

SUBJECT: Expanding uses for 4B sales tax for cities with lower tax revenue

COMMITTEE: Economic Development — committee substitute recommended

VOTE: 5 ayes — B. Cook, Anchia, Deshotel, Kolkhorst, McCall

0 nays

2 absent — Ritter, Seaman

WITNESSES: For — (*Registered, but did not testify*: Donna Chatham, Association of Rural Communities in Texas; Carlton Schwab, Texas Economic Development Council)

Against — None

BACKGROUND: The Development Corporation Act of 1979, V.T.C.S., art. 5190.6, authorizes Texas cities to establish nonprofit industrial economic development corporations that are authorized to spend municipal sales tax dollars for the purpose of financing projects to develop certain businesses and promote the creation and retention of primary jobs. A city may levy a sales and use tax, which is approved by local voters, for the benefit of a development corporation and the projects it finances. Two types of development corporations, known as “4A” and “4B,” are named after the sections of the act in which they were established. A 4B development corporation dedicates proceeds of this tax for use in financing and promoting a wide range of economic development projects, including for specific quality-of-life improvements such as parks, affordable housing, entertainment facilities, and other similar categories defined by the act.

The general definition of an economic development project includes infrastructure developments — such as streets and utilities — and job training, both for the purpose of developing primary jobs. A primary job is a job in a company of which the majority of products or services ultimately are exported to markets outside the city where the company is located. A primary job also is one that is included on the act’s list of specific qualifying job sectors, examples of which include manufacturing, management of companies, and scientific research. HB 2912 by Homer, enacted in 2003 by the 78th Legislature, amended the act to require the

direction of economic development projects toward the creation of primary jobs.

**DIGEST:**

CSHB 2755 would amend the definition of an economic development project to include elements that a 4B corporation found suitable for the development, retention, or expansion of business enterprises in its community. This would apply to a 4B corporation in a city that had not received more than \$50,000 in sales and use tax revenues per year for the preceding two years. In addition, the city's governing body would have to have authorized the project by adopting a resolution that received two separate readings at least one week apart.

The bill would take immediate effect if finally passed by a two-thirds record vote of the membership of each house. Otherwise, it would take effect September 1, 2005.

**SUPPORTERS  
SAY:**

CSHB 2755 would grant greater flexibility to development corporations in how they spent 4B sales tax funds. Some of the reforms enacted last session were too restrictive and greatly reduced the benefits a development corporation might have for towns that generate small sums of tax revenue. It is unrealistic to expect, for example, that a development corporation in a small town could attract outside business for the creation of primary jobs with a mere \$10,000 per year in tax revenue to spend on a project. These towns need the flexibility to fund projects that work for them, which was allowed under the act prior to the changes made last session.

Before the 2003 revisions, 4B development corporations were designed to be more flexible than the 4A model and to allow for smaller communities to finance a variety of quality-of-life improvements. CSHB 2755 simply would return the law governing development corporations in smaller communities to its original purpose.

The bill contains the necessary safeguards to protect against misuse of development funds. For example, the \$50,000 cap on tax revenues would ensure that the bill would apply only to small communities that truly need the flexibility, not to suburbs with small populations and large tax revenues. In addition, an eligible town could not exceed \$50,000 in revenues for two consecutive years, which would prevent a community from engaging in creative accounting to fit under the cap — changing the length of one fiscal year, for example. Finally, the bill would require that any project proposal be addressed at two city council meetings at least a

week apart, which would support due process in the community by allowing all interested parties to receive appropriate notice.

A statewide survey found that 85 percent of development corporations in rural communities favor a change in law to allow them to better use their development corporation tax funds. This bill would assist more than 100 communities with 4B development corporations.

Any jobs, primary or otherwise, stand to improve economic development in rural communities. Rural communities increasingly have difficulty recruiting industrial companies and must compete with cities around the world to attract these businesses. The focus should turn in part to developing local entrepreneurship as a means to economic development, which this bill would support.

**OPPONENTS  
SAY:**

The enactment of HB 2912 last session simply refocused the Development Corporation Act on its intended mission of attracting new businesses from outside a community for the purpose of creating primary jobs. Prior to these reforms, some development corporations had begun to interpret the act very liberally, which led to misuse of funds. For example, there were reports that funds were being used to compensate for municipal budget shortfalls and to purchase city vehicles, which are not the intended uses of 4B sales tax dollars. CSHB 2755 would allow a return to such inappropriate spending by economic development corporations. Even if the bill would apply to only 100 communities, any retreat from the act's original intent of supporting primary job creation would be questionable.

This bill improperly would allow retail businesses to receive funds, which would not result in the creation of primary jobs. Development corporation tax dollars should be used to attract new jobs from companies with ties outside of the community, which in turn would attract and support local retailers by pumping new dollars into the town. Giving 4B grants to local entrepreneurs may support those businesses at the expense of other local businesses. Such an investment would not create new dollars for a community, but simply would recycle local dollars.

**NOTES:**

The committee substitute differs from the original bill in that it would require the city's governing body to authorize the project following the two hearings conducted at least one week apart.

HB 2928 by Kolkhorst, a related bill that would expand permissible uses of 4B corporation funds in cities of 20,000 or less, passed the House on May 2 and has been referred to the Senate Business and Commerce Subcommittee on Emerging Technologies and Economic Development.