions related to collecting and processing tax revenue and auditing taxpayer accounts. An examination showed that if tax collecting and auditing functions were combined, they could be accomplished at a lower cost through elimination of duplication of effort. In addition, 80 percent of alcoholic beverage taxpayers pay taxes to and are potentially subject to audit by both agencies. The consolidation of like processes may increase the effectiveness of tax collection within state government and takes advantage of economies of scale that may exist. By combining the tax collection and processing and auditing activities of the TABC with those activities at the comptroller's office, the state could provide a more cost effective and convenient tax system to the members of both the alcoholic beverage and bingo industries.

RECOMMENDATIONS

- **The statute should be amended to transfer the tax collection and processing function, auditing function, and ports of entry function from the TABC to the comptroller's office on or before September 1, 1994. In addition, the TABC and the comptroller's office should enter into a memorandum of understanding to ensure that information gathered through both auditing and enforcement activities is shared.**

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The effective date of this transfer is proposed for September 1, 1994. This one year period can be used to work out the details of the employee transfers, space allocation, information system adjustment and other elements of the transfer process.

Under this recommendation, the TABC would continue to perform licensing and enforcement functions prescribed in the Alcoholic Beverage Code as well as bingo licensing and enforcement. However, the collection and processing of alcoholic beverage and bingo taxes, and auditing of these tax accounts would move to the comptroller's office. The comptroller's office would also handle tax security requirements for alcoholic beverage accounts, as it does now for sales tax and other tax accounts.

Removing alcoholic beverage tax administration duties from the TABC and transferring them to the comptroller's office would leave the ports of entry program as the only tax collecting function at the TABC. The comptroller's office, through the ports of entry

stations, would be able to assess and collect use tax from individuals who purchase goods outside the U.S. and import those goods into the country.

Ensuring that communications are continued between tax collection and enforcement functions would be the purpose of a memorandum of understanding between the TABC and comptroller's office. The MOU should outline the mechanisms for the rapid transfer of needed information. The communication process set out by the two agencies in the MOU will be important to ensure that the state's taxes are fully protected and that public safety matters are rapidly addressed. The MOU should be in place by September 1, 1994.

Transfer of the tax collecting, processing, and auditing functions would allow the TABC to concentrate on the enforcement of the Alcoholic Beverage Code in areas such as underage drinking, proper licensing and permitting of alcoholic beverage businesses, and marketing and advertising practices. The agency would be able to focus on its primary duty of protecting the welfare, health, peace, temperance and safety of the citizens of the state.

FISCAL IMPACT

The recommendation would result in savings to the state from a reduction in positions and related expenses. Savings can be primarily realized through consolidation of TABC auditing offices throughout the state with those of the comptroller's office. The consolidation would reduce the need for some supervisory and support personnel. Administrative staff in the auditing division located at the TABC headquarters could be combined with similar administrative staff at the comptroller's office resulting in the elimination of additional supervisory and support positions. Based on the duplication of positions described above, it is estimated that 11 supervisory positions and related expenses could be quickly phased out. In addition, it is anticipated that the total level of auditors and support staff could be decreased over the years through cross training and elimination of duplicated efforts; however, these longer term costs savings cannot be calculated at this time.

The comptroller's office has indicated that it would reduce the number of audits performed on alcoholic beverage gross receipts tax accounts each year. However, the Alcoholic Beverage Code provides for a two-year taxpayer record retention period. Assuming the comptroller's office audited all mixed beverage accounts while the records are available, at least half of the accounts would be audited each year. This rate would be a reduction from the TABC's present 87 percent annual audit coverage rate. A reduced number of audits would result in the elimination of the need for some audit positions. Based on a 50 percent annual audit coverage it has been estimated that 34 audit positions and five support positions and related overhead could be phased out.

Total savings are estimated to be about \$2.3 million per year as a result of this recommendation. However, first year savings would be reduced due to costs associated with the transfer, such as moving expenses and integration of computers.

Fiscal Year	Savings to the General Revenue Fund
1994	\$0
1995	\$1,043,000
1996	\$2,270,000
1997	\$2,270,000
1998	\$2,270,000

ISSUE 3: If the tax collection and auditing functions of the TABC are transferred to the comptroller's office, the current statutory fee level should be increased to cover the cost of regulating the alcoholic beverage industry.

BACKGROUND

The Texas Alcoholic Beverage Commission issues 55 different types of alcoholic beverage licenses and permits and five bingo licenses and permits. Fee revenue derived from the issuance of these licenses and permits is deposited in the state's General Revenue Fund. Appropriations made by the legislature from the General Revenue Fund support the agency's programs that regulate the alcoholic beverage and bingo industries and collect and audit alcoholic beverage and bingo taxes. Looking specifically at alcoholic beverage fees and expenditures, the state received \$17.1 million from alcoholic beverage license and permit fees and expended \$24.5 million regulating the alcoholic beverage industry in fiscal year 1991, resulting in a \$7.4 million shortfall. In the same fiscal year, the state received \$3.28 million from fees related to bingo and expended approximately \$2.49 million regulating the bingo industry.

County and city governments are also authorized by the Alcoholic Beverage Code to charge license and permit fees on alcoholic beverage establishments in their jurisdiction. Counties and cities may charge a local fee for many permits and licenses that can be up to 50 percent of the state fee. Increases in the level of state fees result in the increase of local fees. In fiscal year 1991, counties and cities were authorized to collect up to \$9.3 million in local alcoholic beverage license and permit fees. Local fees are authorized by the statute to reimburse local governments for services performed such as collecting beer license fees and forwarding the funds to the state. The local fees also help recover costs associated with police protection and other services provided to licensees and permittees.

It is becoming an increasingly accepted policy in state government that fees paid by businesses and professionals should cover the costs to the state of regulating the industry or profession. The costs incurred by the state to regulate the alcoholic beverage industry were examined and compared to the revenue generated by fees paid by alcoholic beverage licensees and permittees. The comparison indicated a disparity in revenues collected versus the overall costs of regulation. Findings resulting from the comparison are discussed in the following material.

FINDINGS

- ▶ **From fiscal year 1988 to today, fees have not generated enough revenue to cover the costs of alcoholic beverage regulatory operations.**

- For the last four fiscal years, the state has not generated enough revenue through alcoholic beverage license and permit fees to recover the costs of regulating the alcoholic beverage industry. In fiscal year 1991, the Texas Alcoholic Beverage Commission was only able to cover 70 percent of its alcoholic beverage regulatory costs through fees. The following chart shows that revenues generated through fees have declined, while the cost of regulating the alcoholic beverage industry has increased.

	FY 1985	FY 1986	FY 1987	FY 1988	FY 1989	FY 1990*	FY 1991*
Fees	\$22.9	\$22.2	\$21.1	\$20.0	\$18.9	\$17.8	\$17.1
Expenses	\$18.9	\$20.5	\$19.8	\$20.9	\$20.9	\$22.8	\$24.5
Difference	\$4.0	\$1.7	\$1.3	\$-.9	-\$2.0	-\$5.0	-\$7.4

(all numbers are in millions)

*bingo fees and expenditures not included.

- The Texas Alcoholic Beverage Commission recovers the costs of regulating the bingo industry through fees charged to charities, lessors, and the manufacturers and distributors of bingo products. In fiscal year 1991, the TABC estimates that it expended \$2.49 million to regulate the bingo industry. During the same year, licensing fees related to bingo generated \$3.28 million resulting in a surplus of \$790,000.
- ▶ **Fees paid by alcoholic beverage licensees and permittees have not increased in several years.**
 - The last major fee increase for alcoholic beverage licenses and permits was in 1983. This fee increase affected the majority of licenses and permits and represented a 22 percent increase in fees.
 - Fees in most other professional licensing and regulatory agencies were increased by the legislature in both 1985 and 1987.
- ▶ **The state recovers the costs of regulating other businesses and professions through fees.**
 - In addition to the alcoholic beverage industry, the state also regulates many other businesses or industries. For example, the state presently regulates the insurance, utility, real estate, solid waste disposal and radiation control industries. The state recovers the costs of regulating all these industries through fees paid by the participating businesses.

- The state also regulates professionals such as doctors, pharmacists and lawyers. Of 29 professional groups regulated by the state, the state recovers the costs of regulating 22 professional groups.
- ▶ **Although costs would be reduced by consolidating alcoholic beverage tax collection and auditing in the comptroller's office, a fee increase would still be needed to recover alcoholic beverage regulatory costs.**
 - A projection of expenditures and fee revenues through fiscal year 1998 indicates that, if no changes are made, the shortfall will increase to \$8.6 million.
 - If the tax collection and auditing functions are transferred to the comptroller's office, the savings from the transfer would reduce the shortfall to \$5 to \$6 million per year.
 - The shortfall for fiscal year 1994 will approximate \$7 million. Although fees could be increased to cover this shortfall, the savings effects of the transfer would require fees to be reduced for fiscal year 1995 by over \$1 million.
- ▶ **Postponing the fee increases until implementation of the transfer would minimize the negative effects of such increases on the industry.**
 - The transfer would not take place until 1995 and savings would not be available to offset fees until this time.
 - If fees are raised in 1994 before the transfer takes place, licensees will face a 41 percent increase followed by a reduction in 1995.

CONCLUSION

It is general state policy to recover the costs of regulating an industry through fees. The costs of regulating many other industries and professions in the state are recovered through fees, and most fees were increased in the mid-1980's to accomplish cost recovery. Alcoholic beverage regulatory fees, however, have not been increased since 1983 and no longer cover the costs of regulation. To ensure that the needed fee increases are established in a stable and predictable manner, the increases should be implemented when the transfer of duties between the TABC and the comptroller's office is effective in fiscal year 1995.

RECOMMENDATION

- **If the transfer of functions takes place, the statute should be amended to:**
 - **increase existing alcoholic beverage fees by 34 percent to recover all costs of regulating the alcoholic beverage industry starting with fiscal year 1995; and**

- require the comptroller's office to develop and maintain information on the costs it incurs to carry out the alcohol and bingo taxation and audit functions. The cost information would be reported to the Legislative Budget Board and the Governor's Budget Office annually.

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This recommendation would affirm the policy that fees paid by the alcoholic beverage industry should bear the cost of regulating the alcoholic beverage industry. The present fee levels in the statute would be increased to recover the full costs of regulation, including the costs of tax collection and auditing. If the audit and collection of alcoholic beverage taxes are moved to the comptroller's office, the costs of those activities would need to be separately tracked so the legislature could include those costs in future fee increase. By reporting the audit and collection costs to the state's budget entities, the legislature would have the information necessary to determine the fee levels.

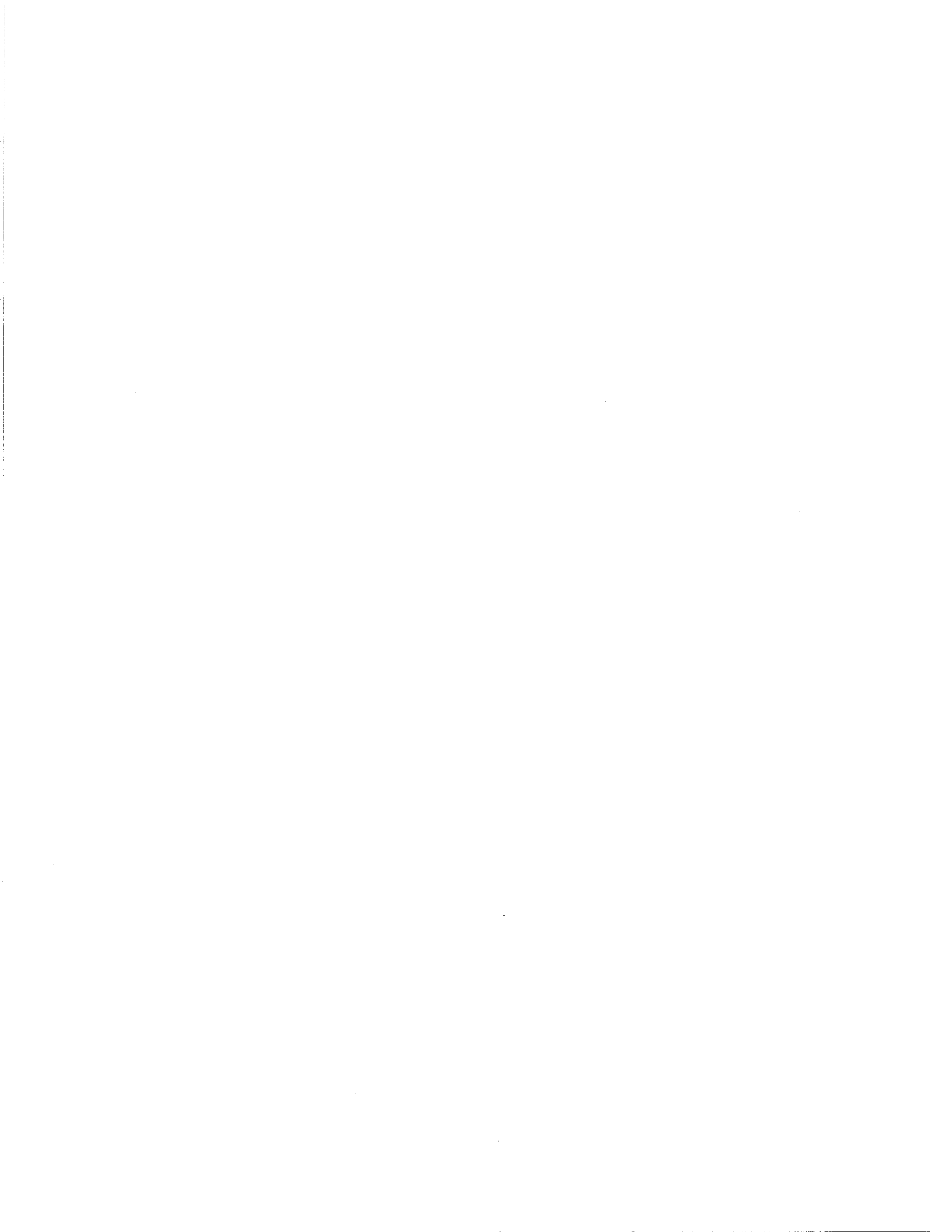
If the transfer approach is adopted, it is recommended that the fee increases be implemented in fiscal year 1995. Although fee increases could be imposed to cover the 1994 shortfall, these increases would result in an over collection in comparison to the estimated cost of alcoholic beverage regulation in succeeding years. Although fees will need adjustment as costs of regulation change over the years, the variations will be minimal once the reorganization is fully implemented.

FISCAL IMPACT

Based on revenue and expenditure projections provided by the TABC and on estimated savings from transferring the tax collection and auditing functions from the TABC to the comptroller's office, fees would need to be increased by 34 percent to cover the shortfall between fees and expenditures for fiscal year 1995. In addition, counties and cities could collect additional local license and permit fees of up to \$2.9 million per year, once the fee increase is effective.

Fiscal Year	Increased Revenue to the General Revenue Fund
1994	-0-
1995	\$5,781,000
1996	\$5,542,000
1997	\$5,324,000
1998	\$6,367,000

POLICYMAKING BODY



ISSUE 4: The size of the Texas Alcoholic Beverage Commission should be statutorily expanded to six members.**BACKGROUND**

The Texas Alcoholic Beverage Commission is a three-member policymaking body originally created in 1935 as the Texas Liquor Control Board. The members of the commission are appointed by the governor to six-year staggered terms. The governor designates one member as chairman. Members of the commission must have resided in Texas for five years and may not have any connections to the alcoholic beverage business.

The primary responsibilities of the commission include developing and implementing policies to carry out provisions of the Alcoholic Beverage Code and the Bingo Enabling Act, selecting an administrator to carry out the day-to-day functions of the agency and adopting the legislative appropriation request and subsequent agency budget.

State boards and commissions are generally structured to provide for the efficient performance of their duties, to ensure that the interests of the citizens of the state are appropriately represented and to allow for clear compliance with state statutes governing the operations of boards and commissions. A review of the structure, the responsibilities and the appointments to the Texas Alcoholic Beverage Commission revealed several significant findings which are discussed in the following material.

FINDINGS

- ▶ **A larger commission allows for increased ethnic, gender and geographic diversity in commission appointments.**
 - Since 1935, 29 people have served on the commission. The only minority or female that has served on the commission is the current chairman.
 - Of the past 10 appointments to the commission, eight have come from major urban areas.
 - The General Services Commission shows that greater diversity can be achieved when there is an expansion from three members to six members. Four appointments have been made to the commission since it was expanded in 1991. Three of the new members are female and two are members of ethnic minority groups.

- ▶ **Recent supreme court interpretations of the Texas Open Meetings Act indicate that three member boards and commissions may have difficulty in complying with that act.**
 - A May 1990 Texas Supreme Court opinion, Acker v. Texas Water Commission, states that a meeting occurs any time a quorum discusses or acts on public business.
 - With a three-member commission, every time two members meet they now must be certain that no matter pending before the commission is discussed in any way.
 - Under a six-member commission, for example, it would take four members meeting together in order for there to be a quorum under the Texas Open Meetings Act.
- ▶ **Only two other major Texas state agencies have three-member part-time policymaking bodies.**
 - The Public Safety Commission and the Texas Transportation Commission are the only three-member part-time commissions in Texas.
 - Most Texas boards or commissions are composed of either six or nine members.
- ▶ **Other states' alcoholic beverage licensing agencies that use a commission structure are generally overseen by larger boards or commissions.**
 - Of the 32 states that use a licensing approach to regulate alcoholic beverages, 16 states have an oversight board or commission. Of these 16 states, 11 have a larger board or commission. For example, New York and Illinois have five-member commissions. Of the two neighboring states that use a commission structure, Oklahoma has a seven-member commission and Arkansas has a five-member commission.

CONCLUSION

Each state board or commission should be structured to allow for appointment of members that provide representation of the citizens of the state into the decisions that affect them. In addition, the six-member structure should allow for easy and clear compliance with the Texas Open Meetings Act and other state statutes. A review of the appointments to and responsibilities of the commission showed that the present three-

member structure makes it difficult to represent the diverse geographical and ethnic make-up of the state and ensure that there are no violations of the Texas Open Meetings Act.

RECOMMENDATION

- **The statute should be amended to increase the size of the Texas Alcoholic Beverage Commission to six members.**

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An increase in the size of the commission to six members would provide more opportunity for the governor to appoint members to the commission that reflect the geographic and ethnic diversity of the state. Such a change in the size would allow for subcommittees to be created to review staff recommendations, as needed, prior to the commission's decisions. In addition, increasing the size of the commission would ease its difficulty in ensuring compliance with the Texas Open Meetings Act.

FISCAL IMPACT

Based on costs experienced by other policymaking boards that meet on a monthly basis, the change in the number of commissioners would increase direct costs approximately \$15,000 per year in travel and per diem expenses.

Fiscal Year	Cost to the General Revenue Fund
1994	\$15,000
1995	\$15,000
1996	\$15,000
1997	\$15,000
1998	\$15,000

ISSUE 5: The statute should require the establishment of a citizens advisory committee and a bingo advisory committee to assist the commission in identifying and addressing problems related to the alcoholic beverage and bingo industries.

BACKGROUND

The Texas Alcoholic Beverage Commission is responsible for the regulation of both the alcoholic beverage and bingo industries. The regulatory structure for these activities is statutorily complicated, and many rules have been developed to provide guidelines for both the agency and the regulated community to interpret the Alcoholic Beverage Code and the Bingo Enabling Act. For example, the agency has developed rules to guide its decisions on licensure of the many different types of businesses regulated under the code and the act. The agency also has developed rules on enforcement of the code which are designed to assist the enforcement personnel in protecting the public.

In 1988, the agency established an ad hoc advisory committee to review agency rules. Members of the committee represented various segments of the alcoholic beverage industry. The committee did not come to any conclusions and disbanded. The agency has recently appointed an ad hoc bingo advisory committee to identify problem areas in the industry's dealings with the TABC and establish strategies to deal with those problems. The committee also will look to identify areas of mutual concern regarding bingo. Agency staff have also begun conducting meetings about once a month around the state to listen to citizens' concerns regarding the agency.

State agencies need to obtain regular input from the public and groups they regulate or serve concerning issues and problems related to the agency's operations. The TABC's activities were reviewed to see if its structure provided an opportunity for the public and others to adequately participate in the development of the agency's policies and procedures. The review resulted in the following findings.

FINDINGS

- ▶ **The commission is charged with regulating the distribution, sale and consumption of alcoholic beverages and the playing of bingo. These activities affect the public and Texas business in several major ways.**
- The alcoholic beverage industry plays a significant role in the lives of Texas residents and has a large impact on Texas business. In 1990, an estimated 500 million gallons of liquor, wine, beer and malt liquor were consumed in Texas. Controls on the sale and marketing of these products

has an impact on consumers. Regulatory efforts to reduce the abuse of these products can have an impact on all citizens. The regulation of these products can also have serious impacts on business and the state's economy.

- Bingo has become a regular pastime for many citizens and is a significant source of revenue for many Texas charities and the businesses that work with those charities. In fiscal year 1991, over \$652 million was spent by patrons on bingo games conducted by over 1,770 charities across the state. Charities received over \$52 million and businesses that lease space to charities for bingo earned almost \$40 million from bingo in fiscal year 1991. Regulatory efforts to ensure that funds are properly paid out in prizes, to ensure that charities receive their fair share and to protect against illegal or unfair games are important to the citizens who participate in bingo, the charities who benefit and the businesses that provide goods and services.
- ▶ **The agency does not have a regular formalized procedure to obtain input on alcoholic beverage issues and problems from citizens, local communities and businesses.**
 - Although anyone may address the commission at their monthly meeting, there is no regular, formal mechanism to ensure that local communities, citizen groups or the regulated businesses have input into the development of the rules and procedures that affect them.
 - Groups that are involved in alcohol consumption issues and communities that deal with problems such as underage drinking and drunk driving have little opportunity to provide input into the development of or changes to rules that affect them. Input is generally limited to commenting on rules during the public hearing stage. However, this limitation bypasses these groups in the process of identifying the issues and problems that may need to be addressed in agency rules. It also excludes groups from involvement in the development of approaches to deal with a particular issue in rules.
 - The rules of the agency contain the procedures used to enforce the laws relating to the sale of alcoholic beverages to minors and affect other alcoholic beverage issues of concern to local communities. There is no regular mechanism, however, to obtain the opinions of people in the communities regarding agency rules.
- ▶ **The agency does not have a regular formalized procedure to obtain input from the bingo industry on the development of rules and procedures affecting bingo charities and lessors.**

- Although the bingo division works informally with members of the bingo industry, there is no regular, formal mechanism to ensure input into the development of rules and procedures. Input has been limited to speaking before the commission or participating in the public hearings on any rules developed. Although the TABC has been responsible for regulating bingo for over two years, the agency just recently appointed a bingo advisory committee to assist them in identifying problems in the regulation of bingo. The committee is ad hoc, and there is no assurance that it will continue in place.
- Input of community groups and the bingo industry in the agency's decision-making process is important because of the significant effect that these decisions have on the public and the bingo charities. Bingo is an important fundraising mechanism for over 1,700 charities in Texas. Any significant change in the way the bingo industry is regulated or taxed can have a major impact on the amount of funds that are raised for charitable purposes.
- ▶ **Most state agencies regularly use advisory committees to assist in the development of policies and procedures.**
 - Advisory committees are a common approach used in Texas to open up an agency's decision-making process to concerned citizens. For example, in the 1991 legislative session, the legislature created 46 advisory committees to provide advice to various state agencies.
 - Advisory committees are set up to provide a range of viewpoints or technical assistance to state boards or commissions from those affected by or interested in an agency's decisions. Advisory committees are, when they work well, a means by which issues can be discussed before they become problems and can keep the agency tuned to what communities are thinking.
 - For example, the Texas Commission on Alcohol and Drug Abuse has a statewide advisory committee which identifies problems related to alcohol and drug abuse and recommends approaches to address those problems. The commission also regularly organizes special advisory committees to work on specific problems and make recommendations to the commission.
 - Eleven other health and human service agencies use advisory committees to obtain input on program operations and the need for changes.
 - Many police departments in Texas use citizens' advisory groups or committees to provide input into their departments' practices and policies.

These groups often represent the interests and concerns of varying segments of the local communities.

CONCLUSION

The regulation of alcoholic beverages and bingo in Texas can have a significant impact on many people. With the exception of a recently appointed bingo advisory committee, the commission has made little effort to obtain input from citizens, public groups and the regulated industries in the development of the regulatory framework that affects them. Without a formal mechanism in statute which says that this activity should be a high priority, there is no assurance that communities, citizens groups or the alcoholic beverage and bingo industries will be given opportunities to participate in the development of governmental policies on a consistent basis.

RECOMMENDATION

- **The agency's statute should be amended to create a citizens advisory committee and a bingo advisory committee. The citizens advisory committee should:**
 - **be composed of nine members, appointed by the commission, with a balance of interests representing public groups interested in alcohol consumption issues, local communities, local police enforcement agencies and the alcoholic beverage industry;**
 - **advise the commission on the needs and problems of communities relating to the sale and consumption of alcoholic beverages;**
 - **be provided the opportunity to comment on rule changes during their development and prior to their final adoption unless an emergency requires immediate action;**
 - **provide an annual report to the commission on the committee's activities; and**
 - **perform other duties as determined by the commission.**
- **The bingo advisory committee should:**
 - **be composed of nine members, appointed by the commission, with a balance of interests representing the general public, charities that operate bingo games, and lessors (both charities and commercial lessors);**

- advise the commission on the needs and problems of the state's bingo industry;
- be provided the opportunity to comment on rule changes during their development and prior to their final adoption unless an emergency requires immediate action;
- provide an annual report to the commission on the committee's activities; and
- perform other duties as determined by the commission.

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Statutorily created advisory committees ensure that local communities, interested groups and the agency's regulated industries have an opportunity to participate in the policy development of the commission. Many of the agency's decisions and procedures can have a significant impact on the public. Providing a method in statute for input of these groups will ensure that their views will be considered in the policy development process and that this role will continue in the future. Requiring the committees to be composed of nine members provides for the representation of the interests needed on the committees but limits the size to ensure that decision-making can be made expeditiously.

FISCAL IMPACT

Additional costs would result from expenses incurred by members of the advisory committees as they attend meetings. Based on one day quarterly meetings, the expenses of the committees should not exceed \$20,000 annually.

Fiscal Year	Cost to the General Revenue Fund
1994	\$20,000
1995	\$20,000
1996	\$20,000
1997	\$20,000
1998	\$20,000



OVERALL ADMINISTRATION

ISSUE 6: The statute should be changed to include provisions that strongly encourage the agency to continue to give top priority to its efforts in recruiting and hiring women and minorities.

BACKGROUND

As a state agency, the TABC must meet a number of requirements relating to the recruitment and hiring of women and minorities. The purpose of the guidelines is to give these protected classes equal opportunity in the hiring and promotion processes and to reduce the underrepresentation of women and minorities in the work place. State agencies are also required to develop a plan to recruit and select qualified women and minorities and use selection procedures that are in compliance with the Texas Human Rights Act.

In addition to the general guidelines to be used in hiring, the state has established specific minority employment goals that are set out in the General Appropriations Act. These goals are set for eight job categories including officials/administrators, professionals, technicians, protective services, paraprofessionals, office/clerical, skilled craft, and service/maintenance. The appropriations act also requires all agencies to report the number of minority hirings and total hires made during the year to the Texas Commission on Human Rights.

In 1991, due to a controversy with the governor's office over agency hiring practices, the agency's overall policies were called into question. It was determined that the agency did not have adequate policies and procedures in place to allow the agency to effectively recruit and hire women and minorities. The agency did not have an active recruiting effort for women and minorities, there was not an individual assigned to concentrate on recruitment and hiring policies, each district or division made independent hiring decisions, and management positions were not opened to applicants outside the agency.

As a result of internal and external pressure, the TABC has made numerous changes to its employment policies within the past year. One of the most significant changes was the decision by the agency to use the civilian work force in Texas as the ultimate work force goal of the agency. This decision was significant because the goal chosen by the agency is much more difficult to attain than the goals set in the General Appropriations Act.

A government agency should strive to meet all state and federal employment goals in a timely manner by using all programs and policies available to recruit, hire, and retain qualified women and minority candidates. The review of the agency's recruitment and hiring efforts resulted in several findings which are discussed in the following material.

FINDINGS

- ▶ **While the TABC has met work force goals in six of seven applicable job categories, the agency has not met the minority work force goal set out in the 1992-93 appropriations act for the protective services job category.**
- The 1992-93 appropriations act encourages each state agency to meet the following work force percentages for minorities in eight job categories. While the agency has met these requirements in six out of the seven job categories that apply, it has not yet met the employment goal for minorities in the protective services category. This category includes the TABC's enforcement agents which are commissioned peace officers.

Category	State Target Percent	TABC Percent	Percent of TABC Staff in Categories
Officials & Adm.	14	14.3	2.0
Professionals	18	19.0	32.6
Technician	23	69.7	18.5
<u>Protective Services</u>	<u>48</u>	<u>21.3</u>	<u>24.6</u>
Paraprofessionals	25	25.3	12.8
Administrative Support	25	40.3	8.7
Skilled Craft	29	33.3	0.8
Service & Maintenance	52	n/a	n/a

- ▶ **The work force goals in the appropriations act differ from the work force percentages in the statewide civilian work force. Based on a comparison to the civilian work force in Texas, the agency has underrepresentation of ethnic groups, races and genders in several employment categories including protective services.**
- In the officials/administrators category, the work force of the TABC does not contain as high a percentage of women and minorities as the civilian work force in Texas.

Officials and Administrators

	White Male	Hispanic Male	Black Male	Other Male	White Female	Hispanic Female	Black Female	Other Female
Texas Civilian Laborforce (%)	40.9%	11.1%	5.6%	0.7%	28.7%	6.9%	5.5%	0.6%
TABC Laborforce (%)	61.5%	7.7%	15.4%	7.7%	7.7%	0.0%	0.0%	0.0%

-- In the professional job category, the work force of the TABC does not contain as high a percentage of women and minorities as the civilian work force in Texas.

Professionals

	White Male	Hispanic Male	Black Male	Other Male	White Female	Hispanic Female	Black Female	Other Female
Texas Civilian Laborforce (%)	40.9%	11.1%	5.6%	0.7%	28.7%	6.9%	5.5%	0.6%
TABC Laborforce (%)	63.4%	10.1%	3.5%	0.4%	18.1%	3.5%	0.9%	0.0%

-- The greatest concentration of underrepresentation is among women in the protective services (law enforcement) category. Compared to the civilian work force in Texas, the work force of the TABC does not contain as high a percentage of women and minorities.

Protective Services

	White Male	Hispanic Male	Black Male	Other Male	White Female	Hispanic Female	Black Female	Other Female
Texas Civilian Laborforce (%)	40.9%	11.1%	5.6%	0.7%	28.7%	6.9%	5.5%	0.6%
TABC Laborforce (%)	74.3%	12.8%	5.6%	0.6%	4.5%	1.7%	0.6%	0.0%

-- There is also underrepresentation of women and minorities in other job categories including technicians, paraprofessionals, administrative support, and skilled craft.

► In response to the governor’s office 1991 review of hiring practices at the TABC, the agency developed and implemented programs and policies to increase the agency’s ability to recruit and hire women and minorities.

- The agency adopted the goal of ultimately raising the percentages of women and minorities in its work force to percentages reflected in the statewide civilian work force.
- The agency hired a civil rights compliance specialist responsible for handling grievance procedures, recruiting, and evaluating applicants. The personnel director, along with the civil rights compliance specialist, is responsible for evaluation, review and ranking of all applicants prior to any hiring decision. The civil rights compliance specialist is also responsible for identifying specific problem areas in recruitment, hiring and promotion; ensuring that the agency moves toward work force targets; and developing contacts with professional and civil rights organizations and other minority groups.
- The agency modified its hiring process to provide centralized control of all hiring decisions. The compliance specialist and the personnel director evaluate and select applicants for all positions in the agency regardless of whether the position is located in the headquarters office or in one of the districts. This process ensures that agency hiring policies are applied consistently and that all applicants, regardless of race, national origin or gender, receive equal consideration.
- The agency revised its affirmative action plan with the assistance of the Governor's Equal Employment Opportunity Office. The goal of the plan is to identify areas of underrepresentation and make a concentrated effort to fill these positions with qualified female and minority applicants.
- The agency adopted a policy of opening management positions to applicants from outside the agency when it is determined that internal experience and knowledge is not expressly required. Traditionally, management positions had been filled by promoting from within the agency.
- The agency instituted a policy that prevents the hiring of any member of an employee's family, in an effort to enhance the ability of the agency to attract, recruit, hire, and promote women and minorities and prevent nepotism.
- The agency will report to the TCHR on its progress in recruitment and hiring of women and minorities for three years and will require all supervisory personnel to attend the TCHR's program on equal employment opportunity.

- ▶ **The human resources function at the TABC may be inadequate to handle all the recruiting, selection, and personnel matters of an agency with over 700 employees.**
 - All human resource functions for the Texas Alcoholic Beverage Commission are being handled by three individuals: the civil rights compliance specialist; the personnel director; and a business manager in the audit division, who handles benefits. The TABC does not have a human resources division specifically responsible for developing or implementing policies and procedures related to human resources, recruitment and hiring. These functions are assigned to the executive division that, in addition to human resources, is also responsible for coordinating the activities of all divisions in the agency.
 - In comparison, a range of other state agencies have larger human resource staffs. The Department of Commerce has 350 employees and nine human resource personnel. The Public Utility Commission has approximately 229 employees and six human resources personnel. The Department of Public Safety, which is considerably larger than the TABC, has 5,600 employees and a 34 person human resources staff. The Texas Department of Transportation (TDOT), which has approximately 15,000 employees, recently created a civil rights division made up of 19 employees. The TDOT ultimately plans to expand this division to 45 employees.
- ▶ **Other state agencies have had or have recently developed strong organizational structures related to personnel and human resources.**
 - The Texas Department of Agriculture has a well developed human resources division with a high level of oversight over their district hiring practices. To ensure that minority recruitment and hiring are given importance within the organization, the department has created a hiring process that requires the central office to review the applicant pool and selection process.
 - In 1991, the Texas Department of Transportation created a division of civil rights to handle complaints and grievances against the department, monitor the affirmative action plan and develop policies and procedures to facilitate the recruitment and hiring of women and minorities. The director reports to the commission annually on recruitment and hiring efforts.

CONCLUSION

Prior to 1991, the agency did not have strong policies and structures in place to promote the recruitment and hiring of women and minorities. Since then, the agency has taken

many steps to develop and implement policies and procedures to identify areas of underrepresentation and facilitate the recruitment and hiring of qualified women and minorities. The following recommendations are intended to continue this improvement and provide a statutory basis for further efforts in recruiting and hiring women and minorities.

RECOMMENDATION

The following requirements should be placed in statute to guide the personnel policies of the agency in the future.

- **Create a human resources section that will be responsible for handling all personnel, recruiting, hiring and other human resource functions.**
- **Require the human resources section to develop policies and procedures related to recruitment and hiring that are in compliance with all applicable state and federal laws.**
- **Develop a recruiting program that identifies underrepresentation within the agency and focuses on recruiting different ethnic, race and gender groups for specific job categories in which underrepresentation exists.**
- **Require that all pools of applicants be reviewed by the human resources section to ensure proper consideration of underrepresented classes.**
- **Open upper management positions to applicants from outside the agency in order to diversify the work force.**
- **Require the administrator to report annually to the commission on recruitment and hiring.**

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Discussions with the Texas Commission on Human Rights indicated that the recommendations made above constitute a framework of policies and procedures that are essential in addressing issues related to recruitment and hiring. The recommendations would require the agency to identify areas of underrepresentation and develop approaches to attract and recruit qualified women and minorities. The policies regarding the recruitment, hiring and promotion of women and minorities, just as with any other policy, must be supported by the commission and upper management to be effective.

FISCAL IMPACT

Development of policies and procedures related to recruitment and hiring would not have a fiscal impact. Staffing a human resources section would result in the addition of a human resources officer and a human resources assistant. Costs for the positions would approach \$73,300 for salaries, benefits and travel.

Fiscal Year	Cost to the General Revenue Fund
1994	\$73,300
1995	\$73,300
1996	\$73,300
1997	\$73,300
1998	\$73,300



ISSUE 7: If the tax collection and auditing functions are not transferred to the comptroller's office, the commission should be required to cover the cost of regulating the alcoholic beverage industry through fees and have the authority to set the fee levels in rules.

BACKGROUND

The Texas Alcoholic Beverage Commission issues 55 different types of alcoholic beverage and five bingo licenses and permits. Fee revenue derived from the issuance of these licenses and permits is deposited in the state's general revenue fund. Appropriations made by the legislature support the agency's programs that regulate the alcoholic beverage and bingo industries and provide services that protect the health, safety and welfare of Texas residents. In fiscal year 1991, the TABC generated \$20.4 million in fee revenue from both bingo and alcoholic beverage licenses and permits and had expenditures of approximately \$27 million, resulting in a shortfall of approximately \$6.6 million. Looking specifically at alcoholic beverage fees and expenditures, the agency collected \$17.1 million from alcoholic beverage license and permit fees and expended \$24.5 million regulating the alcoholic beverage industry in fiscal year 1991, resulting in a \$7.4 million shortfall.

County and city governments are also authorized by the Alcoholic Beverage Code to charge license and permit fees on alcoholic beverage establishments in their jurisdiction. Counties and cities may charge a local fee for many permits and licenses that can be up to 50 percent of the state fee. Increases in the level of state fees results in the increase of local fees. In fiscal year 1991, counties and cities were authorized to collect up to \$9.3 million in local alcoholic beverage license and permit fees. Local fees are authorized by the statute to reimburse local governments for services performed such as collecting beer license fees and forwarding the funds to the state. The local fees also help recover costs associated with police protection and other services provided to licensees and permittees.

The TABC does not have the authority to increase the level of its fees to cover the costs of regulation because the cost of each license or permit is set in statute. To change the cost of each license or permit the TABC must go to the legislature to request an increase in fees. Overall, allowing regulatory agencies to set fees and cover the costs of regulating an industry or profession is a practical approach that has received increasing legislative acceptance in recent years. The review of the agency's fee setting authority and cost recovery revealed several findings which are discussed in the following material.

FINDINGS

- ▶ **From fiscal year 1988 to today, fees have not generated enough revenue to cover the costs of alcoholic beverage regulatory operations.**

- For the last four fiscal years, the TABC has not generated enough revenue through fees to cover the costs of regulating the alcoholic beverage industry. In fiscal year 1991, the Texas Alcoholic Beverage Commission was only able to cover 70 percent of its alcoholic beverage regulatory costs through fees. The following chart shows that revenues generated through fees has declined, while the cost of regulating the alcoholic beverage industry has increased.

	FY 1985	FY 1986	FY 1987	FY 1988	FY 1989	FY 1990*	FY 1991*
Fees	\$22.9	\$22.2	\$21.1	\$20.0	\$18.9	\$17.8	\$17.1
Expenses	\$18.9	\$20.5	\$19.8	\$20.9	\$20.9	\$22.8	\$24.5
Difference	\$4.0	\$1.7	\$1.3	-\$-.9	-\$2.0	-\$5.0	-\$7.4

(all numbers are in millions)

*bingo fees and expenditures not included.

- The Texas Alcoholic Beverage Commission recovers the costs of regulating the bingo industry through fees charged to charities, lessors, and the manufacturers and distributors of bingo products. In fiscal year 1991, the TABC estimates that it expended \$2.49 million to regulate the bingo industry. During the same year, licensing fees related to bingo generated \$3.28 million resulting in a surplus of \$790,000.
- ▶ **The Texas Alcoholic Beverage Commission does not have the authority to set the level of fees to recover the costs of regulation.**
 - The fee for each permit or license issued by the TABC is set in statute. This prevents the agency from modifying fee rates through the rulemaking process, and any changes to the level of a specific fee must be made by the legislature.
 - The legislature, however, does not regularly pass legislation to make fee adjustments for the agency. The last major fee increase for alcoholic beverage licenses and permits was in 1983. This fee increase affected the majority of licenses and permits and represented a 22 percent increase.
 - Fees in most other professional licensing and business regulatory agencies were increased by the legislature in both 1985 and 1987.

- ▶ **The state recovers the costs of regulating other businesses and professions through fees.**
 - Of 29 professional licensing agencies contacted, all have the authority to set their own fees through rules. Twenty-two of these agencies are required by statute to recover their costs of regulation through fees.
 - A survey of six business regulatory agencies and programs in the state showed that five of these agencies have the authority to set their own fees through rules. These agencies include the Board of Insurance, the Public Utility Commission, the Real Estate Commission, the Water Commission and the Air Control Board. Two divisions under the Texas Health Department, radiation control and solid waste disposal, have the authority to set their own fees through rules to recover their costs. All of these business regulatory agencies and programs recover their costs of regulation through fees.

- ▶ **The Texas Alcoholic Beverage Commission is similar to agencies that have the authority to set their own fees and recover the costs of regulation through fees.**
 - Other business regulatory agencies such as the Real Estate Commission, the Water Commission, the Public Utilities Commission and the Air Control Board have the authority to change the level of their fees and cover the costs of regulation through fees.
 - Like the Water Commission, Air Control Board, Board of Insurance, and Public Utility Commission, the TABC licenses and permits businesses and regulates their activities.

- ▶ **Recovering the costs of regulating the alcoholic beverage industry through fees and giving the TABC the authority to set fees would increase revenue to the state.**
 - In fiscal year 1991, the TABC permit and license fees would need to have been increased by approximately 43 percent to generate the \$7.4 million required to cover the difference between fee revenues and alcoholic beverage regulatory costs.
 - A projection of expenditures and fee revenues through fiscal year 1998 indicates that if no changes are made, the shortfall would increase to \$8.6 million.

CONCLUSION

The Texas Alcoholic Beverage Commission does not recover the costs of regulating the alcoholic beverage industry and does not have the authority to raise fee levels to do so. Most other professional licensing and business regulatory agencies in the state recover regulatory costs through fee revenues and have the authority to set fee levels to recover costs. By recovering the costs of regulating the alcoholic beverage industry, the commission could generate approximately \$7 million in additional fee revenue in fiscal year 1994.

RECOMMENDATION

- **If the tax collection and auditing functions are not transferred to the comptroller's office, the statute should be amended to require the commission to recover the state's costs of regulating the alcoholic beverage industry through alcoholic beverage license and permit fees. To accomplish this requirement, all present fee amounts should be removed from the code and the commission should be directed to set the fees in rule to recover the state's costs of regulating the alcoholic beverage industry.**

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This recommendation would affirm the policy that fees paid by the alcoholic beverage industry would cover the cost of regulation of the industry. The fee setting process would allow the industry and the public to have input in developing the fee system. Authorizing the commission to set fee levels to recover the state's costs of regulating the alcoholic beverage industry would prevent the legislature from having to enact legislation just to keep up with inflation and the increasing costs of regulation. The particular fee amounts should reflect both regulatory costs and take into account the economic impact of the fee increase on different types and classes of licenses and permits.

The legislature would, however, continue to determine the amount of regulatory effort needed in the state by setting the amount of expenditures through the appropriations process. The agency's appropriations, as set by the legislature, would also serve as the cap on fees.

FISCAL IMPACT

The authority to set fees would allow the alcoholic beverage commission to recover the state's costs of regulating the alcoholic beverage industry. This would increase the amount of money that the Texas Alcoholic Beverage Commission deposits in the general revenue fund. By increasing fees to recover costs, the state would receive an estimated \$6.8 million to \$8.6 million annually. In addition, counties and cities would be authorized to collect additional local license and permit fees of between \$3.4 million and \$4.3 million if these

entities charged the maximum amount allowed in the Alcoholic Beverage Code. The increase to the state's general revenue fund is based on the projected shortfall between the state's alcoholic beverage regulatory costs and alcoholic beverage license and permit fees from fiscal year 1994 to fiscal year 1998.

Fiscal Year	Increased Revenue to General Revenue Fund
1994	\$7,000,000
1995	\$6,800,000
1996	\$7,800,000
1997	\$7,600,000
1998	\$8,600,000



EVALUATION OF PROGRAMS

ISSUE 8: The agency's enforcement powers should be strengthened by amending the Texas Alcoholic Beverage Code to provide the agency with clear suspension and administrative penalty authority.

BACKGROUND

The agency's enforcement division is responsible for enforcing provisions of the Alcoholic Beverage Code and related agency rules and regulations. To ensure industry compliance, enforcement personnel inspect and conduct undercover activities at licensed premises and respond to complaints from the public, other law enforcement agencies, and other licensees. The agency has two formal enforcement tools to encourage compliance: cancellation and suspension. The agency has the authority to cancel, after notice and a hearing, a permit or license. However, suspension is the commission's primary enforcement tool. Currently, the agency has the power to suspend a permit or license for noncompliance for up to 60 days. The threat of suspension can be an effective deterrent because the permittee or licensee is required to cease the sale of alcoholic beverages during the period of the suspension. However, under statute, the commission must provide a permittee or licensee facing a suspension with the option of paying a fine in lieu of the suspension. The statute sets the minimum fine at \$150 for each day of the suspension but does not limit the maximum amount the agency can assess. When determining the amount of the fine, the agency is required by statute to consider the negative economic impact a suspension would have on the permittee or licensee. The penalty option was placed in statute during the 65th legislative session in 1977. Prior to this time, straightforward suspensions and cancellations were the agency's primary enforcement tools.

The agency has recently developed a penalty matrix to provide the district offices with guidelines for determining the length of a suspension or fine amount for specific violations. The purpose of the matrix is to attempt to ensure that suspensions and fines are applied consistently throughout the state. The matrix, which has not been adopted in rules, takes into account the severity of the violation and whether it is a first or repeat offense. The TABC is currently upgrading its penalty matrix so that it can more accurately determine the economic impact a suspension would have on a permittee when determining the amount of the fine. However, the TABC has indicated that it has had difficulty applying the economic impact criteria. As a result, the TABC, in most cases, has chosen to apply the minimum \$150 fine, per day of suspension, regardless if the violator is a small or large volume licensed premise. For example, in fiscal year 1991, approximately 71 percent of the fines assessed by the TABC were based on the \$150 per day minimum.

In fiscal year 1991, 3,046 permittees and licensees found in violation of the code or agency rules had the option of paying a fine in lieu of suspension. Of this total, 1,738 permittees and licensees (57 percent) chose suspension, while 1308 permittees and licensees (43 percent) chose to pay a fine in lieu of suspension. Fines assessed by the TABC in fiscal

year 1991 were based on a per day fine amount that ranged from \$150 to \$1,250 per day. In fiscal year 1991, the average total fine assessed against violators was approximately \$1,263. This amount represented an average suspension of approximately seven days. The largest total fine assessed during this period was \$25,000 and the longest suspension was 60 days. The total amount of fines collected by the agency was \$1,652,300 for fiscal year 1991.

For most major regulatory agencies, the state has authorized an enforcement structure that provides an increasing array of stronger enforcement powers. These actions include authority to warn in minor cases of non-compliance, suspend for serious violations of the statute, and cancel or revoke for the most egregious cases of non-compliance. Also included in this array is administrative penalty authority which provides regulatory agencies with an enforcement tool that is flexible enough to take action against permittees and licensees for a variety of violations, including repeat violations. The enforcement structure of the TABC was compared to this standard structure for regulatory agencies. The review resulted in the following findings.

FINDINGS

- ▶ **The TABC's authority to suspend or fine differs significantly from that given to other regulatory agencies.**
 - The agency currently has the authority to suspend a permit or license. Even though TABC has suspension authority, it is required by statute to offer the permittee or licensee the option of paying a fine, in lieu of the suspension.
 - The Texas Alcoholic Beverage Code sets the fine at a minimum of \$150 per day. The code does not set a maximum amount for the fine. However, other agencies that have the authority to fine licensees are generally provided limits for penalty assessments. For example, the State Board of Insurance has authority to assess administrative penalties up to \$25,000 per violation against anyone regulated by the board who violates state law or board rules.
 - Even though the TABC is required by the code to provide a violator with the option of paying a fine in lieu of suspension, it does not have direct administrative penalty authority.
- ▶ **The current structure of the TABC suspension and fine authority allows the violator and not the agency to choose the appropriate sanction.**
 - The TABC is effectively prevented from suspending a permit or license without offering the violator the option of paying an administrative penalty

in lieu of the suspension. Agency staff indicated that cancellation is the only enforcement tool the agency can use to force a permittee or licensee to cease the sale of beverage alcohol for serious violations of the Texas Alcoholic Beverage Code and commission rules.

- In fiscal year 1991, the agency attempted to suspend 3046 permits and licenses. However, because the agency is required to offer a permittee or licensee the option to pay a penalty in lieu of suspension, only 1738 or 57 percent of the permits and licenses were actually suspended.
- ▶ **Larger volume mixed beverage permittees are better able to avoid suspensions by paying the fine than smaller permittees and licensees.**
 - An analysis of mixed beverage permittees found in noncompliance indicated that the higher the permittee's tax liability (the more sales revenue generated), the more likely a permittee would choose to pay the fine in lieu of suspension.
 - In fiscal year 1991, approximately 36 percent of mixed beverage permittees (64 out of 178 permittees) with a gross receipts tax liability of less than \$15,000 charged with violations, opted to pay a fine rather than accept a suspension. However, approximately 78 percent of mixed beverage permittees (271 out of 346 permittees), with a gross receipts tax liability greater than \$15,000, charged with violations, opted to pay a fine rather than accept a suspension.
- ▶ **Other state agencies' suspension and administrative penalty authority are structured in a more straightforward way.**
 - The majority of major regulatory agencies have a range of available sanctions including separate suspension and administrative penalty authority. Examples of major regulatory agencies with enforcement structures that do not allow violators the option to pay a fine in lieu of suspension include Texas Air Control Board, the Water Commission, the Texas Department of Agriculture, the State Board of Insurance, the State Department of Health and the Texas Railroad Commission.
 - These agencies are authorized administrative penalties as a tool to discourage violations. For example, the State Board of Insurance can assess administrative penalties up to \$25,000 per day for violations of the Insurance Code and board rules.

- ▶ **Changing the statute to provide TABC with clear suspension and administrative penalty authority would strengthen the agency's enforcement structure.**
 - Clear suspension authority would allow the commission to eliminate the option to pay a fine by permittees and licensees for violations that threatened the public welfare such as sales of alcoholic beverages to a minor or sale or delivery of drugs by a permittee or licensee. Short of cancellation, the agency must allow these businesses the option to pay a fine and continue to operate.
 - Clear suspension authority would provide the commission with an enforcement power that would be visible to the public when used. A suspended permittee or licensee would have to cease the sale of alcoholic beverages and in many cases would have to shut down during the period of the suspension.
 - Clear administrative penalty authority could provide the commission with a method of dealing with less serious or repeat violations. For example, permittees or licensees guilty of violations such as permitting a minor in a package store or sale of alcoholic beverage for resale, would be first subject to an administrative penalty rather than to suspension or cancellation. Some repeat offenses such as consignment sale of liquor and beer or purchase of alcoholic beverages from another retail dealer for resale, would also be subject to administrative penalties.

CONCLUSION

The state generally provides regulatory and professional licensing agencies with sufficient enforcement powers to encourage compliance from the businesses or professions they regulate. Currently, the agency has the authority to suspend a permit or license for non-compliance with the Texas Alcoholic Beverage Code and agency rules. Short of cancellation, the agency must allow the permittee or licensee found in noncompliance to pay a fine in lieu of suspension. This approach is different from that used by most regulatory and professional licensing agencies and has resulted in high volume permittees being able to avoid suspension more often than other permittees. The structure of the agency's suspension and fine authority reduces the agency's ability to most effectively enforce the Texas Alcoholic Beverage Code and agency rules.

RECOMMENDATION

- **The statute should be changed to provide the agency with better enforcement authority by:**

- removing the option provided to a violator to pay a fine in lieu of a suspension;
- establishing clear suspension authority; and
- authorizing the agency to levy an administrative penalty against permittees and licensees found in violation of Texas Alcoholic Beverage code and commission rules. The agency's administrative penalty authority should be patterned after the approach used in other regulatory and licensing agencies and would provide a maximum penalty amount of \$25,000 per violation.

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The present statutory approach provides greater flexibility to permittees and licensees who violate the code and agency rules than to the TABC. This recommendation would authorize a standard set of enforcement powers for the TABC. These enforcement powers would apply to all elements of the alcoholic beverage industry, including manufacturers, wholesalers and retailers, and could be used against all violations of the code. The agency would be authorized to set penalties to fit the severity of the violation, taking into account the past history of the permittee and the extent to which the permittee may have acted without knowledge or intent to violate the law. The agency's administrative penalty authority would be modeled after the standard sunset approach used in the past to provide administrative penalties in other regulatory agencies. Under this approach, the code would contain guidelines the TABC would use when determining the amount of a penalty. The TABC would develop, in rules, the approach it would take in applying the statutory guidelines. This approach would also establish the permittee's or licensee's right to appeal the penalty and would require that all penalties be deposited in the general revenue fund.

The agency would be required to follow a standard method for using administrative penalty authority that would be set out in statute. Further details, including a penalty structure would be adopted by the commission in rules. The adoption of the penalty mechanism, in rules, provides the public and the regulated industry with input in the day-to-day working of the administrative penalty system.

Clear authorization to suspend a permit or license will allow the TABC to take visible action against all violators, particularly against those violations that threaten the public welfare, such as a licensed premise selling alcoholic beverages to a minor. Setting a maximum penalty of \$25,000 per violation would help ensure that the penalty is an effective deterrent and would be consistent with the maximum range of administrative penalties found in other major state regulatory agencies.

FISCAL IMPACT

This recommendation would result in a positive fiscal impact. The authority to levy administrative penalties would result in increased revenue to the general revenue fund. The exact amount cannot be estimated at this time due to the lack of information on how often and in what amounts the commission would levy such penalties. In addition, there could be some costs associated with the recommendation. For example, there could be an increase in the number of administrative hearings if suspensions and administrative penalties are contested by permittees and licensees. However, the increase in the number of administrative hearings is similarly difficult to estimate without knowledge of how often these decisions will be contested.

ISSUE 9: Statutory prohibitions against the sale of alcoholic beverages to minors by licensees and permittees should be clarified to improve the TABC's enforcement effort.

BACKGROUND

The legislature, with the passage of Senate Bill 21 in 1985, raised the state minimum drinking age to 21 years of age, primarily in response to the potential loss of federal highway funds for states that did not raise their drinking age to this level. Both administrative and criminal provisions of the Alcoholic Beverage Code prohibiting the sale, possession and consumption of alcohol by minors are specifically regulated by the enforcement and marketing division of the TABC. Age law violations are identified through the investigation of complaints, routine inspections of retail establishments and "sting" operations. The enforcement division spends a considerable amount of time on age law violations. In fiscal year 1991, the enforcement division employed 314 personnel at the headquarters office and in the 21 enforcement district offices and reported 1,154 administrative and 31,349 criminal age law violations. This represents approximately 30 percent of all the administrative and 69 percent of all the criminal cases identified by the enforcement division.

The TABC possesses both administrative and criminal authority to curb the sale of alcohol to minors by alcoholic beverage permittees and licensees. The criminal provisions against the seller for age law violations consist of misdemeanors with a range of fines from \$100 to \$1,000 or confinement in jail of not more than a year. The code also provides sanctions for use against minors that possess or attempt to buy alcoholic beverages. Persons under the age of 21 can be charged with a misdemeanor for age law violations with fines of \$25 to \$500 and be subject to community service and alcohol awareness education requirements. The TABC may also render administrative sanctions against a licensee or permittee if it is found that they sold, served, dispensed or delivered an alcoholic beverage to a minor. Sanctions range from a warning, to suspension or cancellation of a license or permit. A fine of at least \$150 per day of suspension may be substituted by a licensee or permittee for the actual suspension.

In order for enforcement personnel to take action against someone for the sale of an alcoholic beverage to a minor, the statute requires the agency to show that an improper sale of alcoholic beverages did occur. In the criminal prosecution of age law violations, the offender must have violated the law "with criminal negligence". In an agency administrative action against the licensee or permittee, the retail seller must have "knowingly" sold the alcoholic beverage to a minor.

In 1990, an alcoholic beverage retailer's permit was suspended for selling an alcoholic beverages to a minor. The retailer appealed the suspension order and in 1991, the Fifth District Court of Appeals at Dallas determined that the criminal negligence and knowingly

standards in the Alcoholic Beverage Code conflict. The court ruled that, in instances of conflicting standards, the most specific standard applies. In this case, the provisions for administrative enforcement were more specific, and the court determined that the knowingly standard therefore applies. Because of previous court decisions that made it very difficult to prove the standard of knowingly, the agency placed a moratorium on administrative actions against licensees and permittees who may be found selling alcoholic beverages to minors. The moratorium has been in place since July 1991.

The impact of the appeals court decision and the agency's general enforcement powers regarding the sale of alcoholic beverages were examined to determine whether the agency has sufficient powers to implement the state's policy of prohibiting sale of alcoholic beverages to minors. The results of this analysis are contained in the following findings.

FINDINGS

▶ **Underage drinking, particularly related to driving, is a serious problem nationally as well as in Texas.**

- All 50 states have set their legal drinking age at 21 years old. However, studies continue to show significant levels of alcohol use and driving while intoxicated (DWI) by minors.

A June 1991 study by the U.S. Office of the Inspector General reported that 51 percent of the nation's junior and senior high school children have had at least one drink in the past year. Eight million or 34 percent of the children surveyed drink weekly. Nearly seven million or 34 percent purchase their own alcohol. In addition, the 1990 National High School Senior Survey found that 89.5 percent of high school seniors have drunk alcohol at least once.

- Studies also indicate that Texas youth show substantial levels of alcohol use and incidence of DWI.

In fiscal year 1991, the TABC reported 27,665 criminal cases of minors in possession of an alcoholic beverage and 947 administrative cases against retailers for sale of alcoholic beverages to minors.

The Texas Juvenile Probation Commission reported that 2,300 or two percent of the 98,000 referrals of youths under the age of 17 to local juvenile probation departments, were for liquor law violations in 1990. However, over 17,400 or 18 percent of all referrals were reported to involve symptoms of alcohol abuse.

The Texas Commission on Alcohol and Drug Abuse 1990 Texas School Survey of Substance Abuse reported that about 81 percent of secondary school students reported having drunk alcohol. The survey also showed that over one-half of Texas secondary students or 52 percent reported it would be easy to get alcohol if they wanted some.

A 1990 Texas Department of Public Safety report on DWI showed that minors under the age of 21 make up approximately 13.4 percent of all DWI drivers involved in accidents statewide.

- ▶ **Texas' approach in preventing the sale of alcoholic beverages to minors is ineffective.**
 - A recent court decision prevents the TABC from enforcing administrative provisions of the Alcoholic Beverage Code that prohibit the sale of alcoholic beverages to minors. The code contains two different methods for determining the manner in which a person sold an alcoholic beverage to a minor. In June 1991, the Fifth District Court of Appeals at Dallas ruled that because the code has two conflicting statutory provisions on one subject, the more specific provision must apply. Previous court decisions have interpreted the more specific court provision so narrowly that agency staff indicate it is extremely difficult to prove that a licensee or permittee violated the code.
 - As a result, little or no action is currently being taken by the agency against licensees and permittees who sell alcoholic beverages to minors. In July of 1991, in response to the appeals court ruling, the agency instituted a moratorium on all administrative hearings concerning the sale of alcoholic beverages to minors. Since that time, the number of administrative cases involving sale to minors dropped significantly.
 - In the first six months of fiscal year 1991, the TABC developed 556 cases for the sale of alcoholic beverages to minors. In comparison, during the first six months of fiscal year 1992, the agency only developed 39 cases regarding sales to minors. This represents a 93 percent drop in the number of cases. In addition, only three age law cases have been sent to headquarters for a hearing in the first six months of fiscal year 1992, representing a 95 percent decrease from the previous year.

CONCLUSION

Sanctions against licensees and permittees for the sale of alcoholic beverages to minors have virtually ceased in Texas. Although studies continue to show significant levels of alcoholic beverage consumption in Texas and the nation by those under the legal drinking

age, the ability to take enforcement action against those who sell alcoholic beverages to minors has been crippled by a recent court ruling. Without a statutory change to rectify an inconsistency in the Alcoholic Beverage Code that was identified by the Dallas Fifth District Court of Appeals, it is unlikely that enforcement efforts against those who sell alcoholic beverages to minors will resume.

RECOMMENDATION

- **All sections of the Alcoholic Beverage Code pertaining to the sale of alcoholic beverages to minors should be amended to consistently use "criminal negligence" as the standard that must be met to prove that the sale occurred.**

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This recommendation would change the standards of proof for age law violations that currently use "knowingly" as the standard to instead use the term "criminal negligence". This rectifies an inconsistency in the code created in 1987 when the legislature changed the standard of proof for criminal age law violations to criminal negligence, while not changing the standard for administrative cases against licensees. The "criminal negligence" definition would apply to the sale, service, dispensing or delivery of alcoholic beverages to minors or for allowing a minor to possess of consume an alcoholic beverage.

Since the recent court decision prevents the agency from taking administrative enforcement action against licensees and permittees for sale of alcoholic beverages to minors, this change would allow the TABC to reactivate its enforcement efforts in this area. It is expected that the number of administrative cases for age law violations would return to levels similar to those that existed before the appeals court decision.

FISCAL IMPACT

Because the agency is currently appropriated funds for their enforcement activities, including full enforcement of minimum drinking age laws, there would be no fiscal impact from this recommendation.

ISSUE 10: The statute should be changed to eliminate provisions which prevent the agency from performing its audit function in the most efficient manner.

BACKGROUND

The TABC is responsible for the administration of alcoholic beverage and bingo taxes. In addition to collecting these taxes, the TABC audits tax accounts to ensure that taxpayers have complied with applicable tax laws and that taxpayers have remitted all taxes owed to the state. The majority of audits conducted by the TABC are on alcoholic beverage gross receipts tax accounts. In fiscal year 1991, the TABC conducted a total of 7,172 audits, of which 7,092 or 99 percent were on alcoholic beverage gross receipts tax accounts. In fiscal year 1991, the TABC spent \$5.78 million and employed 158 staff in its audit division.

In 1991, the TABC developed and implemented an audit select procedure designed to identify and select those mixed beverage accounts with the highest probability of incurring a tax deficiency. This is consistent with the 1992-1993 Appropriations Act which requires the TABC to develop and implement an audit select program based on audit productivity rather than audit frequency, where feasible. The purpose of the audit select procedure is to identify risky accounts and allow the agency to focus on these accounts, rather than spending audit time and money on accounts that will result in little or no deficiency. However, requirements in the Texas Alcoholic Beverage Code prevent the agency from fully utilizing the audit select procedure to focus its audit efforts on high risk accounts.

The agency's audit procedure was the subject of the 1989 and 1992 state auditor reports of the TABC. The State Auditor recommended that the TABC develop and implement an audit select procedure that focuses on high risk accounts and noted that provisions in the Alcoholic Beverage Code hindered the agency in improving the audit selection procedure. The 1992 state auditor report recommended that the record retention period for taxpayers be extended, the requirement that each permittee be examined be removed, and the TABC be authorized to charge interest on delinquent tax payments.

Agency governing statutes should not prevent an agency from performing functions and activities in the most effective and efficient manner. A comparison of the TABC's statutory provisions and its auditing process to the statutes and processes of other tax collecting entities resulted in the following findings.

FINDINGS

- ▶ **The agency's audit resources cannot be efficiently used due to specific audit requirements in the Alcoholic Beverage Code.**

- The Alcoholic Beverage Code (Section 202.06b) requires that mixed beverage permittees retain all alcoholic beverage purchase and sale records for two years. Because of this two-year record retention requirement, the TABC must audit mixed beverage accounts at least every two years to make sure that records needed to verify payment of taxes are available.
 - The Alcoholic Beverage Code (Section 202.09a) requires that each mixed beverage gross receipts tax account be examined. The agency interprets this provision to require an audit of each account at least once during the two-year record retention period. This provision, in combination with the record retention requirement, prevents the agency from instituting a selective audit program that concentrate the agency's time and resources on high risk accounts.
- ▶ **Other state agencies that collect taxes are given audit flexibility and do not have provisions in their statutes which require them to audit all accounts.**
- The comptroller's office audits 29 different types of tax accounts including public utility tax accounts, motor fuels tax accounts and sales tax accounts, which makeup the largest portion of revenue collected by the comptroller's office. In fiscal year 1991, the comptroller's office collected \$15.2 billion in taxes. The comptroller's office is not required to audit each sales tax account. In fiscal year 1991, the comptroller's office audited approximately 12,400 of its 503,000 sales tax accounts.
 - The Texas Employment Commission audits employers to ensure that all eligible employees have been reported and that the proper amount of unemployment tax has been paid. The TEC is not required to audit each employer. The U.S. Department of Labor does require the TEC to audit at least four percent of employers in Texas each year. To meet this requirement, the TEC audits approximately 12,000 of the state's 300,000 employers.
 - The State Board of Insurance is responsible for auditing more than 2,100 licensed insurance companies in Texas and in other states. The State Board of Insurance is not required to audit each account.
- ▶ **Other state agencies that collect taxes require taxpayers to retain their financial records for more than two years.**
- The comptroller's office requires sales tax accounts to maintain financial records for four years. Staff of the comptroller's office indicated that the statute of limitations on collecting delinquent taxes is also four years. This allows the comptroller's office to identify and collect deficiencies up to four years old.

- Texas Employment Commission requires unemployment tax accounts to maintain financial and employment records for four years.
- The Board of Insurance requires that licensed companies and surplus lines agents maintain their financial records for four years.
- ▶ **The TABC is required by provisions in the alcoholic beverage code to audit all gross receipt tax accounts every two years regardless of risk or size. Taxing entities that have flexibility are able to utilize an audit select procedure to identify and audit high risk accounts.**
 - The TABC utilizes a limited audit select procedure and a random selection process to identify accounts for audit. However, restrictions in the Alcoholic Beverage Code compress the audit cycle to less than two years on alcoholic beverage gross receipts tax accounts. In fiscal year 1991, TABC audited 7,092 or 87 percent of its 8,133 alcoholic beverage gross receipts tax accounts. In comparison, the comptroller's office audit process includes an audit select procedure to focus its efforts on high risk accounts, as well as a random select procedure. The comptroller's office audits approximately 12,400 or 2.5 percent of more than 503,000 sales tax accounts.
 - The Texas Employment Commission's audit program also includes an audit selection process designed to identify employers likely to under-report wages and under-pay taxes. Other audits are the results of tips or cross-checks with other agencies' records, and some audits are selected at random. The TEC audits approximately 12,000 or four percent of its 300,000 unemployment tax accounts.
 - The State Board of Insurance is developing an audit select procedure which will identify high risk accounts and also consider the geographic location of different accounts since two-thirds of its tax accounts are located in other states. The State Board of Insurance audits approximately 345 or 16 percent of its 2,100 licensed company tax accounts each year.
- ▶ **Because of provisions in the code which require that tax accounts be audited at least once every two years, the TABC spends a great deal of time and money on audits which identify little or no deficiency.**
 - In fiscal year 1991, the TABC conducted a total of 7,092 audits on alcoholic beverage gross receipt tax accounts and identified more than \$7.78 million in deficiencies. Approximately 57 percent or 4,072 of these audits identified zero deficiency. On average, it cost the TABC approximately \$626 to conduct a no deficiency gross receipts tax audit in fiscal year 1991. Based on that per audit cost, the agency spent \$2.55

million or 44 percent of its \$5.78 million audit budget conducting audits which resulted in zero deficiency.

- In comparison, in fiscal year 1991 the comptroller's office conducted a total of 12,416 sales tax audits and identified more than \$268 million in deficiencies. Approximately 36 percent or 4,520 resulted in zero deficiency. On average, it costs the comptroller's office approximately \$844 to conduct a no deficiency sales tax audit. Based on that per audit cost, the comptroller's office spent \$3.8 million or 11.6 percent of its \$32.7 million audit budget on zero deficiency audits.
- ▶ **Because of the audit restrictions which limit the agency's ability to focus audit efforts on high risk accounts, the TABC has a lower dollar return on its alcoholic beverage audit effort than the comptroller's office.**
 - The TABC's inability to focus its audits minimizes its return on audit expenditures. In fiscal year 1991, the TABC audited 87 percent or 7,092 of 8,133 alcoholic beverage gross receipts tax accounts. Of those 7,092 audits, 43 percent identified deficiencies that totalled more than \$7.78 million. Based on audit expenditures, the TABC identified \$1.50 in deficiencies for every \$1.00 spent on auditing.
 - During the same year the comptroller's office audited 2.5 percent or 12,400 of 503,000 sales tax accounts. Of those 12,400 sales tax audits, 64 percent identified deficiencies totaling \$268 million. Based on auditing costs the comptroller's office identified \$10.23 in deficiencies for every \$1.00 spent on sales tax audits. Other factors, such as the high volume of sales tax revenues generated, also affect the comptroller's office's deficiency identification rate.
 - A subset of sales tax accounts, which is similar to mixed beverage tax accounts, is made up of beer and wine entities. In fiscal year 1991, the comptroller's office audited 1.9 percent or 163 of 8,655 beer and wine sales tax accounts. Of those 163 audits, 63 percent identified deficiencies of more than \$1.1 million. Based on audit expenditures, the comptroller's office identified \$4.35 in deficiencies for every \$1.00 spent on auditing.
 - Other agencies are also able to obtain a higher return on their audit expenditures. For example, in fiscal year 1991, the State Board of Insurance identified \$24.50 for every \$1.00 spent on auditing and the TEC identified \$2.14 for every \$1.00 spent on unemployment tax audits.
- ▶ **If the record retention period is expanded to four years, interest should be charged on delinquent taxes.**

- The State Auditor's 1992 report on the TABC recommends extending the record retention period to four years. The report notes that increasing the time between audits could result in lost revenue for the state unless interest is charged on delinquent tax payments. However, the TABC is not authorized to charge interest on delinquent taxes.
- Other state agencies that collect taxes are generally directed to charge interest on late taxes. For example, the comptroller's office is authorized to charge 12 percent interest on delinquent sales tax payments. The Texas Employment Commission is authorized to charge one percent interest per month on delinquent taxes after the agency has received a judgement on late taxes. The State Board of Insurance is authorized to charge nine percent interest on delinquent tax payments.
- The interest charge would act as a deterrent to paying taxes late and discourage the interest free "borrowing" of state tax revenue. In addition, the Auditor's Office indicates that charging interest on late taxes could help offset any increase in deficiencies created by extending the two-year record retention period to four years. The TABC's auditing division estimates that over a 12 month audit cycle, a 12 percent interest charge on delinquent taxes could generate revenue of up to \$1,000,000.

CONCLUSION

Because of provisions in the Alcoholic Beverage Code which restrict the agency's ability to develop a flexible audit process, the agency is required to audit a high percentage of alcoholic beverage gross receipts tax accounts resulting in a high percentage of zero deficiency determinations and low returns on audit expenditures. In comparison, other tax collecting entities in the state are not restrained by provisions in their statutes that require audits of every account or limit the number of years that records must be retained. Removing audit restriction provisions in the code would allow the agency to develop a flexible audit process that includes an audit select procedure that focuses efforts on high risk accounts.

RECOMMENDATION

- **The agency's statute should be changed to modify provisions that restrict the flexibility of the audit process. These changes should:**
 - **extend the period that records must be retained by an alcoholic beverage taxpayer from two years to four years;**

- authorize, instead of require, the commission to examine the tax account of each mixed beverage permittee;
- authorize the agency to charge interest of 12 percent on delinquent taxes; and
- provide clear authorization for the commission to establish audit procedures and requirements it considers necessary.

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Adjusting the statute as recommended would allow the agency to design its audit efforts to more fully utilize its audit select procedure and focus its auditing efforts on high risk and large liability accounts. The agency could also subject smaller liability accounts to a random selection procedure. The combination of the audit select and random select procedure would allow the agency to focus audit staff efforts where the greatest amounts of state tax may be due, while encouraging smaller liability accounts to comply with tax laws through the threat of random audit. Increased ability to develop and implement a flexible audit process would allow the agency to reduce the number of audits and therefore reduce the costs of their audit operations. The charging of interest on late taxes, as recommended by the state auditor, would prevent tax payers from "borrowing" the state's money interest free. The interest charge becomes a particularly important deterrent to delinquent taxes when the time period between audits is extended.

FISCAL IMPACT

Other tax collecting entities in the state that have developed and utilize an unrestricted audit select procedure audit less than 20 percent of their total tax accounts. Removing the statutory restrictions as recommended would allow the agency to develop an audit select procedure to focus audit resources on high risk accounts. Assuming that the agency would subject lower risk accounts to a random selection procedure, the agency can significantly reduce the total number of alcoholic beverage gross receipts tax audits. Based on current per audit costs, if the agency reduced audit coverage to 50 percent of all alcoholic beverage gross receipts tax accounts each year from the current rate of 87 percent, there would be savings of approximately \$1.99 million annually. These savings would result from the elimination of 43 auditor positions and five support positions.

Authorizing the TABC to charge interest on delinquent tax payments would increase the deterrence to paying taxes late or underpaying taxes and revenue generated by the interest charge could offset any increase in deficiencies resulting from extending the record retention period. The TABC's auditing division estimates that a 12 percent interest charge could generate up to \$1,000,000 per year based on their current practices. However, the actual amount of revenue generated from interest under a modified annual audit coverage cannot be calculated at this time.

Fiscal Year	Savings to the General Revenue Fund
1994	\$1,990,000
1995	\$1,990,000
1996	\$1,990,000
1997	\$1,990,000
1998	\$1,990,000

ISSUE 11: The two percent alcohol excise tax discount should be repealed, and the agency should be provided with authority to ensure timely payment of the excise tax.

BACKGROUND

As a strategy to get people to pay their taxes in a timely fashion, certain tax structures provide incentives such as a discount if they pay on time. The discount is usually tied to "compensating" the taxpayer for complex record keeping, acquiring bonds or other special circumstances related to the tax being collected.

In 1935, Texas created such a discount for persons doing business in the state who manufacture, wholesale or distribute alcohol. Under the Texas Alcoholic Beverage Code, the Texas Alcoholic Beverage Commission is required to collect an excise tax from these persons. The discount was set at two percent when originally established and has not been changed.

In 1991, the excise tax generated about \$140 million in revenue and the discount amounted to \$2.85 million. The tax is levied against holders of manufacturer, wholesale and distributor permits or licenses and is based on the amount of liquor, beer, wine and ale that is sold to retailers. Excise taxes are based on the volume, in gallons, of alcoholic beverage that are sold by wholesalers or distributors to retailers for eventual sale to the public. Under certain circumstances manufacturers may also be allowed to sell directly to retailers and are subject to the excise tax at that time. The tax rates vary for each type of beverage but range from \$2.40 per gallon for distilled spirits to \$6.00 per 31 gallon barrel for beer. In fiscal year 1991, approximately 800 permittees and licensees paid alcohol excise taxes. The following chart identifies taxes collected by type of beverage and the amount of discount applied to each beverage.

IMPACT OF EXCISE DISCOUNT BY TYPE OF BEVERAGE - FY 1991			
Beverage	Number of Taxpayers (Monthly Average)	Taxes Owed and Received	Amount of Discount
Beer	371	\$ 86.2 million	\$1.76 million
Distilled Spirits and Wine	206	\$ 49.1 million	\$1.0 million
Ale and Malt Liquor	222	\$ 4.4 million	\$0.09 million
TOTAL	799	\$139.7 million	\$2.85 million

Under current state policy, tax discounts generally are used as a strategy to compensate taxpayers for assisting the state in collecting and remitting a tax. The review focused on whether there is a valid reason for continuing the two percent discount for timely filing of the alcohol excise tax. The review resulted in the following findings.

FINDINGS

- ▶ **The state generally ties discounts to some extra effort required of the taxpayer in collecting the tax.**
 - Cigarette distributors are given a three percent stamp allowance against the cigarette excise tax for providing the service of affixing stamps to the cigarette packages.
 - Retailers who collect the sales tax from their customers are given a two percent discount for remitting these taxes on time. The sales tax timely filer discount is allowed to taxpayers as reimbursement for the costs associated with the collection and forwarding of sales taxes to the comptroller.
 - Discounts are provided to taxpayers that file and pay motor fuels taxes on time. The discounts, which vary by type of fuel, are given to help cover the costs of collecting the tax from retailers of motor fuel products.

- ▶ **There is no longer an additional effort required of alcohol excise taxpayers that justifies the loss in revenue to the state.**
 - Agency personnel indicate that the two percent alcohol excise tax discount has been in place in the Texas Alcohol Beverage Code since 1935. The tax discount was designed to compensate alcohol excise taxpayers (primarily wholesalers and distributors) for affixing tax stamps on the bottles and containers of alcoholic beverages, keeping records, furnishing bonds and properly accounting for the remittance of the tax due. Prior to passage of "liquor by the drink" laws in the early 1970's, affixing the stamps was a labor intensive activity for the wholesalers and distributors that helped justify the discount available to them as taxpayers.
 - However, alcohol excise taxpayers no longer affix tax stamps on bottles and containers of alcoholic beverages for the state. In addition, approximately 80 percent of all alcohol excise taxpayers have achieved bond exempt status and no longer maintain bonds. Record keeping and accounting are activities that all taxpayers must perform regardless of the type of tax they pay.
 - The two percent discount provided to alcohol excise taxpayers resulted in reduced state revenue of approximately \$2.85 million in fiscal year 1991. In

fiscal year 1991, approximately 99.6 percent of the 799 permittees and licensees required to pay the alcohol excise tax paid the tax in a timely manner and were eligible to claim the two percent discount. Only 34 permittees or licensees or 0.4 percent were delinquent in the payment of the alcohol excise tax.

▶ **Discounts are not provided for the other major tax collected by the agency, the mixed beverage gross receipts tax. Taxpayers required to pay this tax are told to pay on time or face penalties.**

-- The state currently collects \$230 million annually from the mixed beverage gross receipts tax. However, the statute does not authorize discounts for timely payment of the mixed beverage gross receipts tax collected from restaurants, bars and other establishments that serve mixed beverages. Instead, the statute provides sanctions for delinquent tax payments.

-- The incentives (penalties, summary suspension, and license or permit cancellation) available to the TABC to encourage timely payment of the gross receipts tax have produced a three percent delinquency rate for payment of the gross receipts tax. Although this delinquency rate is higher than the 0.4 percent rate for the excise tax, there are between 7,500 to 8,000 gross receipts taxpayers compared to only 799 excise taxpayers. In addition, the gross receipts taxpayers are involved in a primarily cash-oriented business.

▶ **Most other states and the federal government do not provide discounts for timely payment of alcohol excise taxes.**

-- All 50 states assess an alcohol excise tax; however, only 10 other states were identified that provide alcohol excise tax discounts. These states include North Carolina, Nevada, Ohio, Tennessee, Florida, South Carolina, Indiana, Nebraska, Oklahoma and Virginia.

-- The federal government collects approximately seven billion dollars in federal alcohol excise tax but provides no discount for timely payment of the tax by manufacturers of alcoholic beverages.

▶ **Sanctions for delinquent payment of taxes are the more common approach used in the collection of major state taxes.**

-- Although sales taxpayers receive a discount for the task of collecting taxes from their customers, the comptroller's office is also authorized to levy penalties, interest charges and fraud penalties on delinquent and deficient taxpayers. Specifically, delinquent sales taxpayers are subject to a five percent penalty during the first 30 days the tax is delinquent and another five percent penalty after 30 days. The comptroller also charges 12 percent interest on all late tax payments and levies a 25 percent penalty if any fraud is found.

- The Texas Employment Commission (TEC) levies a penalty of 1.5 percent per month on employers who are delinquent in paying their unemployment taxes. The maximum penalty that can be charged by the TEC based on their statute is 37.5 percent. Once this maximum is reached, the TEC may levy an interest charge of one percent on the amount due and the penalty. There is no discount for on-time payment of employment taxes.
- The State Board of Insurance is authorized by the Insurance Code to charge interest and assess a penalty against any insurance carrier that fails to file an insurance premium tax return or fail to pay the insurance premium tax when due. The board is authorized to charge nine percent interest on delinquent insurance premium taxes due to the state. In addition, the board can assess a penalty equal to five percent of the amount of taxes due for each month or portion of a month for which such return or payment is late. The penalty cannot exceed 20 percent of the taxes due. There is no discount for on-time payment of insurance premium taxes.
- ▶ **Current sanctions for delinquent payment of alcohol excise taxes differ significantly from other state taxes and are difficult to use.**
 - Under the Texas Alcoholic Beverage Code, delinquent filing of an alcohol excise tax report for distilled spirits and wine is subject to a misdemeanor penalty of not less than \$100 nor more than \$1,000 or by imprisonment in the county jail for no less than 30 days nor more than one year or both. This sanction has been not been used in the past five fiscal years.
 - The TABC can take administrative action to suspend a permit or license if an alcohol excise tax permittee or licensee fails to file or pay taxes when due. However, the agency cannot immediately suspend an alcohol excise tax permittee or licensee for not filing or paying the alcohol excise tax, as it can a gross receipts tax permittee. The agency must schedule and hold a formal hearing in order to suspend a license or permit for failure to pay excise taxes. The agency estimates that the hearing process takes an average of 61 days before a decision is received and a suspension is ordered. If a permittee continuously fails to file returns or remit taxes in a timely manner, the permit or license may be canceled. In fiscal year 1991, the agency canceled two permits for failure to pay excise taxes.
- ▶ **Removing the excise tax discount would have little effect on the consumer.**
 - If the discount were discontinued, the price increase needed to cover any loss to the industry would be insignificant.
 - The current discount received for beer and ale is equivalent to 0.2 cents per six-pack of 12 ounce containers. The discount for a liter of liquor is 1.3 cents for

the excise taxpayer and for table wine the discount is approximately .01 cents per liter.

CONCLUSION

Tax discounts are generally based on some extra task required to be performed by the taxpayer that benefits the state. Originally, the alcohol excise tax discount was based on an extra task that is no longer required. Allowing the discount to continue produces inconsistent treatment between taxpayer groups and results in unnecessary revenue loss to the state.

RECOMMENDATIONS

- **The Texas Alcoholic Beverage Code should be amended to adjust the system for payment of alcohol excise taxes in the following manner:**
 - **Remove the two percent discount for timely payment of alcohol excise taxes. The removal of the discount should be phased in over a four-year period.**
 - **Expand the existing penalty structure for delinquent payment of gross receipts taxes to apply to excise taxes. This structure would include a penalty of five percent, increasing to 10 percent after 30 days, and the authority for summary suspension of a license or permit for failure to pay the tax. Interest charges of 12 percent, as are recommended in the previous issue for the gross receipts tax, should also apply to late payments of the excise taxes.**

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This recommendation will remove the discount for timely payment of the excise tax to make the tax more consistent with other taxes levied by the state where special collection efforts are not required. To phase in this change, the two percent discount should be reduced by one-half of a percent each year over a four-year period. The recommendation would also strengthen incentives for timely payment of the alcohol excise tax by authorizing the commission to apply to delinquent alcohol excise taxpayers the same penalty structure applied against delinquent gross receipts taxpayers.

This recommendation would have little impact on consumers. The excise tax discount is equivalent to 1.3 cents on a one liter bottle of liquor and less than one cent on wine and beer. However, the recommendation would significantly increase revenues to the state.

FISCAL IMPACT

Phasing in the removal of the discount over a four-year period will result in increased revenue of approximately \$710,000 in fiscal year 1994, \$1.42 million in fiscal year 1995, \$2.13 million in fiscal year 1996 and \$2.85 million in fiscal years 1997 and 1998. Strengthening penalties for late tax payments will provide adequate disincentives to prevent any increases in delinquencies.

Fiscal Year	Increased Revenue to the General Revenue Fund
1994	\$0.71 million
1995	\$1.42 million
1996	\$2.13 million
1997	\$2.85 million
1998	\$2.85 million

ISSUE 12: The Texas Alcoholic Beverage Code should be amended to remove prohibitions on charitable contributions and sponsorship by the distilled spirits and wine industries and to require the Texas Alcoholic Beverage Commission to provide guidelines for these activities in rules.

BACKGROUND

The Texas Alcoholic Beverage Code and commission rules, in addition to regulating the distribution and sale of alcoholic beverages, also sets guidelines that regulate the advertising and marketing of alcoholic beverages in Texas. One common marketing technique used by many industries is the financial support or "sponsorship" of public events. For example, many car manufacturers provide financial support for professional golf tournaments and in return receive substantial recognition through the advertising that accompanies public announcements and broadcasting of the tournaments. Alcohol related industries also use this marketing technique. Nationwide, these industries help sponsor many public events including music concerts, sporting events and charitable functions.

In Texas, the laws governing the use of this marketing technique by the alcoholic beverage industry are very specific. The original statutory provisions developed at the end of prohibition, in 1935, prohibited financial gifts or support from the alcohol industry being supplied for any purpose. These restrictions were loosened in the early 1940's when the legislature authorized the beer industry to provide gifts to "civic, religious, or charitable organizations". During this same period, the beer industry was also allowed to sponsor participants involved in games, sports, athletic contests, or revues (musical concerts). In addition, a beer manufacturer or distributor was allowed to use its insignia and brand name on caps, regalia, or uniforms worn by individuals sponsored by the manufacturer or distributor. The distilled spirits and wine industries continue to be prohibited from making charitable contributions to any person, organization or from sponsoring individuals participating in games, sports, athletic events and revues.

One of the underlying premises for the approach set out in the Texas Alcoholic Beverage Code is to make sure that the public is not "induced" to consume alcoholic beverages. The restrictiveness of this 1930's policy has had the effect of prohibiting a large portion of the alcohol industry from supporting what many consider worthwhile causes such as safe ride home programs, responsible consumption seminars and programs aimed at teenagers to help educate them on the effects of alcohol consumption.

The Texas Sunset Act requires that agency practices be evaluated to determine if there are less restrictive alternative methods of performing a regulatory function. As part of the sunset review, the current statutory approach regarding the regulation of charitable contributions and event sponsorship by the alcoholic beverage industry was examined to determine if it was overly restrictive and if there were less restrictive alternatives available. Part of the examination involved a survey of relevant marketing regulations used in 10

other states. These 10 states include those that are major alcohol markets as well as those that border Texas. The overall examination produced the following findings.

FINDINGS

- ▶ **The Texas Alcoholic Beverage Code is inconsistent in allowing the beer industry to advertise and make charitable contributions while prohibiting liquor and wine industries from similar activities.**
 - The code was amended in the early 1940's by the legislature to allow the commission to relax, for the beer industry, certain restrictions regarding charitable contributions made by the industry and to allow the industry to sponsor individuals participating in various athletic and musical events and in revues.
 - Changes to the code authorized the commission to set guidelines allowing the beer industry to donate beer to civic, religious or charitable organizations, trophies of nominal value, and gifts of money or any item of value made by the manufacturer or distributor. The beer industry was also allowed to make gifts of beer as a purely social courtesy to friends and associates not connected to the alcoholic beverage industry. However, the code was not amended to allow the distilled spirits and wine industries to make similar donations.
 - Other changes made in the code authorized beer manufacturers and distributors to sponsor participants involved in games, sports, athletic contests, or revues (musical concerts). In addition, a beer manufacturer or distributor was allowed to use its insignia and brand name on caps, regalia or uniforms worn by individuals sponsored by the manufacturer or distributor.
 - Since 1935, the distilled spirits and wine industries have been and are still prohibited from making gifts to any person or organization and from sponsoring individuals participating in games, sports, athletic events and revues.
- ▶ **The inability of the wine and distilled spirits industries to support events limits the availability of funds for public-oriented programs and events.**
 - Although the gallon consumption of wine and distilled spirits is much smaller than beer consumption, the wine and distilled spirits industries still represent sizeable businesses. The excise taxes paid by the three industry segments in fiscal year 1991 totaled \$140 million - the wine and distilled spirits industries paid 38 percent or \$53.5 million of the total.

- Interviews and correspondence with staff of "Team-Up Houston" indicate that prohibiting two of the three industry components from sponsoring events has limited its ability to expand its efforts. The Team-Up Houston group is part of a national organization designed to focus attention on responsible consumption of alcohol. For example, the group's efforts include a year-round safe ride home program and community education events that focus on the value of using designated drivers. The group reports that not allowing all components of the alcohol industry to support such efforts reduces overall funds available for program expansion and eliminates the benefits public service groups could obtain through competition between the industry components to help promote responsible consumption.
- ▶ **Texas' limits on charitable contributions and sponsorship are more restrictive than sponsorship approaches used by the federal government and other states.**
 - The federal Bureau of Alcohol, Tobacco and Firearms (BATF) guidelines allow event sponsorship by the beer, wine and distilled spirits industries as long as the manufacturer does not directly fund or provide anything of value to a retailer involved in the event. The BATF uses this restriction to guard against attempts to induce retailers to use a manufacturer's products and brands to the exclusion of other manufacturer's products or brands.
 - A survey of 10 states representing major alcoholic beverage markets and neighboring states indicated that seven states (Arkansas, California, Illinois, Louisiana, New Jersey, New York and Oklahoma) have no restrictions on charitable contributions and sponsorships by the alcoholic beverage industry. Florida has minimal restrictions regarding where sponsored events can be held and Wisconsin prohibits the beer industry from sponsoring events. Tennessee has restrictions similar to those applied in Texas.
- ▶ **Representatives of the distilled spirits and wine industries indicate a desire to participate in similar public oriented programs and events if allowed to under the code.**
 - The Distilled Spirits Council of the United States (DISCUS) indicates that their membership is interested in participating in public oriented programs and other charitable events if allowed under the Texas Alcoholic Beverage Code. For example, the Seagram company currently participates, on a nationwide basis, in the "Meals on Wheels" program, which provides meals to the elderly. However, the Texas Alcoholic Beverage Code prohibits the company from participating in the "Meals on Wheels" program in Texas.

- Representatives of the Wine Institute also indicated that their members may participate in these kinds of programs and events in Texas if authorized under the code.

CONCLUSION

Statutory provisions governing the advertising and marketing of alcoholic beverages in Texas are not consistent between the different facets of the alcoholic beverage industry. The beer industry can make charitable contributions and sponsor individuals participating in athletic and musical events - the distilled spirits and wine industries cannot. Many other states and federal regulations allow all components of the industry to sponsor public events.

RECOMMENDATION

- **The Texas Alcoholic Beverage Code should be amended to allow the distilled spirits and wine industries to make charitable contributions and to sponsor individuals' participation in athletic and musical events. The code should also direct the commission to develop, in rule, standards that would govern sponsorship.**
- **In addition, the code should be amended to require that the above changes be incorporated in rule and go into effect by the beginning of fiscal year 1995.**

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These recommendations create a balanced regulatory scheme involving the ability of all segments of the alcohol industry, including the distilled spirits and wine industries, to make charitable contributions and to sponsor participants in athletic and musical events. Directing the commission, through its rule making authority, to develop a regulatory framework for the sponsorship efforts of the alcoholic beverage industry ensures that appropriate safeguards will be developed through a process that allows for public input. The recommendation would be phased in over a one year period, by the end of fiscal year 1994, to provide the commission with time to incorporate needed changes through the rule making process.

FISCAL IMPACT

No fiscal impact for the agency is anticipated. Agency staff, however, would be required to direct considerable effort toward the development of rules during the phase-in period prescribed by the recommendation.

ISSUE 13: The administrative law division of the TABC should be transferred to the newly created State Office of Administrative Hearings.**BACKGROUND**

The administrative law division acts as the judicial arm of the Texas Alcoholic Beverage Commission and conducts administrative hearings on violations of the Alcoholic Beverage Code and the Bingo Enabling Act by licensees and permittees. The division also considers protests made by various agency divisions and the general public against the issuance or renewal of licenses and permits. The administrative law division conducts hearings by following provisions in the Administrative Procedure and Texas Register Act (APTRA), the Texas Civil Rules of Evidence, and the TABC Rules of Practice. In fiscal year 1991, the division expended approximately \$196,000 and consisted of five employees.

Potential cases and protests are received by the legal division which is responsible for preparing and processing administrative cases dealing with violations of the Alcoholic Beverage Code and the Bingo Enabling Act. In fiscal year 1991, the legal division expended approximately \$273,000 and consisted of seven employees. Each case receives a docket number and is assigned to a prosecutor and examiner by a computerized tracking system known as the Hearings Information Processing System. After the case is examined by the prosecutor assigned to the case, a notice of hearing is prepared and the date and time of the hearing is scheduled. The copy of the notice is then routed to the hearings examiner assigned to the case.

After a hearing is held, the hearings examiner issues a proposal for decision and sends copies to all parties involved in the case. The examiner's hearing record and any exceptions and replies are forwarded along with the proposal for decision to the administrator. A final order adopting the proposal is prepared by the administrator if there is agreement with the decision of the examiner. If there is not agreement, the administrator does not adopt the proposal and alternative findings of fact and conclusions of law are prepared and an order to that effect is issued by the administrator. The final order is distributed to all parties in the case.

Once the case has proceeded to final order, alcoholic beverage licensees and permittees may appeal to district court in the county in which the applicant, licensee or permittee resides. Bingo case appeals are filed in Travis county district court. The preparation of the appeal record is the responsibility of the agency's case prosecutor and is handled by the legal division.

During fiscal year 1991, approximately 1,031 cases were docketed for a hearing. Types of cases docketed include failure to remit monthly tax payments or reports, failure to pay sales tax, sale to a minor, and citizens protests. The majority of cases docketed did not proceed

to a hearing because there was resolution prior to the hearing date. Of the 1,031 cases docketed, approximately 48 percent or 492 went to hearing.

Also in 1991, the legislature created the State Office of Administrative Hearings to conduct hearings in contested cases for agencies under the Administrative Procedure and Texas Register Act (APTRA). The hearings function of each agency that does not have a full-time hearings officer is automatically transferred to the central hearings office. Agencies that have full-time hearings officers, like the TABC, must be reviewed by the legislature separately to determine whether hearings conducted by those agencies should be conducted by the central office. The separate review must include the consideration of the independence of the agency's hearings process as well as the quality and cost of hearings at the agency. The review of each of these agencies is required by statute to be completed by September 1, 1993.

As part of the sunset review of the TABC, an analysis was made of the administrative law division and its processes. The analysis focused on the appropriateness of transferring the agency's hearings function to the new State Office of Administrative Hearings. As noted above, the statute that created the central hearings office specifies that the decision to transfer an agency's hearings function should be based on the independence, quality, and cost of hearings at the agency. To assess these criteria, several factors were examined, including the hiring, firing, and evaluation of the hearings staff, adherence to agency and court precedents, and experience of the hearings staff. In addition, information from other states with central hearings offices was also examined. The findings resulting from the analysis follow.

FINDINGS

- ▶ **The administrative law division of the TABC is not as independent as it would be in a separate hearings agency.**
 - The director of the administrative law division is responsible for overseeing the hearings examiners in the division and also acts as an examiner. The director of the administrative law division is hired, evaluated, and can be fired by the administrator who is also responsible for either adopting the examiners' proposals for final orders or developing alternatives.
 - The current structure significantly increases the potential for the administrator to influence the decisions of the director of the administrative law division and agency examiners. Because of the employee-employer relationship between the director of the administrative law division and the administrator, it is reasonable to assume that the decisions of the hearings staff could reflect the will of the administrator.

- As a division of the TABC, the administrative law division becomes a part of the culture of the agency. The administrative law division, the legal division, and the administrator are all located in the same building, although on different floors. This physical proximity leads to the appearance of a lack of independence and increases opportunities for ex parte communications.
- ▶ **The quality of the decisions can be affected by the structure and resources available for the agency's administrative law process.**
 - Even though the administrator does not hear cases, the hearing decision approval process allows the administrator to issue the final orders. The administrator can modify the order after the hearing is completed and issue a final order based on alternative findings of fact and conclusions of law. Although modifications are rarely made, the agency's approach sets up a potential, common in all agencies that have internal hearing processes, for changes to be made to hearing decisions outside the hearings process. Should changes be made in this manner, there is the potential for the quality of decisions to be diminished.
 - The quality of decision-making through a hearings process is bolstered by consistency. One common approach accepted and practiced by the legal community to assure consistency is the review of "precedent" or a comparison of past decisions involving similar fact situations. The Texas Employment Commission and the Public Utility Commission maintain precedent manuals to help their hearings staff make decisions. The TABC does not maintain a precedent manual. Failure to maintain a precedent manual makes it difficult for hearings examiners to decide similar cases consistently. Likewise, the lack of such a manual makes it difficult for prosecutors, defendants, and the general public to determine the possible outcome of a case or to determine the evidence or approach required to present a thorough case.
 - The administrative law and legal division staff at the TABC indicate that although development and maintenance of a precedent manual would be useful, it has not been developed due to lack of time staff can devote to such a project.
- ▶ **Maintaining a separate administrative law division at the TABC may not be as cost effective as providing the hearings function through a central agency.**
 - The current administrative law division at the TABC is small and consists of five staff - two hearings examiners and three support staff. Although the staff has been able to set and conduct the hearings needed, a lack of resources has minimized the staff's ability to develop quality assurance

tools such as the precedent manual mentioned above. Having access to a pool of resources available in a centralized hearings office would assist in development of such quality assurance measures. Such measures can be developed more cost effectively by using small pieces of time from a large number of hearings staff rather than tying up the minimal resources an agency like the TABC can apply to such efforts.

- Other states have experienced cost savings from centralization of hearing functions:

New Jersey centralized hearings examiners from 50 agencies in the early 1980's. Officials from that state estimated in 1988 that the annual cost of operating a central hearings office was \$7.5 million compared to a projected \$20 million budget that would have been required to support the old decentralized hearings system.

Minnesota established a centralized hearings office in 1975. At the time, the central hearings office was established, the Minnesota Public Utility Commission had an annual \$400,000 budget for an "in-house" hearing system. During the first full year of operation of the central hearings office, the cost of hearings on PUC cases dropped 22 percent to \$311,330. The next year cost dropped 25 percent to \$234,000.

- ▶ **Other states routinely include their alcoholic beverage regulatory hearings process in a centralized hearings office.**

- Fifteen states have some form of a central hearings office. In nine of these states, hearings for the alcoholic beverage regulatory agency are conducted in the central hearings office. These states include California, Florida, Missouri, Minnesota, New Jersey, North Carolina, North Dakota, Tennessee and Washington.

- ▶ **The Texas legislature has created an independent hearings agency and expressed its intent to transfer all appropriate hearings functions to that agency.**

- In 1991, the legislature created the State Office of Administrative Hearings to centralize hearings of contested cases under the Administrative Procedure and Texas Register Act (APTRA). Though the enabling legislation did not transfer each state agency's hearings functions to the new office, it clearly states the legislature's intent to do so if the transfer would improve the independence, quality, and cost effectiveness of hearings.

- The legislature could have excluded the TABC from the provisions regarding the central hearings office, but it did not do so. The only

agencies that were exempted from transfer consideration were those agencies exempt from the contested case provisions in the APTRA. These agencies include, for example, the Texas Workers Compensation Commission and the Department of Human Services on matters regarding financial or medical assistance or benefits, the Texas Employment Commission on matters regarding unemployment claims and the Department of Public Safety on matters regarding driver's licenses.

CONCLUSION

The legislature has clearly expressed its intent to consolidate the hearings functions of administrative agencies if such a transfer would improve the independence, quality and cost effectiveness of hearings. The organizational proximity of the administrative law division to the administrator threatens the independence or appearance of independence of the hearings process. The administrator's responsibility for hiring, evaluating and firing the director of the administrative law division creates this appearance and provides opportunities, if so desired, for the administrator to influence the outcome and quality of the hearings process. The cost effectiveness of the current process might also be improved through placement in a larger centralized agency.

RECOMMENDATION

- **The administrative law division of the TABC should be transferred to the newly created State Office of Administrative Hearings.**

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This recommendation would transfer the administrative law division of the TABC, which conducts hearings, to the State Office of Administrative Hearings. The legal division would remain at the TABC and would continue to be responsible for preparing and prosecuting cases for the agency. The resources of the administrative law division would be appropriated to the Office of Administrative Hearings.

In conducting hearings, the central office would consider the applicable substantive rules or policies of the TABC. In this way, the TABC would still determine how broader policy matters or recurring issues will be treated by administrative law judges. Under the provisions of the central hearings statute, the commission would only be able to change a finding of fact for policy reasons, and it must state in writing the reason and legal basis for the change. This provision would make it clear that the administrative law judge who presided over the hearing would be responsible for determining the facts related to the case. It would also make it clear that the commission would have to specify its reasons for modifying the administrative law judge's findings. Although it must comply with the TABC's substantive rules, the central hearings office would conduct hearings under its own

procedural rules, guiding such things as pre-hearing conferences, discovery, and cross examination. Finally, the examiners assigned to the TABC would be housed at the Office of Administrative Hearings.

These provisions would ensure that the administrative law judges would maintain a degree of independence from the commission and would reduce the risk of improper contacts with agency employees acting as parties to contested cases. Transferring the hearings function to a central hearings office would also improve public confidence in the administrative process by increasing the structural objectivity of the effort.

FISCAL IMPACT

Since the TABC administrative law division is small, immediate cost savings due to elimination of personnel are not anticipated. Long-term cost savings are expected but are dependent on the ultimate structure and staffing of the Office of Administrative Hearings.

The recommendation would involve a significant transfer of responsibility from the TABC to the new hearings office. In fiscal year 1991, the administrative law division expended approximately \$195,900 and in fiscal year 1992 was budgeted \$194,800. A similar amount would be needed to be appropriated to the Office of Administrative Hearings for each year of the 94-95 biennium.

ISSUE 14: The statute should be adjusted to provide bingo charities with more opportunities to earn funds by placing controls on bingo hall lease costs and by allowing charities to associate to purchase a hall.

BACKGROUND

In 1981, the Texas legislature passed and the voters approved a constitutional amendment authorizing bingo to be used as a fundraising technique for charities. Under the statute, a county or city can vote to allow bingo games to be conducted by a variety of charitable organizations. For example, the organizations that are authorized to conduct bingo include non-profit organizations such as Veterans of Foreign Wars (VFW) groups, religious societies such as the Knights of Columbus and civic groups such as the Texas Council on Family Violence. The statute also authorized volunteer fire departments to conduct bingo games as a fund raising technique. Most organizations conducting bingo games must be registered and operating in the state for at least three years before a license can be issued. Religious societies must have been operating in the state for at least 10 years and there is no time requirement for volunteer fire departments.

Regulation of bingo was originally given to the Comptroller of Public Accounts but was moved to TABC in 1990. The TABC carries out bingo regulation through its bingo division. The division's licensing section issues conductor, commercial lessor, manufacturer, and distributor licenses. In fiscal year 1991, the bingo division employed 18 staff and processed 3798 new, renewed and amended applications. In addition, approximately \$21.2 million in bingo taxes and \$3.3 million in fees were collected in fiscal year 1991. The playing of bingo in Texas generated over \$652 million in fiscal year 1991. About \$467 million of this money was paid out in prizes and \$52.4 million went to the charities that use bingo as a fund raising technique in the state. The following chart shows the level of bingo licensing activity over the last three fiscal years.

License	FY 89	FY 90	FY 91
Charities	1871	1777	1777
For-profit Lessors	474	402	374
Conductor (charity) Lessors	115	124	149
Lessors who Lease to Conductor Lessors	10	23	45
Distributors of Bingo Goods	24	23	24
Manufacturers of Bingo Goods	12	11	10

Charities run bingo games in buildings they own or in buildings they rent. The rented space is leased from "lessors" who provide the space for a price set out in the leases executed between the charity and the lessor. Over 70 percent of all charities use rented space to play bingo. Since the passage of the Bingo Enabling Act, the number of commercial, or for-profit, lessors has grown steadily. For example, between 1986 and 1991, the number of for-profit lessors increased from 183 to 374. The reasons behind this increase are mainly tied to the increasing popularity of bingo and the fact that most charities are unable to finance their own building purchases and, therefore, must rent or lease space for bingo games.

Concerned about the increasing commercialization of bingo, the 71st legislature, in 1989, changed provisions of the Bingo Enabling Act. The bingo statute was changed to prohibit new for-profit lessors who leased to more than one charity, and the existing lessors were grandfathered. The grandfathered commercial lessors could continue to operate at the current number of charities who leased from them. The statute also authorized charities to become commercial lessors, in addition to conducting games. Since June 10, 1989, newly licensed for-profit lessors are only able to lease to one charity who then can sublease to one or more charities. At the same time, the statute established a \$600 per occasion rent cap on all rent charged by a lessor.

However, before the legislation became effective, the total number of licensed lessors rose considerably. Since the new lessors needed to have charities signed up to play in their halls, all segments of the bingo licensing population increased dramatically. During the one year period prior to the effective date of this legislation, the number of bingo-related license applications processed rose from 6038 to 8032, an increase of about 33 percent.

Bingo is a fundraising activity that allows the charities to raise funds to provide needy persons benefits, opportunities, and assistance. Since charities are non-governmental entities, they relieve the state from some of the burden of assisting needy people in the state. To make sure that the cost of the space needed to conduct bingo does not substantially offset the charities "earnings", the state has established a statutory framework to regulate the balance of interests of everyone involved in the bingo industry. A review of the balancing elements of the framework is contained in the following material.

FINDINGS

- ▶ **The TABC does not determine whether the rent charged a charity to play bingo is "fair and reasonable" as is required in the Bingo Enabling Act.**
 - The Bingo Enabling Act directs the TABC to ensure that rent charged to a charity does not exceed \$600 per occasion. However, the act also directs the TABC to ensure that rent is "fair and reasonable". According to agency staff, no rules have been developed to help define "fair and reasonable rent". The agency has assumed that anything under \$600 is fair and reasonable to the charity.

- ▶ **Rent prices for charities are a large part of the total costs of conducting bingo.**
 - Even with the \$600 cap, rent is a substantial cost element for charities that lease space to play bingo. For example, an analysis of a charity's expenses for three months revealed that rent consumed more than 30 percent of the net proceeds. Rent was the single largest expense for the entire cost of operating bingo for that charity.
 - Lessors charging the \$600 cap can earn substantial lease income. For example, a grandfathered lessor leasing to four charities can earn \$31,200 for the use of a bingo hall for a maximum of 52 sessions each month.
 - From a random sample of lease payments of 100 charities for the first quarter of 1992, the average rent paid is about \$348 per bingo session. If 52 sessions were held in a hall leasing at the average rate, the lessor would earn \$18,096 per month, or \$217,152 per year from charities conducting bingo games.
 - Knowledge of the business costs of the lessor, specifically their expenses related to their lease or property costs, is generally unknown. Although the act gives the agency the authority to request and examine commercial lessor information, this information is not required to be submitted to the TABC.
 - During interviews with members of several charitable associations in Texas, their primary complaint was high rent prices. At a recent conference for bingo conductors in Austin, participants from 15 organizations listed high rent prices as their primary concern over the operation and regulation of bingo.

- ▶ **Other states exert tighter controls over the regulation of rent.**
 - The state of New York requires the commercial lessor to report the reasonable and necessary costs of operation of operating a building for the conduct of bingo and sets the maximum rent that can be charged by a lessor on those figures. This maximum rent is calculated by using a "cost plus" formula. The formula allows a 10 percent profit above allowable costs and expenses. The state sets the reasonable and maximum allowances of lessor expenses. This scheme is designed to closely control the rental of commercial premises for bingo games in order to minimize the exploitation of charities and commercialization of bingo games.
 - The state of Minnesota requires that rent be charged on a per square foot basis (at 6,000 square foot intervals) with rates set by the legislature. The maximum rent for the conduct of bingo is \$400. This scheme for rent calculations restricts the commercialism of lessor/lessee relationships through close controls on rent charged to the charities. For example, based on the experience of a current Texas charity using a commercial hall with a space of 10,000 square

feet, their rent, using the Minnesota scheme, would cost the charity \$300 per occasion. This charity currently pays \$550 per occasion, \$250 more than in Minnesota.

- The Indiana Legislature recently passed legislation that dramatically changed the state's regulatory approach to the conduct of bingo in the state. Specifically, the high level of commercialization in the state was reviewed and legislation was passed that placed more limitations on commercial interests in the conduct of bingo. Indiana's regulation of bingo was changed from a free market (open) system to a more restrictive system by controlling rent and lease agreements. Indiana personnel stated that the changes stemmed from abuses of the charities by commercial interests. The legislation, effective in June of 1992, was therefore designed to end commercialism of bingo in the state and give nonprofit organizations a better chance to use money raised from the conduct of bingo.

Under Indiana's new law, a rent cap of \$200 per day is set, which includes rental expenses (such as chairs, janitorial services, etc.). Facilities are limited to lease to only one charity, the payment of workers or operators is not allowed, and a charity is limited to playing bingo on only two nights per week. Before this legislation passed there were no controls on rent and bingo could be played seven nights per week.

▶ **Unlike other states' approaches, restrictions in the bingo act do not allow charities the full ability to play bingo outside of the lessor/lessee relationship.**

- In Texas, a group of charities are not allowed to co-own a building to play bingo. The TABC can only issue one commercial lessor license to one organization pertaining to the same premise. Although single organizations are able to lease or own buildings and allow other licensed organizations to conduct bingo in these buildings, associations of charities are not allowed those same privileges. This restriction keeps smaller charities from leaving rental situations and completely controlling their own games of bingo.
- In contrast, for-profit commercial lessors that own property to be leased for the conduct of bingo are not required to be single persons or organizations. They may be a person, partnership, corporation, or other group, however organized.
- Since many charities are financially unable to afford the purchase of property alone, they are forced to stay in a lessor/lessee situation. At the end of fiscal year 1991, the bingo division had issued only 149 conductor-lessor licenses to charities to operate and lease their own halls. Agency staff indicate that approximately 1,200 bingo charities, which is about 70 percent of the total, use commercial lessors.

- Six other states surveyed with large levels of bingo activity (Washington, New Hampshire, New York, Massachusetts, Michigan, and Minnesota) allow associations of charities to own a building for the purpose of conducting bingo. Discussions with other states' staff indicate that this approach, along with other provisions in their law, allow nonprofit organizations to operate outside of the lessor/lessee relationship.

CONCLUSION

Nonprofit organizations in the state use bingo as a fundraising activity for their charitable purposes. Currently, these organizations are restricted in their ability to maximize bingo proceeds for charitable purposes. One reason has been that the agency has not used its statutory authority to determine fair and reasonable rent charged to charities for use of bingo halls. This and other factors have resulted in rental costs being one of the highest expense components of conducting bingo. Every dollar used for expenses is not available for the group's charitable purpose. Other states have developed alternate approaches to limit expenses and increase the amount of funds going to charity. However, the current statute does not contain the flexibility or direction for the agency or charities to use other approaches to the operation of bingo.

RECOMMENDATION

- **The statute should be amended to increase opportunities for charities to earn more funds through bingo by:**
 - **requiring the TABC to develop rules governing the determination of fair and reasonable rent for each charity; and**
 - **amending the statute to authorize associations of licensed charitable organizations to co-own buildings for the conduct of bingo.**

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These recommendations are intended to increase the ability of charities to enter into and conduct bingo in a manner that allows for a significant level of proceeds going to charitable purposes. The first recommendation would require the TABC to develop rules that would define what is fair and reasonable rent. Other states have developed alternative regulatory structures that appear to adequately control expenses such as rent. For example, the process used by the state of New York in defining fair and reasonable rent could be considered for use in Texas. The New York approach calculates the standard costs and expenses of the lessor and allows for a reasonable profit over costs. If used in Texas, each lease agreement would be evaluated using the "cost plus" formula to determine whether fair and reasonable rent is being charged.

The second recommendation would allow charities to pool their resources to buy a hall to play bingo. This change would allow those charities who choose to associate for the purpose of buying a hall to control their own costs based on the number of other charities involved and the costs of the building.

FISCAL IMPACT

The process of developing the rules for determining fair and reasonable rent will involve some staff effort, but no new staff would be required. Once the approach is developed, the lease costs would just be another item to check during the licensing process. Therefore, no new costs are anticipated from this recommendation. The recommendation to allow charities to associate to purchase a bingo hall would have no fiscal impact for the state.

ISSUE 15: The agency should be provided with the ability to use fines in bingo regulation to improve its enforcement efforts.

BACKGROUND

The regulation of bingo was transferred from the comptroller's office to the TABC in 1990. The TABC regulates the charities, lessors, and manufacturers and distributors of bingo products primarily through the agency's bingo division. Assistance is also provided by the auditing division that audits bingo activity to ensure that all taxes are paid and that proceeds are distributed for charitable purposes as required in statute. The enforcement division, through its local field offices, also assists in the regulation of bingo activity.

The agency can take enforcement action against a bingo licensee for any violation of the Bingo Enabling Act or rules of the commission. Typically, major types of violations are for activities such as the involvement of a lessor in the operations of a charity's bingo operations or for falsification of information on applications. In fiscal year 1991, the TABC took a total of 253 bingo enforcement actions. Of this number, there were 231 that led to a proposed suspension or revocation. In most cases, the licensee took action to ensure the violations did not reoccur and the enforcement case was settled. The agency suspended or revoked nine licenses in fiscal year 1991. Suspension or revocation of a license are the only formal enforcement tools provided in the statute.

For most regulatory agencies, the state has authorized an enforcement structure that provides an array of increasingly stronger enforcement powers. These powers include the authority to warn a licensee in less severe cases of non-compliance, to suspend for serious violations of the statute, and to cancel or revoke for the most severe violations. Often included in this array is the authority to fine a licensee, which provides regulatory agencies with an enforcement tool that is flexible enough to take action against licensees for a variety of violations. The enforcement structure for bingo regulation was compared to this standard structure for regulatory agencies. The results of this review are described in the following material.

FINDINGS

- ▶ **The TABC's enforcement structure for bingo differs significantly from that given to other regulatory agencies.**
 - Most regulatory agencies have a range of penalties that enable the agencies to graduate penalty severity as well as focus directly on the violator. The Bingo Enabling Act, however, does not provide the authority to fine a violator if that is the most appropriate action to be taken.

- The amount of fines that can be levied in response to a violation vary among agencies. Generally, professional licensing agencies are authorized to assess fines of \$1,000 or less. Agencies which regulate health care or dangers to the environment are usually authorized to assess fines of \$25,000 or less.
- ▶ **The statute does not enable the TABC to focus its assessment of enforcement sanctions solely on the responsible parties.**
 - The enforcement powers set out in the Bingo Enabling Act are limited to suspension and revocation for every area of bingo - charities, lessors, distributors, and manufacturers. Unlike most regulatory structures, fines are not authorized for violations of the Act.
 - If a lessor is suspended, all bingo activity in the hall must stop. As a consequence, the charities cannot conduct bingo games during the suspension period. The charities are unduly penalized for the actions of the lessor when they have not been involved in the violation. For example, a lessor can be suspended for failing to notify the TABC of changes on their application and this offense is unrelated to any charities leasing from the lessor. The suspension of a lessor can cause a loss of revenue for both the related charity and the state. Using fiscal year 1991 statistics, on average, the state could lose over \$225 in taxes per charity per three day lessor suspension, and a charity could lose over \$950 for the same time period.
 - The TABC, in its self evaluation report to the Sunset Advisory Commission, stated that the lack of fines as penalties against a lessor who violates the bingo act unfairly penalizes the charities who play in the hall because they have no place to play during the suspension.
- ▶ **The current penalty structure has been infrequently used against lessors.**
 - Agency staff indicated that there is a reluctance to use suspensions due to the harm it causes the charities when the halls are closed. Only 15 proposed suspensions were sent to lessors in fiscal year 1991. Eight of the cases are still pending and seven cases were settled prior to a hearing. The agency reports that another reason for the low level of enforcement action on lessors is due to the training that was needed when bingo responsibilities were transferred from the comptroller's office to the TABC in 1990.
- ▶ **For charities, a license suspension is virtually identical to a fine.**
 - If a charity's license is suspended, the charity cannot conduct bingo games

during the period of the suspension. This results in the loss of all proceeds for the period of the suspension, which can be a significant loss of revenue. As shown previously, on average, a charity may lose over \$950 in net proceeds for a three day suspension. In comparison, a lessor only loses rental income for the period a lessor's license is suspended. The average rent to a lessor per bingo event is about \$350.

CONCLUSION

The state generally provides regulatory licensing agencies with sufficient enforcement powers to encourage compliance from the businesses they regulate. In addition, sanctions are generally aimed solely at those who are out of compliance with a statute or rules. Currently, the TABC may only suspend or revoke a license when formal action is necessary. In the case of suspension of a lessor's license, the effect is that the charities playing in the lessor's hall are also suspended, regardless of whether they had any role in the violation. While the lessor's suspension is in effect, the charities cannot conduct bingo to raise funds for their charitable purpose.

RECOMMENDATION

- **The statute should be modified to authorize administrative penalties up to \$5,000 per violation against lessors for violations of the Bingo Enabling Act and agency rules.**

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The recommendation would provide the agency with a standard set of enforcement powers for bingo regulation similar to that of other regulatory agencies. This change would give the TABC greater flexibility to set penalties to fit the severity of the violation, taking into account the past history of the licensee and the extent to which the licensee may have acted without knowledge or intent to violate the law. In addition, the availability of fines as an enforcement tool would allow charities to conduct bingo in lessor halls even if the lessor commits an offense that warrants a sanction.

The agency's administrative penalty authority for bingo regulation would be modeled after the standard sunset approach used in the past to provide administrative penalties in other regulatory agencies. Under this approach, the statute sets out specific factors for the agency to consider when determining the amount of a penalty. This approach would also establish the licensee's right to appeal a penalty and would require that all penalties be deposited in the general revenue fund.

The agency would also be required to follow a standard method for using administrative penalty authority that would be set out in statute. Further details, including a penalty

structure would be adopted by the commission in rules. The adoption of the penalty mechanism in rules provides the public and the regulated industry with input in the day-to-day working of the administrative penalty system. Setting a maximum penalty of \$5,000 per violation is expected to be an effective deterrent for violations of the Bingo Enabling Act or related agency rules.

FISCAL IMPACT

The use of administrative fines would result in some revenue for the state but the amount cannot be estimated at this time. Some additional staff effort would be necessitated for the development of the initial rules associated with administrative penalties; however, this effort would not require additional agency staff.

***ACROSS-THE-BOARD
RECOMMENDATIONS***

From its inception, the Sunset Commission identified common agency problems. These problems have been addressed through standard statutory provisions incorporated into the legislation developed for agencies undergoing sunset review. Since these provisions are routinely applied to all agencies under review, the specific language is not repeated throughout the reports. The application to particular agencies is denoted in abbreviated chart form.

Texas Alcoholic Beverage Commission			
APPLIED	MODIFIED	NOT APPLIED	ACROSS-THE-BOARD RECOMMENDATIONS
			A. GENERAL
		X	1. Require public membership on boards and commissions.
	X		2. Require specific provisions relating to conflicts of interest.
**			3. Provide that a person registered as a lobbyist under Article 6252-9c, V.A.C.S., may not act as general counsel to the board or serve as a member of the board.
		*	4. Require that appointment to the board shall be made without regard to race, color, handicap, sex, religion, age, or national origin of the appointee.
		*	5. Specify grounds for removal of a board member.
		*	6. Require the board to make annual written reports to the governor and the legislature accounting for all receipts and disbursements made under its statute.
**			7. Require the board to establish skill-oriented career ladders.
**			8. Require a system of merit pay based on documented employee performance.
	X		9. Provide for notification and information to the public concerning board activities.
		*	10. Place agency funds in the treasury to ensure legislative review of agency expenditures through the appropriation process.
X			11. Require files to be maintained on complaints.
X			12. Require that all parties to formal complaints be periodically informed in writing as to the status of the complaint.
**			13. Require development of an E.E.O. policy.
X			14. Require the agency to provide information on standards of conduct to board members and employees.
		*	15. Provide for public testimony at agency meetings.
X			16. Require that the policy body of an agency develop and implement policies which clearly separate board and staff functions.
X			17. Require development of accessibility plan.
X			18. Place agency under the state's competitive cost review program.

* Already in law -- no statutory change needed.

** Already in law -- requires updating to reflect standard ATB language.

Texas Alcoholic Beverage Commission (cont.)			
APPLIED	MODIFIED	NOT APPLIED	ACROSS-THE-BOARD RECOMMENDATIONS
			B. LICENSING
		X	1. Require standard time frames for licensees who are delinquent in renewal of licenses.
		X	2. Provide for notice to a person taking an examination of the results of the exam within a reasonable time of the testing date.
		X	3. Provide an analysis, on request, to individuals failing the examination.
		X	4. Require licensing disqualifications to be: 1) easily determined, and 2) related to currently existing conditions.
		X X	5. (a) Provide for licensing by endorsement rather than reciprocity. (b) Provide for licensing by reciprocity rather than endorsement.
		X	6. Authorize the staggered renewal of licenses.
		X	7. Authorize agencies to use a full range of penalties.
		X	8. Specify board hearing requirements.
		X	9. Revise restrictive rules or statutes to allow advertising and competitive bidding practices which are not deceptive or misleading.
		X	10. Authorize the board to adopt a system of voluntary continuing education.

* Already in law -- no statutory change needed.

** Already in law -- requires updating to reflect standard ATB language.

MINOR MODIFICATIONS

Discussions with agency personnel concerning the agency and its statute indicated a need to make minor statutory changes. The changes are non-substantive in nature and are made to comply with federal requirements or to remove out-dated references. The following material provides a description of the needed changes and the rationale for each.

**MINOR MODIFICATIONS TO THE STATUTE
TEXAS ALCOHOLIC BEVERAGE COMMISSION
TEXAS ALCOHOLIC BEVERAGE CODE**

Change	Reason	Location in Statute
1. Delete the section.	The section relating to a change of license or permit expired in 1980.	Section 11.491
2. Add " <u>or tax security</u> " to bond requirements in several sections of the Act.	The agency was authorized in 1979 to allow various types of tax security for designated licenses and permits in place of bonds. However, several sections were missed during the process. This change would formally authorize current practice.	Section 204.01 (h) Section 204.01 (i)
3. Add " <u>letters of credit or certificates of deposit</u> " following "bonds" in the subsection of the Act.	The agency was authorized in 1977 to allow various types of tax security for designated licenses and permits in place of bonds. However, several sections were missed during the process. This change would formally authorize current practice.	Section 204.03 (d)

