

Economic Development Sales Tax

Susan Combs, Texas Comptroller of Public Accounts

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Pursuant to the Development Corporation Act of 1979 ("the Act") (Article 5190.6, Vernon's Texas Civil Statutes), voters in many Texas cities have the option of imposing a local sales and use tax to help finance their community's economic development efforts.

These cities may adopt an economic development sales tax rate of 1/8, 1/4, 3/8 or 1/2 of 1 percent if the new total rate of all local sales and use taxes would not exceed 2 percent. They also may limit the duration of the tax and the use of the funds. The Act was recently amended by the 2007 Texas Legislature, Regular Session, by H.B. 2278, H.B. 3440, S.B. 1089, and S.B. 1523.

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Who is eligible?

§4A Sales Tax

All cities located in a county with a population of less than 500,000 may impose the tax under §4A if the new combined local sales tax rate would not exceed 2 percent.

Some cities located in counties with a population of 500,000 or more (Bexar, Dallas, El Paso, Harris, Hidalgo, Tarrant and Travis) may also use §4A for economic development efforts but a city's eligibility varies from county to county. For information on which cities are eligible in these counties, call the Comptroller's Local Government Assistance section toll free at (800) 531-5441, ext. 3-4679.

§4B Sales Tax

All cities are eligible to adopt the §4B tax if the combined local sales tax rate would not exceed 2 percent.

How is the tax administered?

Development Corporations

For both §4A and §4B, the Development Corporation Act requires cities to establish a corporation to administer the sales and use tax funds.

The corporation must file articles of incorporation with the Secretary of State. The articles of incorporation must state that the corporation is governed by Art. 5190.6, §4A or Art.

5190.6, §4B of the Development Corporation Act of 1979.

Board of Directors

The composition of the corporation's board of directors and the length of a member's term differ between §4A and §4B.

Under §4A: The city's governing body must appoint at least a five-member board. Each member is appointed to a term not to exceed six years.

Under §4B: The city's governing body must appoint seven directors. Three of the seven

directors cannot be employees, officers or members of the city's governing body. The other four directors may be — but are not required to be — members of the governing body or city employees. All directors are appointed to a two-year term under §4B.



The directors of a corporation authorized under §4B must be residents of the city authorizing the sales tax if the city's population is 20,000 or more. There is no city residency requirement for §4B directors in cities with less than 20,000 population as long as the director is a resident of the county in which the majority of the city is located, or resides within 10 miles of the city and is in a county which borders the county in which a majority of the city is located.

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The board of directors authorized under §4A and §4B serves at the pleasure of the governing body and must conduct meetings within the city's boundaries.

A corporation's registered agent must be a Texas resident, and the corporation's registered office must be within the city's boundaries.

How can tax revenue be used?

§4A Sales Tax

The tax is primarily intended for manufacturing and industrial development. Cities may use the money raised by this sales tax to acquire or pay for land, buildings, equipment, facilities expenditures, targeted infrastructure and improvements for purposes related to:

- manufacturing and industrial facilities, recycling facilities, distribution centers, and small warehouse facilities;
- research and development facilities, regional or national corporate headquarters facilities, primary job training facilities for use by institutions of higher education, job training classes, telephone call centers, and career centers that are not located within a junior college taxing district;
- a general aviation business service airport that is an integral part of an industrial park;
- certain infrastructure improvements that promote or develop new or expanded business enterprises;

- airport facilities (new as of 2007);
- the operation of commuter rail, light rail or commuter buses (new as of 2007);
- port-related facilities to support waterborne commerce; and
- maintenance and operating costs associated with projects.

After a public hearing and voter approval, §4A corporations may use their revenue to undertake projects eligible under §4B without voting to abolish the §4A tax and impose the §4B tax. The law specifies the §4A corporation's requirements for publishing notice of a proposed §4B project and the procedures for holding at least one public hearing on the proposed project before the election. The

ballot must clearly describe the §4B projects that will be funded from the §4A tax.

§4A corporations may, following a separate election to gain voter approval, spend §4A sales tax to clean up contaminated property.

A corporation created under §4A cannot assume, or pay principal or interest on, debts that existed before the city created the corporation.

§4B Sales Tax

The tax provides cities with a wider range of uses for the tax revenues because it is intended to give communities an opportunity to undertake a project for quality of life improvements, including economic development that will attract and retain primary employers. Before spending §4B sales tax revenue, a corporation is required to hold at least one public hearing on the proposed



The §4A sales tax is primarily intended for manufacturing and industrial development.

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project that will be funded by this tax. §4B corporations created by cities with populations of less than 20,000 are not required to hold public hearings on projects authorized under Section 2 of the Act (same uses as authorized for §4A).

Cities may use money raised by this sales tax for a wide variety of projects including land, buildings, equipment, facilities expenditures and improvements related to projects defined in Section 2 of the Act or found by the board of directors to be required or suitable for use for:

- professional and amateur sports (including children's sports) and athletic facilities, tourism and entertainment facilities, and convention and public park purposes and events (including stadiums, ballparks, auditoriums, amphitheaters, concert halls, parks and open space improvements, museums and exhibition facilities);
- related store, restaurant, concession, parking and transportation facilities;
- related street, water and sewer facilities; and
- affordable housing.

To promote and develop new and expanded business enterprises that create or retain primary jobs, a city may provide:

- public safety facilities;
- recycling facilities;
- streets and roads;

- drainage and related improvements;
- demolition of existing structures;
- general municipally owned improvements;
- maintenance and operating costs associated with projects; and
- any other project that the board determines will contribute to the promotion or development of new or expanded business enterprises that create or retain primary jobs.

§4B corporations created by cities with a population of 20,000 or less and those classified as "landlocked" communities may use sales tax proceeds to fund projects that promote new or expanded business development without the project having to create or retain primary jobs. Landlocked communities are defined as a city that is wholly or partly located in either Harris or Dallas counties and has within its city limits and extraterritorial

jurisdiction less than 100 acres that can be used for the development of manufacturing or industrial facilities in accordance with the zoning laws or land use restrictions of the city.

If a project of this nature would require an expenditure of more than \$10,000, the governing body of the city creating the corporation would have to adopt a resolution authorizing the project after giving the resolution at least two separate readings. However, this additional approval step does not apply to a landlocked community.



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Sewer utilities and site improvements and beach remediation along the Gulf of Mexico are also allowable infrastructure that all development corporations may fund to promote new or expanded business development.

§4B corporations may, following a separate election to gain voter approval, spend §4B sales tax for a water supply or water conservation program or to clean up contaminated property.

Special Provisions for Border Communities

Development corporations created by cities located within 25 miles of the Texas-Mexico border may fund airport facilities if the city has a population of less than 50,000 or an average unemployment rate that is greater than the state average rate during the most recent 12-month period for which data is available preceding when the project is approved. In addition to airports, §4A and §4B corporations located in Hidalgo County may fund airports and sewer or solid waste disposal facilities required or suitable for infrastructure necessary to promote or develop new or expanded business enterprises.



with jurisdiction in that area. For example, if a city locates a project beyond city limits, it should receive approval from the county's commissioners court.

Reporting Requirements of §4A and §4B Corporations

§4C of the Development Corporation Act requires all §4A and §4B corporations to file an annual report with the Texas Comptroller of Public Accounts by February 1. The report must include the corporation's economic development objectives, total revenues and expenditures for the preceding fiscal year, a breakdown of these expenditures and a list of the corporation's assets. The Comptroller may also ask for any other information the Comptroller requires to determine the use

of the sales and use tax imposed under §4A or §4B to encourage economic development in the state. The report form and instructions for submitting the report are available through the Comptroller's office or online at: <https://ecpa.cpa.state.tx.us/edcr/EdcrSearch.jsp>.

The Comptroller will use this information to report to the Legislature each biennium about the use of §4A and §4B sales tax revenues to encourage economic development.

How do you impose the tax?

City voters must approve this special, dedicated tax at an election held for that purpose.

Cities may call for this election in one of two ways:

- the governing body may call an election on its own; or

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Can you undertake projects outside city limits?

An economic development corporation may undertake projects outside city limits so long as it is clear that the city benefits from the project. If a city undertakes a project outside its limits, it must receive permission to do so from the governing body of the entity



- the city must call for the election if petitioned by at least 20 percent of the number of voters who cast ballots in the most recent regular municipal election.

The city's governing body must adopt an ordinance calling for the election at least 62 days before it is held.

The election must be held on one of the two uniform election dates:

- the second Saturday in May; or
- the first Tuesday after the first Monday in November.

How long is the tax effective?

A tax approved without a limit on its duration is effective until repealed by an election. A tax imposed for a specified period expires at the end of that period. A city imposing a tax for a specified period may extend the period or reimpose the tax after its expiration date only with voter approval.



A tax for a specific project expires when all debts related to the project and obligations from the tax proceeds have been paid in full. A tax imposed for a specific project may also be reimposed by an election.

A \$4A or \$4B sales tax is effective until the city notifies the Revenue Accounting, Tax Allocation Section of the Comptroller's office to stop collecting the tax. A city must continue assessing the tax until all obligations incurred by the corporation, including principal and interest on bonds, are satisfied.

What about tax increases or tax decreases?

Initiating Ordinance

As with adoption, the sales and use tax must be increased or decreased in increments of 1/8 of 1 percent with a minimum of 1/8 of 1 percent and a maximum of 1/2 percent and may not result in a combined rate of all local sales and use taxes exceeding 2 percent.

If a city is already imposing a tax under this Act, the city's governing body may adopt an ordinance calling for an election to increase, reduce or repeal the tax rate.

The ordinance may be initiated in either of two ways:

- by a majority vote of the governing body; or
- by petition of registered voters.

Petition Requirements

In order to initiate a change in the rate of a \$4A tax by petition, 10 percent or more of the registered voters must petition the city to call an election for that purpose.

Procedures for tax rate changes are not addressed under \$4B; however, general provisions of the Tax Code for calling an election may be used. Under these provisions, the city council must call an election if a number of qualified voters of the municipality equal to at least 20 percent of the number of votes cast in the most recent regular municipal election petitions the governing body for a vote. Dissolution of a \$4B corporation can be called for by petition of 10 percent of the registered voters in the city.

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If the election to adopt or change the tax rate is by petition, the governing body must determine if the petition is sufficient within 30 days of receiving it. If the petition is sufficient, the city must adopt the ordinance calling for the election within 60 days after receiving it to be held on the next uniform election date.

Reducing or Abolishing a §4A Tax and Adopting a §4B Tax

If a city wants to hold an election to reduce or abolish its §4A sales tax and adopt a sales tax under §4B, the city may address the two issues in a single ballot proposition.

A municipality may combine into one ballot a proposition to lower or repeal any dedicated or special purpose municipal sales tax, and by the same proposition raise or adopt any other dedicated special purpose municipal sales tax. Only sales tax elections that may be called by the governing body of a city would apply. A combined sales tax proposition would have to contain substantially the same language as required for the lowering, repealing, raising or adopting of each tax as appropriate. If a combined sales tax proposition is defeated, there would be no effect on any existing sales taxes already imposed.

When do tax collections and allocations start?

Certifying Election Results

If voters approve the tax, the governing body must adopt a resolution or ordinance declaring the election results in meeting minutes.

The city secretary must send the certified copy of the resolution or ordinance with the election results to the Revenue Accounting, Tax Allocation Section of the Comptroller's office. The information sent to the Comptroller must include:

- the date the election was held;
- the proposition voted on;
- number of votes cast for adoption;
- number of votes cast against adoption;
- number of votes by which the proposition was approved; and
- a statement that the proposition did pass.

The Comptroller's office must receive this information from the city secretary through U.S. certified or registered mail. The Comptroller's office will notify the city secretary when it is ready to handle the administration of the tax.

Effective Date

The tax becomes effective after one complete calendar quarter elapses from the date the Comptroller's office receives notification of voter approval. For example, if voters approve the tax in May, and the Comptroller's office receives notification in June, then the tax becomes effective on October 1, after the calendar quarter of July-August-September has elapsed. The Comptroller's office will notify area merchants to begin collecting the new tax rate on October 1. The city will then begin receiving revenue from the tax in December.



If a city wants to hold an election to reduce or abolish its §4A sales tax and adopt a sales tax under §4B, the city may address the two issues in a single ballot proposition.

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Propositions and Effective Dates for a §4A Tax or §4B Tax with a Tax to Reduce the Property Tax Rate

If a city wants to adopt the §4A sales tax and a sales tax to reduce the property tax rate in the same election, the city may address them in a single ballot proposition. If the proposition passes, the sales tax to reduce the property tax rate must take effect on October 1 after one complete calendar quarter

has elapsed. The §4A tax would start at the beginning of the first calendar quarter after the completion of one full calendar quarter.

If a city wants to adopt a sales tax under §4B and a sales tax to reduce the property tax rate in the same election, the city must address them as two separate ballot propositions. If voters approve both of these propositions, they both become effective on October 1.

Ballot Language for the Economic Development Sales Tax

Under §4A

Following is ballot language specified under §4A of the Development Corporation Act:

1. For a city to adopt, increase or reduce the tax, the ballot must state: *The adoption of a sales and use tax for the promotion and development of new and expanded business enterprises at the rate of _____ of one percent. (Insert one-eighth, one-fourth, three-eighths or one-half as appropriate for the proposed tax rate.)*
2. A city may also hold an election to adopt, increase, reduce or repeal the §4A sales tax and the sales tax to reduce the property tax rate on the same ballot: *The adoption of a sales and use tax within the city for the promotion and development of new and expanded business enterprises at the rate of _____ of one percent (insert one-eighth, one-fourth, three-eighths or one-half as appropriate for the proposed tax rate) and the adoption of an additional sales and use tax within the city at the rate of _____ of one percent to be used to reduce the property tax rate. (Insert one-eighth, one-fourth, three-eighths or one-half as appropriate for the proposed tax rate.)*
3. A city may also allow a vote on a ballot proposition limiting the length of time a sales and use tax may be imposed. The following language should be added to #1: *to be imposed for _____ years.*
4. A city may also indicate a specific project on the ballot to be funded with the sales tax revenue. In this case, a description of the project is substituted in #1 or #2 in place of the following ballot language: *new and expanded business enterprises.*
5. For a city to dissolve the §4A corporation, the ballot should state: *Dissolution of the (name of development corporation).*

Under §4B

Except for specific projects such as water supply facilities, water conservation programs and cleanup of contaminated property, the Development Corporation Act does not provide specific ballot language for §4B. City officials should consult with their city attorneys when drafting the ballot language under this section.

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Comptroller representatives can provide presentations on matters related to local sales tax, including §4A and §4B sales taxes.

Method of Payment

The Comptroller's office will issue a payment for the total city tax and a letter with the first payment (that includes the economic development sales tax) with instructions explaining how to calculate the portion due the city and what is due the development corporation. After a city receives the sales and use tax revenues from the Comptroller's office, the city must deliver the revenue to the development corporation.

Need more information on the economic development sales tax?

Comptroller representatives can provide presentations on matters related to local sales tax, including §4A and §4B sales taxes. Representatives can also meet in forums with city officials and the public to help them assess possible effects of the tax on

their local communities, including effects on revenue. For more information about the sales tax, or to request a speaker to present information about the sales tax to your community, call toll free (800) 531-5441, ext. 3-4679. The Office of the Attorney General (OAG) also has an *Economic Development Handbook* (2006) containing more detailed information as well as citations to the various statutes, which can be viewed on the OAG Web site at <http://www.oag.state.tx.us/newspubs/publications.shtml> by clicking on "Handbooks and Special Reports."

Disclaimer: This brochure should not be construed as, and is not a substitute for, legal advice. Cities are urged to consult their own legal counsel for any questions or interpretations about economic development laws.

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