

The Texas Economic Development Sales Tax: A PRIMER FOR LOCAL OFFICIALS

2008 Update

BACKGROUND

The economic development sales tax is the undisputed workhorse of local economic development in Texas. First created in 1989 to give smaller Texas communities the financial wherewithal to build effective economic development programs, the tax today serves as the backbone of local economic development efforts in more than 450 cities across the state.

The broader “4B tax” remains the more popular choice for Texas communities. As of December 2007, 556 Texas cities have adopted the economic development sales tax: 337 impose the 4B tax, 116 impose the 4A tax, and 103 impose both the 4A and 4B tax.

Although the economic development tax is nearly twenty years old and has been the subject of many legislative changes, the original intent of this critical tool remains the same: helping communities attract primary jobs and create wealth for its citizens.

RECENT CHANGES TO THE ECONOMIC DEVELOPMENT SALES TAX

Over its lifetime, hundreds of bills have been filed to change the rules surrounding the economic development sales tax. Although not all of the bills filed passed (fortunately!), several major bills have helped shape the tax into what it is today. One of those bills was HB 2912, which passed in 2003 with the support of the Texas Economic Development Council (TEDC). The bill eliminated loopholes in the Development Corporation Act (DCA) that enabled Texas communities to use 4A and 4B tax revenues in ways never envisioned, such as building fire stations and city halls.

In 2005, Texas lawmakers passed HB 2928 which reinserted some of the loopholes that were eliminated back in 2003. Although the TEDC remained neutral on language in HB 2928 that granted small, rural communities additional flexibility to attract retail development, our members strongly opposed “carve out” language that gave certain communities their own set of rules.

The most recent legislative session (2007) was a surprisingly quiet one for the economic development sales tax. Only a handful of bills passed, such as SB 1089 by Shapiro which allows 4A or 4B corporations to spend economic development sales tax revenues on light rail, commuter rail, or motor buses and HB 3440 by Parker which adds certain facilities and infrastructure located on or adjacent to an airport facility to the definition of eligible project for 4B corporations. Another bill, SB 1523 by Wentworth, which contained language waiving the public hearing requirement for 4B primary job projects in communities with under 20,000 residents, also passed in the final days of the legislative session.

KEY TERMINOLOGY

The Development Corporation Act of 1979 (DCA) is the law that regulates the use of the economic development sales tax. The DCA was originally found in Article 5190.6 of Vernon’s Civil Statutes, however the laws governing the economic development sales tax are being recodified in the Local Government Code.

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.

Primary Jobs are jobs that infuse new dollars into the local economy by creating or selling a product or service that is ultimately exported to regional, statewide, national, or international markets.

DIFFERENCES BETWEEN THE 4A AND 4B TAX

This practitioners guide offers a quick snapshot of what you can do with economic development sales tax dollars. It is in no way intended to substitute for the counsel of your local attorney or the in-depth TEDC training materials.

4A Eligible Projects

Land, buildings, equipment, facilities, improvements, and expenditures related to:

- Manufacturing, industrial, research & development, recycling, small warehouse and corporate headquarter facilities, and distribution centers.
- Closed or realigned military bases.
- Job training for primary jobs and commercial/retail.
- Business airport facilities and port-related facilities.
- Clean-up of contaminated project sites (with a special election and specific ballot language).
- Infrastructure assistance to retail or commercial projects.
- Business-related sewer utilities and site improvements.
- Beach remediation in Gulf communities required or suitable to promote or develop new or expanded business enterprises.
- Projects designed to attract new military missions, prevent the closure of existing missions, and redevelop a closed or realigned military base.
- General airport facilities for communities located 25 miles from US/Mexico border only.
- Light rail, commuter rail, or motor buses.
- 4B projects with voter approval.

4B Eligible Projects

- Everything authorized under 4A of the DCA, 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.
- Projects designed to attract new military missions, prevent the closure of existing missions, and redevelop a closed or realigned military base.
- Sewer or solid waste disposal facilities in Hidalgo County.
- Direct incentives for retail development in communities with fewer than 20,000 residents and certain land-locked cities.
- Hangars, airport maintenance and repair facilities, air cargo facilities, related infrastructure located on or adjacent to an airport facility.
- Airport facilities provided that the eligible municipality enter into an approved development agreement with an entity that acquires a leasehold or other possessory interest from the economic development corporation.

Legislative History of the Economic Development Sales Tax

1979

Development Corporation Act passed, authorizing cities to create economic development corporations.

1989

4A tax authorized to provide funding source for recruiting and retaining manufacturing and industrial projects.

1991

4B tax authorized for broader community development projects.

1997

- State reporting requirement enacted.
- 4A corporations authorized to undertake 4B projects with voter approval.

1999

Allowable 4A and 4B projects expanded to include targeted infrastructure, job creation and retention, job training, and educational facilities.

2001

- Allowable projects expanded to include R&D facilities (4A/4B).
- Training requirements established.

The economic development sales tax statute 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).

Eligible NAICS Sectors

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 5419551	Management of Companies and Enterprises
56142	Telephone Call Centers
922140	Correctional Institutions
928110	National Security

2003

- Allowable 4A and 4B projects narrowed to exclude educational facilities, learning centers and municipal buildings.
- "Primary jobs" language inserted into DCA, limiting retail incentives to infrastructure, job training, and promotional expenditures.
- Performance contract requirement established.

2005

- Restrictions on retail incentives removed for certain Texas communities.
- Allowable 4A and 4B projects expanded to include certain sewer utilities and site improvements.
- Call centers added to definition of primary jobs.
- Cities authorized to determine the number and term of office (up to six years) of 4A corporation directors, and remove a 4A corporation director at any time without cause.
- Allowable use of 4A and 4B revenues expanded for military related projects.

2007

- Light rail, commuter rail, or motor buses added to list of eligible 4A and 4B projects.
- Hangars, airport maintenance and repair facilities, air cargo facilities, related infrastructure located on or adjacent to an airport facility added to list of eligible 4B projects.
- Airport facilities added as allowable projects for 4B corporations provided that the municipality enter into a development agreement.
- Public hearing requirement waived for 4B primary job projects in communities with under 20,000 population.

THE ECONOMIC DEVELOPMENT SALES TAX: WORKING FOR TEXAS

The economic development sales tax is the state's largest and most effective 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 (TEDC) will continue to advocate, educate, and inform economic development professionals, local officials, and lawmakers on developments related to the tax, including best practices and necessary statutory changes. TEDC members will also closely monitor special interests that have their eye on the tax as a funding source for local projects that fall outside the scope of economic development, such as hospitals and community colleges.

The Texas Economic Development Council is proud to be the most vocal and effective supporter of the economic development sales tax.

FOR MORE INFORMATION ABOUT THE ECONOMIC DEVELOPMENT SALES TAX

USEFUL RESOURCES:

“Economic Development Sales Tax, August 2007.”

This recently updated brochure 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.window.state.tx.us/taxinfo/taxpubs/tx96_302.pdf

“Economic Development Handbook for Texas Cities, 2006.”

This publication, which does not incorporate legislative changes from the 2007 session, is published 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 at the Attorney General's web site at:

www.oag.state.tx.us/AG_Publications/pdfs/2006econdevhb.pdf

KEY CONTACTS:

- **Carlton Schwab**, Texas Economic Development Council
Phone: (512) 480-8432. **Email:** carlton@texasedc.org
- **Bob Bearden**, Local Government Assistance Division, Comptroller of Public Accounts
Phone: (512) 936-1966. **Email:** bob.bearden@cpa.state.tx.us
- **Julian Grant**, Municipal Affairs Division, Office of the Attorney General
Phone: (512) 475-4683. **Email:** julian.grant@oag.state.tx.us