

City Economic Development



Texas cities are the first—and often only—engine of economic development in the state. Until the controversial Texas Enterprise Fund was created, only cities routinely granted incentives necessary to attract new business to the state. With the Enterprise Fund up and running, larger cities have partnered with the state to attract such major developments as a Texas Instruments facility and a Toyota plant. Smaller cities are usually on their own to attract business.

Until the late 1980s, using city resources to attract business was arguably unconstitutional. In 1987, Article 3, Section 52 of the Texas Constitution was amended to make it clear that economic development serves a public purpose. From that point on, three major channels of city economic development began to open for cities: Chapter 380 agreements; the Type A/Type B economic development sales tax; and property tax incentives.

Chapter 380 Agreements

Chapter 380 of the Local Government Code authorizes cities to establish programs for grants and loans of city resources for economic development purposes. Though it is the most powerful economic development tool for cities, Chapter 380 is often overlooked in favor of other incentives. Cities using 380 agreements must be careful not to simply present a blank check to business and industry prospects: A program providing for checks and balances on a business's use of Chapter 380 money is required

by law. Examples of these checks and balances might be performance agreements tying grant money to the creation of a certain number of jobs, or requiring the business to stay in the city for a certain length of time.

Economic Development Sales Taxes

More than 500 Texas cities have adopted a Type A or Type B economic development sales tax. Some cities have both taxes. The tax was created in 1989, but authority to spend Type A/Type B tax money gradually expanded over the next decade to cover all forms of commercial, retail, and traditional industrial economic development. An important bill, H.B. 2912, passed in 2003. H.B. 2912 scales back the authority of some Type A and Type B economic development corporations. No longer can the sales tax be spent on retail, commercial, or service industries. Instead, the tax must be spent on basic industrial and manufacturing businesses. The authority for some, but not all, Type B corporations to engage in retail, commercial, and service economic development was restored in 2005. The Type A/Type B sales tax remains an important economic development tool for many cities that have the available land and workforce to attract industry. Additionally, instead of a Type A or Type B economic development sales tax, some cities have adopted a municipal development district (MDD) sales tax that may be levied in a specified area in the city or in the city's extraterritorial jurisdiction. The MDD sales tax closely resembles the traditional economic development sales tax, but

the scope of projects that may be funded with an MDD tax is slightly broader.

Property Tax Incentives

Property taxes may be directly tapped to promote economic development in two ways: tax abatement and tax increment financing. Both function by either forgiving (abatement) or dedicating to improvements (increment financing) any **net increase** in property tax revenue as a result of a business moving to town or upgrading existing facilities. Property tax incentives can never forgive or decrease the present taxable value of the land and facilities upon which they are granted. This key feature of the incentives—that all current taxes must continue to be paid—belies the common stereotype that tax incentives are “giveaways.” On the contrary, when done properly, tax incentives create new taxable value that never would have come to town absent the incentive, thus lowering the overall tax burden on other properties.

Tax and Appraisal Caps Threaten Economic Development Proposals to cap, limit, or freeze municipal property tax revenue or property appraisals will have the unfortunate side effect of undermining the very rationale behind many economic development tools. While the purpose of economic development is often to put new taxable value on the rolls, tax caps will ensure that this cannot happen. Tax and appraisal caps, after all, restrict the very growth in appraised value that tax incentives are designed to generate. ★