

**BASICS REGARDING STATUTORY  
ECONOMIC DEVELOPMENT TOOLS  
FOR MUNICIPAL ATTORNEYS**

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BASICS REGARDING STATUTORY ECONOMIC DEVELOPMENT  
TOOLS  
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**I.**  
**GENERAL BACKGROUND FOR CONSIDERING**  
**ECONOMIC DEVELOPMENT INCENTIVES**

**A. Economic Development Goals**

Article III Section 52-a of the Texas Constitution, adopted November 3, 1987, is titled, "Assistance to encourage state economic development," and declares that the following typical economic development goals are public purposes: development and diversification of the economy, the elimination of unemployment or underemployment, the stimulation of agricultural innovation, the fostering of the growth of enterprises based on agriculture, or the development or expansion of transportation or commerce. Various economic development statutes state additional objectives such as retention or expansion of primary employment and attracting major investment to a particular area. Economic development incentives should be structured in a way to successfully achieve one or more of the goals stated in the authorizing statutes. For practice pointers and public purpose considerations relating to economic development incentives, *see* Attachment 1 to this paper.

**B. What is a city's role in economic development?**

In working to successfully promote economic development, a city's role is much larger than offering incentives. For instance, consider the role favorable "soft infrastructure" might play in your city's economic development efforts. The term "soft infrastructure" includes such things as the regulatory structure, availability of adequate workers, quality of life in the community, educational opportunities, and friendliness toward business. The term "friendliness toward business" may include such things as availability of financing, availability of non-profit agencies to assist with business support and training, and availability of transportation for employees. Favorable soft infrastructure is likely to involve collaboration of businesses, government, and educational institutions to create an effective business environment based on the needs and demands of the particular industries and entities involved and those they serve. Each community is likely to have different needs and assets to consider when building the city's soft infrastructure.

In summary, well-managed city services, carefully planned and maintained infrastructure, fair and efficient regulatory policies, and well-planned, effective land use policies are all examples of a municipality's role in promoting the greatest gains for citizens as a whole through its efforts to promote economic development.<sup>1</sup>

**II.**  
**STATUTORY TOOLS TO PROMOTE ECONOMIC DEVELOPMENT**

**A. Economic Development Sales and Use Taxes**

1. 4A and 4B Sales Tax  
Tex. Rev. Civ. Stat. Ann., art. 5190.6 § 4A and § 4B (Vernon Supp. 2004) [Hereafter referred to simply as *4A and 4B*]

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<sup>1</sup> NORTH, DOUGLAS C., STRUCTURE AND CHANGE IN ECONOMIC HISTORY 24 (W.W.Norton & Co. 1981).

- a. What is it? Sections 4A and 4B of the Industrial Development Corporation Act allow voters in eligible cities to approve a local sales and use tax dedicated to promoting economic development projects as delineated in the statute. House Bill 2912, passed during the 2003 regular session, amends the Industrial Development Corporation Act to place additional restrictions on the way the 4A and 4B sales taxes can be used. The Senate Committee Report regarding House Bill 2912 states the purpose of the amendment is to refocus the use of the economic development sales tax on the creation or retention of primary jobs. Among other restrictions, the 2003 revision prohibits a 4A or 4B corporation from providing a direct incentive or making an expenditure on behalf of a business unless the economic development corporation and the business enterprise enter into a performance agreement which at a minimum must provide a schedule of additional payroll or jobs to be created or retained and capital investment to be made as consideration for any direct incentives provided. The performance agreement must also specify the terms under which repayment must be made if the business enterprise fails to meet the performance requirements specified in the agreement. Tex. Rev. Civ. Stat. Ann. art. 5190.6 § 40 (Vernon Supp. 2004).
- b. What is the benefit to the City? Provides a funding source for projects. Authorizes the issuance of bonds and other obligations funded by sales tax. 4A and 4B corporations are not political subdivisions subject to notice and bid requirements applicable to the sale or exchange of land. Op. Tex. Att'y Gen. No. JC-109 (1999).

- (1) How do you know whether you should establish a 4A or 4B corporation?

Size of County

The rule of thumb has historically been that smaller cities have 4A corporations and larger cities have 4B corporations. The line is not as clear now.

In 1993, the legislature made 4B available to any city eligible to adopt a 4A sales tax. Therefore, most cities in a county of less than 500,000 can adopt either the 4A or the 4B sales tax, or both, if they have not reached their local sales tax limit.

To be eligible to create a 4B corporation, a city must be located in a county with a population of 500,000 or more in which the combined rate of all sales and use taxes does not exceed 8.25 percent; or the city must have a population of 400,000 or more and be located in more than one county in which the combined rate of all sales and use taxes imposed does not exceed 8.25 percent; or the city must meet the requirements of Section 4A.

Type of Project

Projects listed in Tex. Rev. Civ. Stat. Ann. art. 5190.6, § 2(11)(A) (Vernon Supp. 2004) are authorized for both 4A and 4B corporations, although certain additional restrictions may apply under either 4A or 4B. In the following definition of “project” the words added by the 78th legislature and effective June 2003 are underlined. According to

§ 2(11)(A), the term “project” means “the land, buildings, equipment, facilities, expenditures, targeted infrastructure, and improvements (one or more) that are for the creation or retention of primary jobs and that are<sup>2</sup> found by the board of directors to be required or suitable for the development, retention, or expansion of manufacturing and industrial facilities, research and development facilities, transportation facilities (including but not limited to airports, ports, mass commuting facilities, and parking facilities, sewage or solid waste disposal facilities, recycling facilities, air or water pollution control facilities, facilities for the furnishing of water to the general public, distribution centers, small warehouse facilities capable of serving as decentralized storage and distribution centers, primary job training facilities for use by institutions of higher education, and regional or national corporate headquarters facilities.”

The types of projects a 4A corporation may undertake are restricted by Art. 5190.6, § 4A(i), which clarifies the primary purpose of a project may not be to provide transportation facilities, solid waste disposal facilities, sewage facilities, facilities for furnishing water to the general public, or air or water pollution control facilities. A 4A corporation may provide these types of facilities to benefit a project having another primary purpose permitted by the statute.

A permissible 4A and 4B “project” also includes job training required or suitable for the promotion of development and expansion of business enterprises and other enterprises described by the Development Corporation Act, but only if the business enterprise seeking 4A or 4B job training funds makes certain commitments in writing regarding the wages of the jobs created. Tex. Rev. Civ. Stat. Ann. Art. 5190.6, § 38(b) (Vernon Supp. 2004).

Effective 2003, a 4A or 4B corporation may not provide a direct incentive to or make an expenditure on behalf of a business enterprise under a project unless the corporation enters into a performance agreement with the business enterprise containing the provisions delineated in the statute. Tex. Rev. Civ. Stat. Ann. Art. 5190.6, § 40 (Vernon Supp. 2004).

4B authorizes the same type projects authorized by 4A, but additionally authorizes projects such as land, buildings or equipment for professional and amateur sports facilities, park facilities and events, entertainment and tourist facilities, and affordable housing. As of September 1, 2001, a 4B project may also include research and development facilities, and a water supply or water conservation program. As of 2003, a water supply or water conservation program must be specifically approved at an election utilizing the ballot language added by § 4B(a-5)(1).

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<sup>2</sup>The words “to promote new and expanded business development” were deleted from the definition of “project.”

### Other differences

A 4A sales tax may be adopted in conjunction with a sales tax for property tax relief under one proposition. There is no authorization for a proposition combining a 4B sales tax with a sales tax for property tax relief.

Once adopted, the 4A tax continues until repealed at an election. The 4B tax continues until the bonds and any other debt obligations have been paid in full for all of the projects undertaken by the 4B corporation.

A 4A sales tax is authorized through use of mandatory wording for the ballot proposition. There is no required statutory language for the 4B ballot proposition. It can be authorized by a general ballot proposition for the adoption of a 4B sales tax for economic development. A Chapter 334 venue sales tax (or other funding options) is authorized through use of mandatory wording for the ballot proposition.

There is no statutory authority for a 4B tax rate to be increased or reduced at subsequent elections. A 4A tax may be reduced, increased or repealed at an election held on the issue. The election to increase or decrease a 4A tax may be called on a city's own motion or on petition of at least 10 percent of the registered voters of the city. A Chapter 334 venue sales tax may be decreased by ordinance of the city. To increase the Chapter 334 venue sales tax would require an election.

Prior to proceeding with a project, both 4A and 4B corporation boards are required to obtain approval of the municipality's governing body. A 4A corporation is not required to conduct additional public notice or public hearings on 4A projects. However, 4B corporations must provide public notice and hold a public hearing prior to undertaking a project. The public has sixty days to petition for an election on whether to pursue the project if it is not a project already approved by the voters.

## 2. Sports and Community Venue Sales Tax and Other Revenue Sources Tex. Loc. Gov't Code Ann. Ch. 334 (Vernon 1999 & Supp. 2004)

### a. What is a venue under Chapter 334?

- (1) An arena, coliseum, stadium, or other type of area or facility for which a fee for admission is charged.
- (2) A convention center, facility or related improvement such as a civic center, civic center hotel, auditorium, theater, opera house, music hall, exhibition hall, rehearsal hall, park, zoological park, museum, aquarium, or plaza located in the vicinity of a convention center or facility owned by a city.
- (3) A tourist development area along an inland waterway.

- (4) A municipal parks and recreation system, or improvements or additions to a park or recreation system, or an area or facility that is part of a municipal parks and recreation system. (The provision regarding municipal parks was added in 1999.)
- (5) A project authorized by art. 5190.6, § 4A or § 4B, as that Act existed on September 1, 1997.
- (6) A watershed protection and preservation project; a recharge, recharge area, or recharge feature protection project; a conservation easement; or an open-space preservation program intended to protect water.

A "venue project" means a "venue" and related infrastructure, planned, acquired, established, developed, constructed, or renovated under Chapter 334.

b. What is the funding source?

- (1) Sales and Use Tax Increase up to 1/2 of 1% (§ 334.081)

Must be in increments of either 1/8, 1/4, 3/8, or 1/2 of 1%.

Provides for reduction of tax rates if adoption of this sales tax would result in a combined sales and use tax rate in excess of 2% in any location in the county or municipality.

- (2) Short-Term Motor Vehicle Rental Tax (§ 334.102)

Rental of 30 days or less.

Increments of 1/8 of 1%, and may not exceed 5%.

May not be used to fund a municipal park and recreation system venue.

Cannot be imposed after bonds or other obligations for the project are paid in full.

- (3) Admissions Tax (§ 334.151)

Imposed on each ticket sold as admission to an event held at an approved venue project if bonds have been issued for the project, but only during the time the bonds remain unpaid.

City may decrease or repeal amount by ordinance.

City may increase amount by ordinance if approved at an election.

Must not exceed 10% of the price of the ticket under any circumstances.

(4) Parking Tax (§ 334.201)

Imposed on each motor vehicle parking in a parking facility of an approved venue project within a period 3 hours before and 3 hours after an event.

Imposed as a flat amount on each vehicle or as a % of the amount charged for event parking, not to exceed \$3 per vehicle.

May be used only if bonds have been issued and are outstanding.

(5) Hotel Occupancy Tax (§ 334.252)

May not exceed 2% of the price paid for the room.

Is in addition to the 6% tax already in effect.

May impose this tax only if bonds are issued and only while the bonds are unpaid.

May not use for venue project that is part of municipal park system.

(6) Facility Use Tax (§ 334.302)

A uniform amount not to exceed \$5,000 imposed on each member of a professional sports team for each professional game the member plays at the approved venue project.

May impose this tax only if bonds are issued and only while the bonds are unpaid.

(7) Bonds and Other Obligations

A city may issue bonds to pay the costs of the project.

The bonds must be payable from and secured by the revenues in the venue project fund.

The bonds may mature serially or otherwise not more than 30 years from their date of issuance.

The bonds are not a debt of and do not create a claim against the revenue or property of the city other than the revenue sources pledged and an approved venue project for which the bonds are issued.

c. For what purposes can the funds collected pursuant to Chapter 334 be used?

The revenues are placed into a venue project fund. The fund can be spent to:

- (1) Reimburse or pay the costs of planning, acquiring, establishing, developing, constructing, or renovating one or more approved venue projects.

- (2) Pay the principal of, interest on, and other costs relating to bonds or other obligations issued by the city to refund bonds, notes, or other obligations.
- (3) Pay the costs of operating or maintaining one or more approved venue projects.

d. What is the benefit to the city of using Chapter 334?

The law creates new funding sources for projects with the potential to create additional revenue for the sponsoring cities. The law is especially beneficial to cities that have reached their local sales tax cap and need additional revenue sources. The types of projects permitted under Chapter 334 are projects that attract visitors to the venue itself as well as to surrounding hotels, restaurants and shops. It is also likely that a venue project will bring new sources of ad valorem tax revenues to the city through new businesses attracted to the vicinity of the venue. Ideally, additional visitors and new businesses will lead to an increase in sales tax revenue to the city's general fund to pay the costs of running the city (i.e. streets, police, fire, code enforcement). The venue project funding options authorized by the statute are the type that will be at least partially funded by the persons visiting the venues.<sup>3</sup>

**B. "Quality of Life" Taxes**

1. Local Hotel Occupancy Tax

Tex. Tax Code Ann. Ch. 351 (Vernon 2002 & Supp. 2004).

a. What is the local hotel occupancy tax?

A hotel occupancy tax may be imposed against any person who pays for the use of a room in a hotel. Most cities are eligible to adopt a hotel occupancy tax rate of up to seven percent of the consideration paid for the use of a hotel room. Certain cities, by statute, may impose a hotel occupancy tax at a higher rate (§ 351.003). The state of Texas imposes a six percent hotel occupancy tax rate. Additionally, a number of counties have received legislative approval to adopt a county hotel occupancy tax not to exceed seven percent of the consideration paid for a hotel room. In certain areas of Texas, the combined hotel occupancy tax rate of up to 20 percent of the cost of the hotel room may be charged. Hotels are required to charge and collect the tax, and the hotel remits the tax to the city on a regular basis established by the city.

b. How is the local hotel occupancy tax imposed?

Cities may adopt an ordinance calling for the levy of the tax. Voter approval is not required, except for a general-law municipality that borders on the Gulf of Mexico and has a boundary that is within 30 miles of Mexico. In that instance, the city may increase the rate to a maximum of 7.5 percent if the increase is approved by a majority of the registered voters voting at the election held for that purpose. *See* Tex. Tax Code Ann. § 351.003(d) (Vernon 2004 Supp.) effective June 18, 2003 until January 1, 2006.

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<sup>3</sup> For a comparison of Tex. Civ. Statutes art. 5190.6 § 4B vs. Loc. Gov't Code Chapter 334, *see* Attachment 2.

c. How can the hotel occupancy tax be used?

- (1) In order to be valid, the hotel occupancy tax expenditure must directly enhance and promote tourism and the convention and hotel industry. The hotel occupancy tax may not be used for general revenue purposes unless directly related to increasing tourism.
- (2) Additionally, local hotel occupancy tax revenues may be used only for expenditures that fit into one of six categories. Briefly stated, these categories are: convention centers, registration of convention delegates, advertising and promotion of the city, promotion of the arts, historical preservation, or certain sporting events in eligible cities.
- (3) Texas law also imposes restrictions on the percentage of hotel occupancy tax revenues that may be spent on each of the six categories listed above. The restrictions differ based on population of the city. Additionally, special legislative provisions apply to certain cities. The Attorney General Handbook on Economic Development Laws for Texas Cities contains a concise statement of the percentage limitations.
- (4) Effective September 1, 2001, before expending hotel occupancy tax revenues, a city must list each scheduled activity, program, or event that is directly funded by hotel occupancy tax proceeds or has its administrative costs funded in whole or in part by the tax. Each activity, program or event must directly relate to enhancing and promoting tourism and the convention and hotel industry.
- (5) Since 1999, cities have been required to keep track of hotel occupancy tax revenues collected and expended, which includes interest earned on the hotel occupancy tax revenues.

2. Street Maintenance Sales Tax

Tex. Tax Code Ann. Ch. 327 (Vernon 2002 & Supp. 2004)

a. What the street maintenance sales tax?

A street maintenance sales and use tax at a rate of 1/8 or 1/4 of one percent may be used only for the maintenance and repair of municipal streets existing at the time the sales tax is approved.

b. Is an election required?

Yes. The sales tax must be approved at an election.

c. How can the street maintenance sales tax be used?

The tax may be used only for maintenance and repair of municipal streets existing at the time of the sales tax election. The statute does not define "maintenance and repair." The statute defines "municipal street" as, "the entire width of a way held by a municipality in fee or easement or dedication that has a part open for public use for vehicular travel." It sounds simple enough, but expect many questions about what can be paid from the sales tax.

Capital expenditures may be justified if they are essential to carrying out the purpose of the statute.

d. What is the duration of the tax?

The sales tax expires four years from the date it takes effect unless reauthorized by voters prior to its expiration. If the tax is not reauthorized prior to its expiration, the tax expires and the city may not call an election on the question of authorizing a new tax before the first anniversary of the expiration date.

3. Crime Control and Prevention Sales and Use Tax

Tex. Loc. Gov't Code Ann. Ch. 363 (Vernon 1999 & Supp. 2004).

a. What is the Crime Control and Prevention Sales and Use Tax?

At an election for the purpose of creating and funding a Crime Control and Prevention District, a sales and use tax may be authorized in increments of 1/8 cent up to a maximum of 1/2 cent.

b. Is an election required?

Yes. The election must be held on a uniform election date. However, the election is held under Chapter 323 of the Tax Code; therefore, as of the date of this paper, the one-year limitation on the frequency of sales tax elections found in Tax Code Chapter 321 is not applicable.

c. How can the crime control and prevention sales and use tax be used?

A temporary Board must be appointed by the city council. The board must formulate and approve a two year budget plan and a two year crime control plan to be approved by the voters in summary form. The sales and use tax may be used to pay for all costs of the approved crime control and prevention program, including the costs of personnel, administration, expansion, enhancement, and capital expenditures. The board must reimburse the city for expenses incurred in creation of the district. The board may not issue or sell general obligation bonds, revenue bonds, or refunding bonds. Additional limitations on expenditures and investments are found in Tex. Loc. Gov't Code § 363.206 (Vernon Supp. 2004).

d. What is the duration of the district?

The district dissolves after five years unless voters approve its continuation. The city or the board may specify continuation of 5, 10, 15, or 20 years, and the district is dissolved at the end of the period for which it is continued under § 363.2515. See Tex. Loc. Gov't Code Ann. (Vernon Supp. 2004) § 363.301.

**C. Ad Valorem Tax Tools**

1. Tax Abatement

Tex. Tax Code Ann. Ch. 312 (Vernon 2002 & Supp. 2004).

- a. What is tax abatement? An exemption of all or a portion of the value of added taxable real property improvements or personal property improvements.
- b. What is the funding source? An ad valorem tax exemption for all or a portion of taxable value added by a project for a period not to exceed ten years.
- c. What is the benefit to the municipality? Ideally, the abatement induces development, adds value to the tax roll, and creates employment opportunities that would otherwise not occur. Even though a portion of the taxes on the added value will not come into the municipal coffers during the life of the tax abatement agreement, jobs will be created and local businesses are likely to benefit from construction of the project. In most instances, the public will benefit from additional employment opportunities. The city will benefit from the additional taxes received on a portion of the added value (unless a 100% abatement is granted) during the life of the agreement. After the agreement expires, the project's added value and employment opportunities should continue to benefit the city.
  - (1) Actions of the governing body required prior to granting tax abatement:
    - (a) Must adopt a resolution indicating intent to participate in tax abatement (312.002).
    - (b) Must adopt tax abatement guidelines and criteria (312.002).
    - (c) Must designate an area as a reinvestment zone (312.201).
    - (d) A tax abatement agreement must be approved by a majority of the members of the governing body at a regularly scheduled meeting (312.207) and the agreement must contain the following [312.205 (a) (1) – (7)]:
      - (i) Description of proposed improvements.
      - (ii) Authority to inspect to determine compliance.
      - (iii) Limit the uses of the property.
      - (iv) Provide for recapturing property tax revenue lost.
      - (v) Contain each term agreed to by the owner of the property.
      - (vi) Require annual certification of compliance by owner.
      - (vii) Provide for cancellation or modification for failure to comply with the agreement.
- d. Findings of the governing body required prior to granting tax abatement:
  - (1) Prior to adopting an ordinance designating an area as a reinvestment zone, the governing body must hold a public hearing and find that the improvements sought are feasible and practical and would be a

benefit to the land to be included in the zone and to the municipality after the expiration of a tax abatement agreement. [§ 312.201(d)]

- (2) To be designated as a reinvestment zone, an area should be determined by the governing body to meet one of the six criteria listed in § 312.202.
- (3) Prior to authorizing a tax abatement agreement, the governing body must find that the terms of the agreement and the property subject to the agreement meet the applicable guidelines and criteria adopted by the governing body. [§ 312.002(b)]

## 2. Tax Increment Financing

Tex. Tax Code Ann. Ch. 311 (Vernon 2002 & Supp. 2004).

- a. What is tax increment financing? Tax increment financing is a tool to finance public improvements within a defined area. The improvements should enhance the area and attract new investment. A municipality makes an area eligible for tax increment financing by designating a "reinvestment zone," also called a "tax increment reinvestment zone," "TIRZ" or a "TIF zone." Costs of selected public improvements within the reinvestment zone ("Zone") may be paid by current or future tax revenues flowing from redeveloped or appreciated real properties in the zone. The additional tax dollars generated by growth of real property value in the Zone are called the tax increment. These dollars flow to a tax increment fund ("Fund") for a specified term of years. Money flowing to the Fund each year is disbursed according to a plan and agreements approved by a Board appointed by participating local governmental units, as set by the ordinance designating the Zone.
- b. What is the funding source? Additional tax dollars generated by growth of real property value in the zone.
- c. What is the benefit to the municipality? Tax increment financing comes with a built-in funding source in areas where taxable values are increasing. The money can only be used for public improvements described in the municipality's project plan.
- d. Initial requirements:
  - (1) Must be initiated by petition of affected property owners or by the governing body of the municipality.
  - (2) If initiated by the governing body, a finding should be made that the area considered for tax increment financing meets at least one of the three criteria listed in § 311.005(a)(1)-(3):
    - (a) The area's present condition must substantially impair the city's growth, retard the provision of housing, or constitute an economic or social liability to the public health, safety, morals, or welfare. Further, this condition must exist because of the presence of one or more of the following conditions: a substantial number of substandard or deteriorating structures, inadequate sidewalks or street layout, faulty lot layouts, unsanitary or unsafe conditions, a tax or special assessment

delinquency that exceeds the fair market value of the land; defective or unusual conditions of title, or conditions that endanger life or property by fire or other cause; or

- (b) The area is predominately open, and because of obsolete platting, deteriorating structures, or other factors, it substantially impairs the growth of the city; or
  - (c) The area is in or adjacent to a "Federally assisted new community" as defined under Tax Code § 311.005(b).
- (3) The Tax Code imposes several additional requirements on a reinvestment zone for tax increment financing.
- (a) No more than 10 percent of the property within the reinvestment zone (excluding publicly-owned property) may be used for residential purposes. This requirement, however, does not apply if the district is created pursuant to a petition of the landowners.
  - (b) A reinvestment zone may not contain property that cumulatively would exceed 15 percent of the total appraised property value within the city and its industrial districts.
  - (c) A city also may not create a reinvestment zone or change the boundaries of an existing zone if the zone would contain more than 15 percent of the total appraised value of real property taxable by a county or school district.
- (4) The governing body must prepare a preliminary reinvestment zone financing plan. The Tax Code does not specify the contents of the preliminary financing plan but a city may find it beneficial to include each item required for the final financing plan described in Tax Code § 311.011.

#### **D. Miscellaneous Statutory Tools**

##### **1. Chapter 380 Economic Development Programs**

Tex. Loc. Gov't Code Ann. Ch. 380 (Vernon 1999 & Supp. 2004).

- a. What is Local Government Code Chapter 380? Chapter 380 of the Local Government Code was enacted pursuant to art. III, § 52-a of the Texas Constitution, which provides that economic development is a public purpose. According to a 1992 attorney general's opinion, "The legislature intended § 380.01 to authorize municipalities to offer a range of incentives designed to promote state or local economic development." Op. Tex. Att'y Gen. No. DM-185 (1992).
- b. What is the funding source? The statute authorizes grants and loans from city funds for economic development purposes, but does not specifically provide for a specific tax or fee to fund the grants and loans.

A home-rule municipality may issue bonds to fund an economic development program that the municipality has established in accordance with § 380.001, but only if two conditions are met. (1) The bonds must be in an amount and

to the extent provided by the municipality's charter. (2) A majority of the qualified property tax-paying voters voting at an election held to consider the bond issue must have approved the issuance. Op. Tex. Att'y Gen. No. DM-185 (1992). Funds granted under § 380.002 to a § 501(2)(3) corporation or a development corporation under art. 5190.6 cannot be from the proceeds of bonds or other obligations of the municipality payable from ad valorem taxes.

Make sure the intended use of funds is consistent with the authorized purposes of the funds. For instance, hotel occupancy tax can be used only for certain purposes. Funds from a 4A or 4B sales tax can be used only for certain purposes. All statutes and "contracts with the voters" applicable to a particular funding source should be evaluated prior to obligating the funds.

The statute also authorizes the use of city staff, city facilities, or city services at minimal or no charge, but the safeguards discussed below should be utilized to avoid an allegation of a donation of public property. See Op. Tex. Att'y Gen. No. JC-0109 (1999).

c. What is the benefit to the City from utilizing Chapter 380? Flexibility to structure a program to meet the needs of the city for a particular project.

d. Initial Requirements:

(1) Establish a program. The statute does not define the term "program." In order to meet the constitutional requirement that a public purpose is served by the expenditure of public funds or the provision of public services, the program should be planned and described in a written document that includes at least the minimal safeguards to achieve the public purpose of economic development. The minimum safeguards are:

(a) Written agreement.

(b) Outline the steps the business must take to justify public funding; for instance, creation of jobs or the expansion of the tax base by construction or enhancement of real property improvements.

(c) Provide for the recapture of incentives provided if the business does not meet its obligations.

(d) Provide an effective method for measuring whether the industry has met its obligations.

(2) Comply with Budget law contained in Chapter 102 of the Local Government Code.

(3) Comply with Municipal Charter for limitations on expenditures.

e. Required Findings:

That the public purpose of economic development will be accomplished through the program.

That there will be a demonstrable benefit to the municipality from use of the incentives.

That sufficient safeguards are in place to determine whether a business has met its obligations, and if the obligations have not been met, that the incentives granted can be recaptured.

*See* Op. Tex. Att'y Gen. No. DM-185 (1992) regarding the constitutionality of Chapter 380.

2. Local Government Corporations

Tex. Transp. Code Ann. § 431.101 (Vernon Supp. 2004); *also applicable*, Tex. Loc. Gov't Code Ann. Ch. 394 (Vernon 1999).

a. What is a Local Government Corporation?

A local government corporation is a non-profit corporation created to aid and act on behalf of one or more local governments to accomplish any governmental purpose of those local governments. Tex. Transp. Code Ann. § 431.101(a) (Vernon Supp. 2004). If the city chooses to create a local government corporation, the city must approve by ordinance or resolution the articles of incorporation and the bylaws of the corporation. The city is entitled to any income earned by the local government corporation that is not needed to pay the corporation's expenses or obligations. The local government corporation is subject to the Public Information Act and the Open Meetings Act (Transp. Code §§ 431.003, 431.004, 431.005) and may issue bonds and notes, but does not have taxing authority. The corporation is dissolved when the purposes of the corporation are fulfilled and all obligations of the corporation have been fully paid. On dissolution or liquidation of a corporation created by a city, the title to all assets shall be transferred to the city. Tex. Trans. Code Ann. § 431.186 (Vernon 1999).

b. What is the funding source?

The corporation may issue bonds and notes. [Transp. Code §§ 431.070; 431.101(b)]

A corporation may borrow money to meet any expense or need associated with the operation of the corporation. [Transp. Code §§ 431.065; 431.101(b)]. Additionally, a home-rule municipality with a population of more than 100,000 may create programs for the grant of public money to the local government corporation, as an organization exempt from taxation as described in Tex. Loc. Gov't Code Ann. § 380.002(a). The funds granted by the municipality may be derived from any source lawfully available to the municipality, other than from the proceeds of bonds or other obligations of the municipality payable from ad valorem taxes. For instance, the grant may be made from a revenue source approved by the voters for a sports and community venue project authorized by Loc. Gov't Code Ch. 334 or 335.

c. What is the benefit to the city of using a local government corporation?

Reasons stated by governmental entities for using local government corporations include:

- (1) Greater flexibility in negotiating and awarding contracts related to the development of a municipal project carried out by the corporation. Except in limited circumstances involving navigation districts, local government corporations are not subject to Professional Services Procurement Act or competitive bidding requirements. [Transp. Code § 431.101(e) and (g); Tex. Attorney General Opinion, JC-0335(2001)].
- (2) One or more governmental entities may contract under Chapter 431 for a shared project. Chapter 431 puts all entities on an equal playing field because they are each operating under the broad authority granted under Chapter 431. The local government corporation receives funding from each entity in accordance with an agreement among the entities, and a board carries out the project on behalf of the entities. The board may include members of the various governing bodies of the governmental units creating the corporation.
- (3) Local Government Code Chapter 334 and 335 authorizing sports and community venue projects does not require or specifically provide for the creation of a corporation as Tex. Civ. Statutes art. 5190.6, § 4A and § 4B do. The city (or county) may choose to carry out all aspects of a Chapter 334 or Chapter 335 project. However, in certain instances, the city (or county) may find it beneficial to enter into a contract with a local government corporation to construct, own, lease and/or operate a sports and community venue project. For instance, the city may prefer that the local government corporation issue bonds for the project and act as the owner and lessor of a project.
- (4) If the city wants to transfer land to a local government corporation to carry out a project on behalf of the city, Loc. Gov't Code § 253.011 provides that land may be transferred to a nonprofit organization (such as a local government corporation) without complying with the notice and bidding requirements of Loc. Gov't Code § 272.001(1) or other law provided the organization is required to use the property to primarily promote a public purpose of the city, and provided that the property is conveyed by instrument that indicates the ownership of the property automatically reverts to the city if the nonprofit organization at any time fails to use the property as required.

d. Examples of current uses of local government corporations.

- (1) Two cities created a local government corporation to acquire, construct and operate a water utility system.
- (2) Four cities and a county created a local government corporation to own, fund and operate a performing arts facility.
- (3) A county created a local government corporation to contract with a sports and community venue district for construction of a stadium for an NFL expansion franchise.
- (4) A city created a local government corporation to construct, operate, maintain and obtain project based financing for a convention center hotel.

- (5) Tax Increment Reinvestment Zone (TIRZ or TIF) boards and Municipal Management District boards sometimes choose to utilize a local government corporation to manage revenues and project plans. The powers of the local government corporation are more clearly defined and broader than the powers provided by statute for the tax increment reinvestment zone board.

3. Land as an Economic Development Tool

Is a city or a 4A or 4B corporation authorized to use land as an economic development tool by donating or selling the land at a reduced price for economic development purposes?

a. Notice and Bid Requirements

- (1) General Rule: Notice and bids are required before a political subdivision (including a City) may sell real property unless the sale fits within an exception. Tex. Loc. Gov't Code Ann. § 272.001 (Vernon Supp. 2003).

- (2) Exceptions:

- (a) Tex. Loc. Gov't Code Ann. § 272.001(b)(1)-(7) (Vernon Supp. 2004).

- (i) narrow strips of land, or land that because of its shape, lack of access to public roads, or small area cannot be used independently under its current zoning or under applicable subdivision or other development control ordinances;

- (ii) streets or alleys, owned in fee or used by easement;

- (iii) land or a real property interest originally acquired for streets, rights-of-way, or easements that the political subdivision chooses to exchange for other land to be used for streets, rights-of-way, easements, or other public purposes, including transactions partly for cash;

- (iv) land that the political subdivision wants to have developed by contract with an independent foundation;

- (v) a real property interest conveyed to a governmental entity that has the power of eminent domain;

- (vi) a municipality's land that is located in a reinvestment zone designated as provided by law and that the municipality desires to have developed

under a project plan adopted by the municipality for the zone; or

(vii) a property interest owned by a defense base development authority.

(b) 4A, 4B corporations

Not a political subdivision and not subject to notice and bid requirement contained in Loc. Gov't Code § 272.001. Op. Tex. Att'y Gen. No. JC-109 (1999).

b. Fair Market Value

Statute to consider:

Loc. Gov't Code § 253.011 provides that a city may transfer real property or an interest in real property to a non-profit corporation without complying with notice and bid requirements if an agreement requires the non-profit to use the property in a manner that primarily promotes a public purpose of the municipality. The statute also states that such a contract is adequate consideration. The conveyance must provide for an automatic reverter if the non-profit corporation fails to use the land as agreed.

c. Other statutes on use of public land as an economic development tool.

(1) Tex. Loc. Gov't Code Ann. § 253.001(b) (Vernon Supp. 2004). Land owned, held or claimed as a public square or park may not be sold unless the issue is submitted to the qualified voters and is approved by a majority of votes. Loc. Gov't Code § 253.001(e), (f) and (i) contain exceptions to the election requirement for certain categories of cities.

(2) Tex. Loc. Gov't Code Ann. § 253.010 (Vernon Supp. 2004). Sale of real property to certain non-profit or religious organizations for public housing and revitalization.

## **E. Districts Commonly Created by Municipalities**

1. Public Improvement District Assessment Act  
Tex. Loc. Gov't Code Ann. Ch. 372 (Vernon 1999 & Supp. 2004).

a. What is a Public Improvement District (PID)? The governing body of a city or a group of affected property owners may initiate a petition to declare a defined area of the city a public improvement district. Within the district the city may levy and collect special assessments to finance needed public improvements.

b. What is the funding source? Costs of improvements may be paid from available general funds of the city, any special assessments levied in the district, and from the proceeds of the sale of general obligation bonds and related revenue bonds, temporary notes and time warrants. The special assessment authorized by Chapter 372 is a first and prior lien against the assessed property, superior to all other liens and claims except liens for ad valorem taxes. However, a homestead may not be subjected to forced sale

for nonpayment of a public improvement district assessment because a special assessment is not considered a tax as that term is used in the Texas Constitution. Op. Tex. Att'y Gen. No. JC-0386 (2001).

- c. What is the benefit to the municipality? In certain instances, a public improvement district may benefit the economic development efforts of the municipality by providing a funding source for costs to improve hard and soft infrastructure. Improved infrastructure may help existing businesses in older parts of a city compete with businesses in newer parts of the city. Additionally, new development may be more likely to locate in an area where improvements to aging infrastructure are planned or have occurred. However, a public improvement district may be cost effective only in certain instances. The district is not a new legal entity, but is part of the city. As with all economic development initiatives and incentives, it is important to determine whether a particular initiative, such as the creation of public improvement districts, will result in a net benefit to the city. The city should consider adopting a policy to promote the creation and administration of PIDS in the manner most likely to result in a net benefit to the city.

## 2. Municipal Management Districts

Tex. Loc. Gov't Code Ann. Ch. 375 and Ch. 376 (Vernon 1999 & Supp. 2004).

- a. What is a Municipal Management District? A municipal management district is created in an area devoted primarily to commercial development and business activity to finance facilities, infrastructure, and services beyond what is already provided by the city and the property owners within the district. § 375.021. The municipal management district is a governmental agency and a political subdivision of the state. § 375.004.
- b. What is the funding source for a municipal management district?

Ad valorem property tax. With the consent of at least two-thirds of the number of directors of the district, the district has the power to levy an ad valorem property tax for water, wastewater, drainage, road, or mass transit improvements that are located inside and outside the district.

Impact fees. A district may also levy impact fees pursuant to the state impact fee act (Chapter 395 of the Local Government Code).

Special Assessments. Upon petition signed by the owners of 50 percent or more of the assessed value of the property in the district, or signed by the owners of 50 percent or more of the surface area of the district, the district may use special assessments to finance certain projects or services. Notice and a hearing on the proposed improvements and the proposed method of assessment must be held prior to levying a special assessment. The types of improvements and services for which a management district may levy special assessments include: landscaping, lighting, signs, streets and walkways, drainage, solid waste, water, sewer, power facilities, parks, historic areas, works of art, parking facilities, transit systems, and other similar improvements. The assessments may also fund supplemental services for advertising, economic development, business recruitment, promotion of health and sanitation, public safety, traffic control, recreation, and cultural enhancement.

Bonds. With approval of the governing body of the city, and upon the written petition of a designated percentage of owners, a district may call a bond election and issue bonds and notes.

Rents or fees. A district may charge rents or fees for use of improvements owned or operated by the district.

c. What is the benefit to the City? Allows commercial property owners to provide improvements and services within a defined area to enhance economic development in the city. Because the management district is a legal entity separate from the city capable of hiring its own consultants and employees, the demand for city staff support should be minimal.

d. What is the city's role in creating and managing management districts under Chapter 375?

(1) A resolution adopted by the governing body of the city in support of the district must be submitted to the Texas Commission on Environmental Quality (TCEQ) along with the petition to create the district.

(2) The initial and succeeding board of directors recommend to the governing body of the city persons to serve on subsequent boards. The City's governing body must approve or disapprove the directors recommended by the board. The governing body of the city does not approve the first directors. The governing body of the city may remove a director after a public hearing for misconduct.

(3) Approval of the city's governing body is required:

(a) before a management district may issue bonds for an improvement project.

(b) before a management district may begin a project that involves street right-of-way or city land.

(4) The governing body of the city by two-thirds vote may dissolve the district. The city succeeds to the assets and liabilities of the district.

Note: Loc. Gov't Code Ann. Ch. 376 relates to Specific Municipal Management Districts and each statute creating an MMD may provide a different relationship with the city.

**PRACTICE POINTERS:  
PUBLIC PURPOSE CONSIDERATIONS  
RELATING TO ECONOMIC DEVELOPMENT INCENTIVES**

1. Is the project for which incentives have been requested an integral part of an adopted economic development plan or policy? If so, public purpose is easier to find.
2. Would the project occur without incentives? If so, there is likely to be the perception (or the reality) that the incentive is a useless transfer of public funds from taxpayers to private business interests.
3. Examine the net benefit to the municipality of a particular project. Consider factors that influence companies' location decisions, such as: land and labor costs; labor supply, quality of services; hard and soft infrastructure. If these factors are clearly inferior in your locale, the level of incentives necessary to compete may be inordinately expensive and fail to result in a net benefit to the municipality.
4. Does the investment induced by tax incentives generate new economic activity for the municipality, or simply displace existing business?
5. Will actual net income gains to employees of a new or expanded enterprise be significant? For instance, if a new or expanding facility hires a number of entry-level workers at high salaries in an area with a high unemployment rate, the net income benefits would probably be significant.
6. Will a significant percentage of jobs created by the project flow to local residents? Higher numbers of workers moving to the area can increase the need for new services, schools, and infrastructure. Migrating workers and their families can consume more in local public services than they contribute to local tax revenues.
7. What steps have been taken to ensure the stated public purpose is accomplished? Claw-back (recapture) provisions, deed restrictions, contractual requirements, reporting requirements, use requirements, limitations on use of property are examples of steps that can be taken to see that the public purpose justifying the incentives is accomplished.

**COMPARISON OF STATUTORY ECONOMIC DEVELOPMENT TOOLS**

Tex. Rev. Civ. Stat. Ann. art. 5190.6 § 4B and  
Loc. Gov't. Code Chapter 334

Type of Sales Tax	Election	Petition	Limits on Use of Funds	Funding Source	Separate Legal Entity?
<b>Art. 5190.6 Sec. 4B development corp.</b>	Yes	On city's own initiative or petition of 20% voters at most recent election	<b>Yes.</b> Use only for purposes allowed by Sec. 4B	<ul style="list-style-type: none"> <li>• Sales Tax</li> <li>• Bonds</li> </ul>	<b>Yes,</b> required by law. One per city.
<b>LGC Ch. 334 Venue Projects</b>	Yes	No petition; Approval of initial resolution by State Comptroller	<b>Yes.</b> Use only for purposes allowed by Ch. 334	<ul style="list-style-type: none"> <li>• Sales Tax</li> <li>• Bonds</li> <li>• Admissions Tax</li> <li>• Car rental Tax</li> <li>• Locker Tax</li> <li>• Parking Tax</li> <li>• Hotel Occupancy Tax</li> </ul>	<b>No,</b> not required by law. May create one or more non-profit corp. to administer projects and funds on behalf of city.

**Other Differences between Ch. 334 and 4B**

**Sales tax increase or decrease:**

**Section 4B** - There is no statutory authority for a tax rate to be decreased by ordinance or increased at subsequent elections. The tax could probably be modified at an election even though the statute does not specifically allow it.

**Chapter 334** - The statute specifically provides that a venue sales tax may be decreased by ordinance of the city after it has been approved at a higher rate by the voters. To increase the Chapter 334 venue sales tax would require an election.

**Election Ballot:**

**Section 4B** - There is no required statutory language for the ballot proposition. The sales tax can be authorized without reference to a specific project by a general ballot proposition for the adoption of a Section 4B sales tax for economic development. In the alternative, a specific project can be described and the description of the project in the proposition limits use of the % tax approved for the project to that particular project.

**Chapter 334** - A venue sales tax (or other funding options) and a specific venue project are authorized through use of mandatory wording for the ballot proposition.

**Notice and Hearing:**

**Section 4B** - If a specific 4B project has not been approved by the voters [*Note: in other words, if the ballot proposition authorized a sales tax for economic development without reference to a specific project*], prior to proceeding with a project, a **4B corporation** board must obtain approval of the municipality's governing body. A 4B corporation must provide public notice and hold a public hearing prior to undertaking a project if the specific project has not been approved by the voters. The public has sixty days to petition for an election on whether to pursue the project if it is not a project already approved by the voters.

**Chapter 334** - A specific project and one or more revenue sources is submitted to the voters (as opposed to a proposition to approve a general economic development sales tax). Once the voters approve a venue project and revenue source, no further public hearings or elections are required by law prior to beginning a project.

**Decision Makers:**

**Section 4B** - A 4B corporation is created by the City and the city appoints a board of directors. The board is comprised of seven members and three must be "citizen" members, i.e. not city employees or officials. The remainder of the board may be, but is not required to be, city employees or officials.

**Chapter 334** - A separate legal entity is not required to administer Chapter 334 funds and projects. The City Council may choose to administer Chapter 334 funds and projects, or the City Council may create a non-profit entity to administer the funds and projects and to act on its behalf. A type of non-profit corporation sometimes used is known as a local government corporation under Chapter 431 of the Transportation Code. Its board is comprised of any number of directors, all of whom must be residents of the city. A director may be a member of the governing body, an officer, or an employee of the city (*See* Transportation Code Section 431.102; Local Government Code Section 394.021). The corporation terminates by board resolution when its purposes are served and all obligations have been fully paid. Title to all funds and property of the corporation revert to the city. An example of this 334/335 venue project and local government corporation is the Harris County-Sports and Convention Corporation and the Harris County-Houston Sports Authority.