

ECONOMIC DEVELOPMENT SALES TAX 101: SOME BASIC TERMINOLOGY

The **Development Corporation Act of 1979 (the Act)** is the law that sets the ground rules for the use of the economic development sales tax. The Act is found in Article 5190.6 of Vernon's Civil Statutes. Sections 4A, 4B, and 4C of the Act relate to the economic development sales tax.

Economic Development Corporations are the legal entities with the statutory authority to spend economic development sales tax dollars. The corporations are city-chartered and governed by a city-appointed board of directors. Corporations are typically referred to either as "4A" or "4B" depending on the type of economic development sales tax uses approved by local voters.

The tax that almost got away.

Nearly fifteen years after it was created, the economic development sales tax has lived a colorful life. When the Texas Legislature meets each odd-numbered year, lawmakers file bills by the dozens to nip and tuck at the tax. As the years passed, however, the tax moved further and further away from its original economic development roots.

The first major change to the tax was passed just two years after the original 4A tax was enacted. In 1991, Texas lawmakers authorized cities in four Texas counties (Bexar, Dallas, Harris, Tarrant) to ask voters to enact a more flexible version of the original 4A tax, commonly called the "4B tax" (SB 376). Revenues generated by this new tax could be used to finance not only manufacturing and industrial projects, but also quality of life improvements such as parks, sports stadiums, tourism facilities, and certain types of transportation infrastructure.

As the economic development sales tax grew more popular, lawmakers were increasingly pressured to expand the number of cities eligible to adopt the tax and to loosen the restrictions on how the tax dollars could be spent. In 1993, the law was changed to allow any city that met the population and tax-rate criteria for collecting the 4A tax to collect the 4B tax instead—with voter approval, of course. By 1993, cities in all but two Texas counties (El Paso and Travis) were eligible to enact the 4B tax with voter approval.

A few years later in 1997, lawmakers authorized cities that collect the 4A tax to seek voter approval to undertake projects authorized under 4B of the Development Corporation Act (HB 1525). That same year, lawmakers established a mandatory reporting system requiring communities that collect the economic development sales tax to submit annual expenditure reports to the Comptroller of Public Accounts (HB 1410).

In 1999, two short years later, Texas legislators expanded allowable uses of the economic development sales tax to include job training, targeted infrastructure, and educational facilities (HB 3029).

In 2001, lawmakers amended Section 4B to allow communities to

spend economic development sales tax dollars on water supply facilities and water conservation programs and incentives—with specific voter approval (HB 2379). That same year, lawmakers passed HB 3178 requiring designated persons to attend a mandatory training seminar on the administration of the economic development sales tax every two years. Like the mandatory annual reporting requirements passed in 1997, the driving force behind HB 3178 were concerns on the part of lawmakers that some communities were not using sales tax dollars in accordance with state law.

Most recently, during the 2003 regular legislative session, lawmakers enacted some major changes to the Development Corporation Act with the passage of HB 2912.

HB 2912—A POSITIVE STEP IN THE RIGHT DIRECTION

HB 2912 was authored by Representative Mark Homer of Paris and sponsored by Senator Ratliff. Following is a summary of the most significant changes made by HB 2912 and what they mean to your community:

Definition of "Project" & Primary Jobs

The heart and soul of the Development Corporation Act is the term "project." Over the years, lawmakers have broadened the definition of project to accommodate the needs of their constituents. HB 2912, in an effort to refocus the tax back on economic development, retools the definition of project by focusing the use of the economic development sales tax—with some exceptions—to projects that create or retain "primary jobs." Other significant changes to the term "project" include:

- Clarifying that 4A and 4B corporations may undertake "expenditures" on behalf of a business (i.e. provide financial incentives such as loans or grants).
- Clarifying that 4A and 4B corporations may provide financial assistance to "regional or national corporate headquarters."
- Restricting the use of economic development sales tax revenues to "primary job training facilities" for use by institutions of higher education, rather than general education facilities.
- Prohibiting the use of 4B revenues to build learning centers (e.g. libraries) and municipal buildings (e.g. city halls).
- Prohibiting the use of 4A revenues to build sewage and water furnishing facilities for the general public.

HB 2912 defines a primary job as a job that is: (1) available at a company for which a majority of the products or services of that company are ultimately exported to regional, statewide, national, or international markets, infusing new dollars into the local economy; and (2) included in one of the following sectors of the North American Industry Classification System (NAICS)

CHART OF NAICS CODES

111	Crop Production
112	Animal Production
113	Forestry and Logging
11411	Commercial Fishing
115	Support Activities for Agriculture and Forestry
211-213	Mining
221	Utilities
311-339	Manufacturing
42	Wholesale Trade
48-49	Transportation and Warehousing
51	Information, excluding movie theaters (51213) and drive-in theaters (512132)
523-525	Securities, Commodity Contracts, and Other Financial Investments and Related Activities; Insurance Carriers, Related Activities; Funds, Trusts, and Other Financial Vehicles
5413, 5415, 5416,	Scientific Research and Development Services
5417, and 5419 551	Management of Companies and Enterprises
922140	Correctional Institutions

RETAIL DEVELOPMENT

Although HB 2912 restricts the extent to which 4A & 4B dollars may be used to fund retail or commercial developments, the new law does not prohibit corporations from supporting these types of projects. In fact, corporations may continue to provide retailers with infrastructure assistance in the form of streets and roads, rail spurs, water, gas, and electric utilities, drainage and related improvements, telecommunications and internet improvements. What's more, corporations may provide job training assistance to retail and commercial projects so long as the employer meets the wage requirements specified in the Act.

In terms of new restrictions, corporations may no longer provide retailers with free land, buildings, equipment, facilities cash grants for relocation costs, loans, or other direct financial incentives.

Job Training

In 1999, Texas lawmakers added job training to the list of eligible 4A and 4B projects. However, the new provision had a catch. In order to qualify for job training incentives, companies had to pay wages equal to or greater than the average county weekly wage. In practice, this well-intentioned provision severely restricted the ability of economic development practitioners to spend 4A or 4B revenues on job training.

HB 2912 amended the 1999 provision by revising the wage requirement. Under the new law, 4A or 4B tax revenues may be used for job training if the benefiting business commits in writing to either: (1) pay at least equal to the prevailing wage for the applicable occupation in the local labor market or (2) increase its payroll to pay wages that are at least equal to prevailing wage for the applicable occupation in the local labor market.

Performance Agreements

HB 2912 added new language to the Development Corporation Act requiring 4A and 4B corporations to enact "performance agreements" before providing direct incentives or making an expenditure on behalf of a business. A performance agreement is a written document designed to protect the interests of local taxpayers by putting a businesses' job creation or capital investment commitments in writing and by linking the payment of any financial incentive to the business fulfilling its written commitments (i.e. clawbacks).

HB 2912 requires that the performance agreement contain a schedule of planned payroll, job creation and capital investment, and include clawback language. HB 2912 also requires the board of directors of a 4A or 4B development corporation to execute a written agreement in connection to the payment of a commission, fee, or other compensation to an agent, broker, or other third party involved in a business recruitment or development transaction.

THE DO'S AND DON'TS OF THE ECONOMIC DEVELOPMENT SALES TAX.

This practitioners guide is intended to provide a quick snapshot of what you can and can't do with economic development sales tax dollars—not as a substitute for the advice and counsel of your local attorney or the in-depth training you can receive at one of the Texas Economic Development Council's regional training seminars.

Here's what you CAN do...

4A Corporations

- Land, buildings, equipment, facilities, improvements, and expenditures related to:
- Manufacturing, industrial, research & development, recycling, small warehouse and corporate headquarter facilities.
- Distribution centers.
- Closed or realigned military bases.
- Job training for primary jobs and commercial/retail.
- Business airport facilities.
- Port-related facilities to support waterborne commerce.
- Clean up of contaminated project sites (with a special election and specific ballot language).
- Job training and infrastructure assistance to retail or commercial projects.
- 4B projects with voter approval.

4B Corporations

- Everything authorized under 4A of the Development Corporation Act, including retail and commercial projects with the same restrictions. • Water supply facilities (with a special election and specific ballot language)
- Projects that improve a community's quality of life, including parks, professional and amateur sport and athletic facilities, tourism and entertainment facilities, affordable housing, and other improvements or expenditures that promote new or expanded business activity that create or retain primary jobs.

Here's what you CAN'T do...

4A Corporations

Facilities with the following primary purposes:

- Transportation
- Solid waste disposal and sewage
- Furnishing of water and sewage services to the general public
- Air or water pollution control

4B Corporations

- Learning centers (e.g. libraries)
- Municipal buildings (e.g. city halls)
- K-12 educational facilities

THE ECONOMIC DEVELOPMENT SALES TAX—WORKING FOR TEXAS

The economic development sales tax is the state's largest local revenue source for economic development. The best way to protect the tax for years to come is to use it with caution, care, and common sense. The Texas Economic Development Council and the Texas Economic Development Sales Tax Association will continue to advocate, educate, and inform economic development professionals on developments related to the tax, including best practices and statutory changes.

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Other useful resources on the economic development sales tax can be found:

Economic Development Corporation Report, Fiscal Years 2000 and 2001, October 2002. This report, published every two years by the Comptroller of Public Accounts, summarizes and analyzes expenditures made by 4A and 4B development corporations. The report is produced to comply with legislative reporting requirements established by HB 1410 in 1999. The full report may be downloaded from Comptroller's web site at www.cpa.state.tx.us.

Economic Development Sales Tax, September 2003. This brochure, also published by the Comptroller of Public Accounts, provides a technical summary of the economic development sales tax, including detailed information on how communities must administer the tax. The brochure can be downloaded from the Comptroller's web site at www.cpa.state.tx.us.

Handbook on Economic Development Laws for Texas Cities, 2002. This 320 page report produced by the Intergovernmental Relations Division of the Office of Attorney General, provides a comprehensive legal and technical overview of major economic development laws, including the economic development sales tax. The full report can be downloaded from the Office of Attorney General's web site at www.oag.state.tx.us. An updated version of this report, reflecting the changes made by HB 2912, should be available in 2004.

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