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Successes in Texas, Presented in California: Economic Development Options

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Texas is the home of many successful, innovative, yet controversial methods of financing economic development (ED) projects. This paper will introduce just some of the legal tools in place since the Texas Constitution was amended back in the 1980's to allow for the Legislature to create the ED statutes that have given local governments many more tools than existed before, when no clear vehicles existed.

Economic Development Sales Tax Corporations

(The general description in this section is based in part on information from Jeff Moore, formerly co-author of the Economic Development Handbook for Texas cities and now a partner at Brown and Hofmeister in Richardson, TX. The specific data on City of Corpus Christi projects in this and other topics comes in part from Mike Culbertson and Charlotte Yochem with the City.)

Formerly and still commonly known as section 4A and section 4B sales tax corporations, now Type A and Type B corporations due to the codification of their original statute into the Texas Local Government Code (TLGC), these corporations are funded by sales taxes which Texas cities may impose for economic development. These sales taxes are authorized pursuant to the Development Corporation Act of 1979, now found in sections 501-507 of the TLGC. Cities must hold a sales tax election to adopt either a Type A or Type B sales tax. If adopted, the city must not exceed the two percent (2%) local sales tax limit.

The sales tax for economic development is one of the most popular tools used by cities to promote economic development. Type A or B economic development sales taxes may be initiated by city council approving an ordinance calling an election on the imposition of the sales tax or by a petition signed by a number of qualified voters that equals at least twenty percent (20%) of the voters who voted in the most recent regular city election. The sales tax rate for either a Type A or B sales tax is 1/8th, 1/4th, 3/8ths or 1/2 of one percent. Any city can create a Type B corporation and, as they have more leeway on the types of projects they can fund, cities would now choose a Type B over a Type A, which are more suited to industrial-type projects. Type B corporations are often known more as community improvement vehicles, as they can spend money on quality of life projects involving parks, museums, sports complexes, and the like, as well as more types of businesses such as retail. Type B's can also do anything that a Type A can. Type A corporations, however, can also obtain community improvement-Type B powers through voter approval, as the City of Corpus Christi has to allow spending on affordable housing and sports facilities.

Both Type A and B corporations may spend no more than ten percent (10%) of the corporate revenues for promotional purposes. A Texas Attorney General opinion, GA-86 (2003) concluded a promotional purpose is a question of fact for the board of directors to resolve in the first instance, subject to judicial review and the supervisory authority of the city council.

Type A and B corporations may not provide a direct incentive or make expenditures on behalf of a business enterprise unless the corporation enters into a performance agreement with the business enterprise. The performance agreement at a minimum must provide for a schedule of additional payroll or jobs to be created or retained and the capital investment to be made as consideration for any incentives. Further, the agreement must specify the terms for any

repayment should the business fail to meet the performance requirements specified in the agreement.

An economic development corporation may undertake projects outside of the city limits with permission of the governing body that has jurisdiction over the property.

The corporations determine which projects to fund, with city council retaining approval authority over all expenditures of the corporation. The first step of corporation approval is required to start the process; without it, the contracts for the project will not be valid.

A Texas home rule city (with a voter-approved charter) is authorized to grant public money to a Type A or B corporation, which is required to use the grant of city money for the development and diversification of the economy of the state, elimination of unemployment or underemployment in the state, and development and expansion of commerce in the state.

In Corpus Christi, Texas, a 1/8th cent sales tax passed in November 2002 and is in effect from April 3, 2003 through April 3, 2018. The ED sales tax has incentivized new companies to locate there, incentivized existing companies to expand, helped train the residents for the jobs that are right here right now, and helped small businesses grow. These funds are the only dedicated economic development funds available in the community.

Economic Development:

These funds have created 1,242 new jobs and retained 637 existing jobs while increasing the investment in the city's tax base by $53,172,045. This represents an annual increase of $303,376.82 in property tax to the City. This number does not include those projects that have not reached completion yet. There is over $1 billion in investment and over 500 jobs in projects that have not been completed yet. The return on investment measured by the amount of increase in tax revenues divided by the amount of ED funding is 60.5% over a ten year period. In other words, every $100 in ED funds resulted in $60.50 in new tax revenue.

Type A funds have been used to provide an incentive for other businesses to either bring them to Corpus Christi or to incentivize them to expand their existing businesses:

AC Distribution: Invested $4,312,109 and created 27 jobs;

McTurbine: Invested $7,113,268 and created 70 jobs and retained 382 jobs;

Commercial Metals Company (CMC): Invested $25,000,000 and had 51 new and retained jobs for a new metal recycling plant;

Turner Industries Group: Invested $13 million and created 200 jobs;

Susser Holdings: Invested $5,060,629 and brought in 71 new jobs into their headquarters for a total of 287 employees;

Kanon Services: Oil Services company invested $3,700,000 and created 40 jobs;

Motorglobe: made Corpus its national headquarters, investing $400,000 and creating 50 high paying jobs;

Majek Boatworks: invested $1,050,000 and created and retained 51 jobs to expand their nationally known boat manufacturing plant;

Rugged Cycles: continued its national headquarters, may invest up to $1,000,000 and create and retain 27 jobs for this creative bicycle business for large companies such as refineries and colleges;

Oneta Company: the last independent Pepsi bottler south of Dallas, will invest $5,000,000 and create 31 jobs and retain 64 jobs;

HEB Bakery: A Texas icon, may invest up to $17,000,000 and retain 388 jobs and will use the grant to repair the city street in front of their manufacturing and distribution center.

Type A funds have been used as part of a larger incentive package:

Upper Padre Partners: Type A grant of $5,000,000 along with other incentives discussed below. The entire incentive package could total $117 million. They will invest up to $552,000,000 and create 300 jobs. This grant is to help with **Schlitterbahn,** the iconic Texas water park brand based in New Braunfels, to move forward with plans to build a water park on North Padre Island. The $41 million resort is tentatively set to open March 1, 2014, ahead of spring break. Early designs showed the park would include a 65-acre water park with lodging, golf and restaurants. It will be built on the existing golf course and tied into a master plan for the area that includes a marina in Lake Padre, an extension of the residential canal system, retail, hotels, condos and single-family homes on about 500 acres of mostly undeveloped land.

M&G Resins (Italian company): Type A grant of $3,000,000 as part of an incentive package that includes County and Del Mar College tax abatements, State training funds, and a possible incentive from the school district. The entire incentive package could total $174 million. They will invest $750,000,000 and create 220 jobs.

Affordable Housing:

The Type "A" Board is responsible for managing the use of the funds. Initially, the Board conducted several public meetings in order to receive public input from citizens as to the type of affordable housing that may be needed in the community. A decision was made and approved by the Board to use the funds for individually owned single-family affordable housing.

Since the inception of the "Affordable Housing Fund" several programs have been funded to ensure there is affordable housing throughout the City for income eligible households. Projects funded have included homebuyer assistance, new construction, land acquisition, and infrastructure.

Affordable housing helps in maintaining and expanding the property tax base. This is beneficial to many entities such as the City, County, School Districts, Colleges, and Hospitals. Funding of affordable housing is vitally important because it helps businesses and creates hundreds of local jobs. The ripple effect created by the construction of new housing is enormous for those that work in the housing industry such as builders, subcontractors, realtors, lenders, title companies and the various other supporting jobs created that are related to housing.

Whataburger Field:

Type A funds were used to construct Whataburger Field. It pays for the debt service on a bond issuance of $24,565,000 made in April 2004. It pays for the debt service, principal and interest on the loan, with the average annual debt payment being $2,286,679. The bonds will be paid in 2018. It should be noted that authorization for levying this sales tax is for a period of 15 years beginning on April 1, 2003 or until the bonds are paid off, whichever is sooner. The lease contract for Whataburger Field is between the Corpus Christi Hooks and the City. The Hooks are the double A minor league team for the Houston Astros.

Whataburger Field was tabbed by *Minor League News* as the best Minor League venue in North America in 2008 and in 2009. It features 5,050 fixed seats, 19 luxury suites and two outfield berm areas to accommodate nearly 2,000 fans. They have an average attendance of 5,752 for the 8 seasons that they have been in Corpus Christi. In that time period they rank 2nd in the Texas League (8 teams) and 4th in Double-A (30 teams) in attendance.

(The general descriptions in the remaining sections come in large part from the Economic Development Handbook for Texas cities promulgated on behalf of the Texas Attorney General and to which this author and many others have contributed in its many editions. Its 2013 edition may be found at https://www.oag.state.tx.us/AG_Publications/pdfs/econdevhb2013.pdf. Much more detailed legal procedures relating to all these ED tools may be found in that handbook.)

Chapter 380 Agreements

Chapter 380 of the Texas Local Government Code provides significant legislative authority for Texas municipalities in the area of economic development. When a city wants to provide a grant or a loan of city funds or services in order to promote economic development, it generally cites its powers under Chapter 380. Cities have utilized provisions under this law to provide a myriad of incentives that have drawn businesses and industries to locales throughout Texas. The text of Chapter 380 is very short but its importance to economic development cannot be overstated. Provided below is the text of its main provision, Section 380.001.

LOCAL GOVERNMENT CODE
TITLE 12. PLANNING AND DEVELOPMENT
SUBTITLE A. MUNICIPAL PLANNING AND DEVELOPMENT
CHAPTER 380. MISCELLANEOUS PROVISIONS RELATING TO MUNICIPAL PLANNING AND DEVELOPMENT
Sec. 380.001. ECONOMIC DEVELOPMENT PROGRAMS.

(a) The governing body of a municipality may establish and provide for the administration of one or more programs, including programs for making loans and grants of public money and providing personnel and services of the municipality, to promote state or local economic development and to stimulate business and commercial activity in the municipality. For purposes of this subsection, a municipality includes an area that:
(1) has been annexed by the municipality for limited purposes; or
(2) is in the extraterritorial jurisdiction of the municipality.

(b) The governing body may:
(1) administer a program by the use of municipal personnel;
(2) contract with the federal government, the state, a political subdivision of the state, a nonprofit organization, or any other entity for the administration of a program; and
(3) accept contributions, gifts, or other resources to develop and administer a program.

What this statute allows is the provision of loans and grants of city funds, as well as the use of city staff, city facilities or city services, at minimal or no charge. Whether a city provides any such incentive is completely discretionary. The provision of grants and loans should be used with caution and with attention to necessary safeguards.

A home rule city may grant public money from authorized sources to a Type A or Type B economic development corporation under a contract authorized by Section 380.002 of the Local Government Code. The Type A or Type B economic development corporation is required to use the money for "the development and diversification of the economy of the state, elimination of unemployment or underemployment in the state, and development and expansion of commerce in the state."

To establish a loan or grant, or to offer discounted or free city services, a city must meet the requirements contained in the Texas Constitution and in applicable Texas statutes. Additionally, a city must review its city charter and any other local provisions that may limit the city's ability to provide such a grant or loan. A discussion of these issues follows.

First, any expenditure in the form of a grant, loan or provision of city services at less than fair market value involves a donation of public property. Article III, Section 52-a of the Texas Constitution sets up the constitutional framework for public funding of economic development efforts. It provides that economic development is a public purpose. However, a city may not simply write out checks to interested businesses in order to promote economic development. The city must ensure that the public purpose of economic development will be pursued by the business. For example, if a city provides a grant or a loan to an industry, the city should enter into a binding contract with the funded industry that outlines what steps the business will take that justify the provision of public funding (creation of jobs, expansion of the tax base by construction or enhancement of the physical facilities, etc.). The city should include a recapture provision in the agreement so that if the business does not fulfill its promises, the city will have a right to seek reimbursement of the incentives that were provided. Any such agreement should also include tangible means for measuring whether the industry has met its obligations under the contract. Without these safeguards and a demonstrable benefit to the municipality, such incentives may not pass constitutional muster for serving a public purpose. *See* Op. Tex. Att'y Gen. No. GA-529 (2007) (City may fund housing project if it finds the project will promote economic development).

Projects involving 380 funds:

La Palmera Mall which invested over $65 million and created 300 new jobs and retained 750 jobs. The 380 funds include a sharing of the increase over a base amount of both property tax and sales tax revenues.

Topaz Power: Purchased two gas fired power plants that had shut down. They have invested over $1 billion in the two plants and are now in operation. They have created or retained 60 jobs.

The Upper Padre Partners resort project: Also contained 380 funds.

voestalpine Texas (lower case is correct!): Austria's largest steel maker has announced a $700 million processing plant that will initially bring 150 permanent jobs to the region. Their development will be located at the Port of Corpus Christi with plans to be operational in the first quarter of 2016. The voestalpine plan has Chapter 381 (of the Local Government Code) funds from San Patricio County. This is the statutory scheme allowing Texas counties to fund economic development grants. Their ability is less than cities but still allows their participation in such deals.

Property Tax Abatements

Local governments often use property tax abatements to attract new industry and commercial enterprises and to encourage the retention and development of existing businesses. More than 1,000 tax abatement agreements have been executed by Texas local governments since the early 1980s. These agreements are credited with producing many new or retained jobs. In 2009, the Texas Legislature re-authorized local governments to continue using property tax abatements until September 1, 2019. The statutes governing tax abatement are located in chapter 312 of the Texas Tax Code.

Incorporated cities, counties and special districts are allowed to enter into tax abatement agreements. However, school districts may not enter into tax abatement agreements under Chapter 312 of the Tax Code. Instead, a school district's ability to limit appraised values on certain property is found in the Texas Economic Development Act, chapter 313 of the Tax Code .

To enter into a tax abatement agreement the area around the project must be designated a reinvestment zone. A reinvestment zone must have certain characteristics such as blight, inadequate infrastructure a history of no growth, etc. Whether a city or a county may initiate a tax abatement agreement depends upon the location of the property that would be subject to the tax abatement. If the property subject to abatement is located within the city limits, the city would be the lead party in the tax abatement. If the property to be abated is located within the extraterritorial jurisdiction (ETJ) of the city, either the city or the county may serve as the lead party. If the property is located outside the city's boundaries and outside the city's ETJ, the county must serve as the lead party for tax abatement.

Cities are eligible to enter into a tax abatement agreement with the owner of taxable real property that is located in a reinvestment zone, but that is not in an improvement project that is financed by tax increment bonds. The tax exemption can include a portion of:
- the real property's value,
- the tangible personal property's value that is located on the real property, or
- both.

The tax abatement agreement cannot exceed 10 years and the owner of the property must make specific improvements or repairs to the property.

Also, cities are eligible to enter into a tax abatement agreement with the owner of a leasehold interest in tax-exempt real property that is located in a reinvestment zone, but that is not in an improvement project financed by tax increment bonds. The tax exemption includes a portion of the value of property subject to property taxes, including leasehold interest, improvements, or tangible personal property located on the real property. As above, the tax abatement cannot exceed 10 years and the owner of the leasehold interest must make specific improvements or repairs to the real property.

Cities can enter a tax abatement concerning tangible personal property located on taxable or tax-exempt real property.

Specific Projects utilizing County/County Drainage District/College tax abatements: voestalpine, M&G, Topaz.

Tax Increment Financing/Tax Increment Reinvestment Zones (TIFs/TIRZs)

Tax increment financing is a tool that local governments can use to publicly finance needed structural improvements and enhanced infrastructure within a defined area. These improvements usually are undertaken to promote the viability of existing businesses and to attract new commercial enterprises to the area. The statutes governing tax increment financing are located in Chapter 311 of the Texas Tax Code.

The cost of improvements to the area is repaid by the contribution of future tax revenues by each taxing unit that levies taxes against the property. Specifically, each taxing unit can choose to dedicate all, a portion, or none of the tax revenue that is attributable to the **increase** in property values due to the improvements within the reinvestment zone. The additional incremental tax revenue that is received from the affected properties is referred to as the tax increment. Each taxing unit determines what percentage of its tax increment, if any, it will commit to repayment of the cost of financing the public improvements. In addition, the governing body of a city may determine, in an ordinance designating an area as a reinvestment zone or in an ordinance adopted subsequent to the designation of a zone, the portion or amount of tax increment generated from municipal sales and use taxes attributable to the zone, above the sales tax base, to be deposited into the tax increment fund.

Tax increment financing may be initiated only by a city or county. Once a city or county has begun the process of establishing a tax increment financing reinvestment zone, other taxing units are allowed to consider participating in the tax increment financing agreement.

Cities and counties may exercise any power that is necessary to carry out tax increment financing. They may acquire real property through purchase or condemnation, or other means, enter into necessary agreements, and construct or enhance public works facilities and other public improvements. In addition, cities and counties may sell real property on the terms and conditions and in the manner they consider advisable to implement the project plan. The power for cities and counties to acquire and sell real property prevails over any law or municipal charter to the contrary.

School District Participation

The Texas Economic Development Act (“the Act"”) is another economic development tool used to attract new industries and commercial enterprises. Chapter 313 of the Texas Tax Code authorizes certain property tax incentives for economic development provided by school districts. School districts have the ability to provide tax credits and an eight-year limitation on appraised value of a property for the maintenance and operations portion of

the school district property tax to eligible corporations and limited liability companies. The property remains fully taxable or the purpose of any school district debt service tax. The expiration of the Chapter 313 incentive was extended from December 31, 2014 to December 31, 2022 under HB 3390 in the last legislative regular session.

Conclusion

The author was for nine years the sole municipal lawyer for the Texas Attorney General's office. During that time the largest number of phone calls for advice from city officials had to do with Economic Development, due in large part to the publication of the ED Handbook mentioned in this paper and the participation of prior lawyers in that position, continued until the present day, as trainers in a day-long, legally mandated annual series of seminars that many ED and city officials had to take every two years on ED sales tax law. Like everywhere else, Texas local officials are obsessed with attracting new businesses and retaining them, but perhaps they are even more obsessed than most, and although the idea of using tax money for subsidies or other arrangements for the benefit of corporations is and will continue to be controversial, there is no question that Texas has led the charge and can serve as an example for other states that wish to follow its lead.