

FISCAL NOTES

A Review of the Texas Economy from the Office of Susan Combs, Texas Comptroller of Public Accounts

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change **BREWING** in Texas

Recent legislation gives craft beer a boost

By Patrick Graves



“Beer has among the most complicated regulatory frameworks of any product in the country.”

BART WATSON
staff economist,
Brewers Association

Since the craft brewing revolution began at the end of the 1970s, America’s beer industry has evolved beyond recognition, as the bewildering variety of brands on offer in any well-stocked grocery will attest. Despite its relatively small sales, craft brewing is growing fast — and supports more than half of all brewery jobs in Texas.

But Texas laws regulating the sale of beer hadn’t seen anything like the same degree of change — and the state’s small brewers say they’ve been a persistent problem.

After years of frustration, though, the 2013 legislative session enacted some reforms intended to help Texas’ burgeoning craft brewing industry. New laws that took effect in June give craft breweries and brewpubs some of the same marketing flexibility enjoyed by their counterparts in the liquor and wine industries, and may help them compete more effectively.

Small but Thriving

Unlike the major companies, craft brewers produce relatively small amounts of their products, generally using traditional brewing methods and avoiding preservatives and cheap “adjuncts” such as corn and rice.

According to the Brewers Association, a national trade group, craft brewers accounted for more than 6 percent of total U.S. beer production volume in 2012, and nearly 12 percent of the U.S. beer market’s \$99 billion in revenues.

So at present, craft brewers have a small share of the market — but they’re the only sector of the industry that’s growing significantly in the U.S. The industry publication *Beverage Dynamics* recently reported that consumption of “mainstream” beer categories fell in 2012, while craft beer consumption rose by 14.6 percent.

And craft brewing creates jobs. In 2011, according to the Texas Craft Brewers Guild, the state’s craft breweries and brewpubs directly accounted for 1,244 jobs — about 51 percent of all Texas brewery jobs — and supported another 2,208 wholesale and retail positions.

Roll Out the Changes

In last year’s legislation, perhaps the biggest winners were the brewpubs — hybrid retail drinking



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NEW TEXAS LAWS

The 2013 Legislature approved reforms allowing Texas brewpubs to market their products off site, by selling to distributors or directly to retailers. Other craft brewers will be allowed to sell beer directly to the public for on-premises consumption.

For detailed information on the new legislation, [see Craft Brewing Laws and Legislative Changes](#) or visit: <http://www.texascraftbrewersguild.org/government-affairs/>

http://www.tabc.state.tx.us/public_information/notices/2013/Summary-of-Bills-2013.asp



and dining establishments that primarily make and sell their own beer. Texas has 53 of them at present.

Barton Springs Beer Hall serves craft beer at the Austin City Limits Festival.

Under the new law, Texas brewpubs, like wineries, now can market their products off site, by selling either to distributors for resale or directly to retailers. The latter sales, called “self-distribution,” are restricted to brewpubs holding wine and beer retailer’s permits, and are allowed only for what they brew themselves. These sales to retailers are limited to no more than 1,000 barrels per location per year, not to exceed a combined 2,500 barrels annually for all brewpubs with the same owner.

Photo by Dave Mead

In addition, brewpub production limits have been doubled from 5,000 to 10,000 barrels a year.

Production or packaging breweries — industry parlance for craft brewers without pubs — got some of what they’ve been after as well. Until the recent legislative changes, these brewers couldn’t sell their products directly to the public, even after tours of their facilities. (Such tours are common — and popular.)

Now, those producing no more than 225,000 barrels annually can sell up to 5,000 barrels a year for on-premises consumption. If they produce less than 125,000 barrels annually, they can “self-distribute” up to 40,000 barrels a year to retailers in addition to sales made to distributors.

Makers of liquor and wine still hold some advantages over brewers, however.

Texas distilleries and wineries can sell directly to customers for both on- and off-premises consumption. Our wineries can ship their products directly to Texas customers (although the amounts are capped). Texas breweries and brewpubs, by contrast, still can’t ship directly to in-state customers.

TOP 5 STATES FOR CRAFT BEER ECONOMIC OUTPUT, 2012



<http://www.brewersassociation.org/pages/government-affairs/economic-impact-data>



The Regulatory Labyrinth

The past and present inequities of beer law in Texas spring from an extraordinarily complex regulatory structure.

“Beer has among the most complicated regulatory frameworks of any product in the country,” says Bart Watson, staff economist of the Brewers Association. “It’s a labyrinthine system set up after Prohibition.”

Prior to Prohibition, some producers used heavy-handed business practices that pressured purveyors to promote their products aggressively, and exclusively. Some watering holes became known as “tied houses,” selling only one company’s brands.

After Prohibition’s repeal in 1933, many states added an intermediate level of suppliers to counteract such coercion and encourage competition — “middlemen” who were supposed to act as buffers against the abuses of producer influence. This arrangement of makers, distributors and retailers, commonly called the three-tier system, became common throughout the nation. Texas has used a version of the system since 1935.

Concurrent with the rise of craft brewing, however, has been the global consolidation of multiple aspects of the beer industry. Roughly 80 percent of all beer sold worldwide is brewed by companies owned either by A-B InBev or MillerCoors — and

Scott Metzger’s Freetail Brewing Co. is San Antonio’s second-oldest brewpub. Its name refers to Texas’ official flying mammal, the Mexican freetail bat.

Photo by Michael Donk, BrewBokeh.com



Craft beer is a new addition to the Austin City Limits Festival.

Photo by Dave Mead

there are rumors that the two giants might merge. Similar consolidation has spurred an increase in the number of large “mega-distributors.”

Against this backdrop, the three-tier system’s historical lines dividing beverage alcohol producers, suppliers and sellers seem to be blurring.

And Watson explains that legislators are recognizing that more locally owned breweries and brewpubs won’t lead to the problems seen before Prohibition. “[They] want to harness the economic potential without harming the balance,” he says.

Roadblocks Remain

Some distributors embrace the new normal. Rick Donley, president of the distributor trade group Beer Alliance of Texas, told state senators last spring that the three-tier system, though not broken, “needs tweaking to reflect changes in the marketplace.”

But the boundaries separating the three tiers’ business activities aren’t changing fast enough for everyone. Brewpubs, for example, must sell their beer to distributors and buy it back to sell it at remote, unlicensed locations such as fairs and other public events.

Furthermore, brewpubs can sell their distribution rights, but production breweries can’t.

Texas is the only state with this restriction in law, says Andrew Christon, a leading beverage industry expert who represents distributors.

Some of the better-established craft brewers want the option to sell their distribution rights so that they can use the proceeds to expand production capacity and grow their brands.

“The state statutes were designed to prevent brewers from investing in and owning/controlling distributors,” Christon’s firm, Ippolito Christon & Co., has pointed out. “[This] is a situation where the distributor is making an investment in the brewer’s brands, not the other way around.”

These objections notwithstanding, Carolyn Beck, the Texas Alcoholic Beverage Commission’s communications and governmental relations director, points out that the new craft brewer production and distribution ceilings are relatively high. Limitations are to be expected, she said, given that sales by producers are exceptions to the three-tier system the Legislature continues to support.

Despite the remaining roadblocks, the outlook for craft beer’s



The fermentation tanks at Live Oak Brewing Company in Austin. The Texas Craft Brewers Guild projects more than 800 percent growth in Texas craft brewing during the next six years.

Photo by Live Oak Brewing Company

CRAFT BREWING LAWS AND LEGISLATIVE CHANGES, 2013					
SUBJECT	BILL	AUTHOR	STATUTE SUMMARY		EFF. DATE
			PREVIOUS LAW	NEW LAW	
Brewpub Production and Sales for Resale	SB 515	Eltife	Production capped at 5,000 bbl./yr. Sales for on-premises and off-premises consumption allowed. No sales for resale or direct to consumer shipping sales allowed. Sales of own products away from the licensed premises prohibited.	Production cap raised to 10,000 bbl./yr. Sales of own products to wholesalers & distributors for resale allowed. Specific permit holders selling only their own products may sell to retailers (up to 1,000 bbl.) & qualified persons outside Texas. Total sales of all products to Texas retailers capped at 1,000 bbl./yr. for each licensed brewpub location and 2,500 bbl./yr. for all brewpubs operated by same licensee. (Retail sales amount included in 10,000 bbl. production limit.)	June 14, 2013
Brewer’s Permit (Ale/Malt Liquor) Self-distribution	SB 516	Eltife	Producers making less than 75,000 bbl./yr. (total malt beverages) could self-distribute any amount (sell directly to retailers). No direct consumer, in-state shipping sales allowed.	Raises production limit for self-distribution to not more than 125,000 bbl./yr. Qualifying producers may self-distribute up to 40,000 bbl./yr. (sell direct to retailers) after obtaining a Brewer’s Self-Distribution Permit.	June 14, 2013
Manufacturer’s License (Beer) Self-distribution	SB 517	Eltife	Producers making less than 75,000 bbl./yr. (total malt beverages) could self-distribute any amount (sell directly to retailers). No direct consumer, in-state shipping sales allowed.	Raises production limit for self-distribution to not more than 125,000 bbl./yr. Qualifying producers may self-distribute up to 40,000 bbl./yr. (sell direct to retailers) after obtaining a Manufacturer’s Self-Distribution License.	June 14, 2013
Brewers and Manufacturers	SB 518	Eltife	Producers may dispense free malt beverages on site and conduct samplings off premises but not sell directly to consumers or sell or serve other producers’ beverages.	Producers making less than 225,000 bbl./yr. combined (all malt beverages) may sell up to 5,000 bbl./yr. of what they make to customers for on-premises consumption (until midnight 7 days a week).	June 14, 2013
Brewers, Manufacturers, Brewpubs & Distributors	SB 639	Carona	Silent, although agency bulletin prohibited “reach-back pricing.”	Clarifies the prohibition on producers raising prices based on distributors’ resale price increases. Prohibits producers, but not distributors, from selling their distribution rights via territorial agreements.	June 14, 2013

SOURCES: Texas Alcoholic Beverage Commission, Texas Legislature Online, House Research Organization

future in Texas is bright. Brewpubber Scott Metzger, who once taught economics at the University of Texas at San Antonio,



**SCOTT
METZGER,**
Founder and
CEO, Freetail
Brewing Co.

stands by a forecast he made for the Texas Craft Brewers Guild in 2012: an 800+ percent growth rate and an annual \$5.6 billion overall economic impact by 2020.

He also cites an informal survey of his beer-making brethren indicating that they are poised to invest \$22 million in capital improvements and expansion projects and to add more than 100 new jobs.

The Brewers Association's Watson puts the current economic impact of craft beer in Texas at \$2.3 billion for 2012, supporting slightly more than 20,000 jobs paying more than \$700 million in wages. His data put Texas seventh among states in craft beer production in 2012 and eighth in its total number of craft brewers.

But Texas was in the bottom 10 percent of states for craft brewers per capita. So there's plenty of room for expansion. Cheers! **FN**