ARKANSAS FINANCING OPTIONS FOR ECONOMIC DEVELOPMENT

FORWARD

"You can't just ask customers what they want and then try to give that to them. By the time you get it built, they'll want something new." – Steve Jobs

Steve Jobs' quote regarding constant innovation is certainly applicable in today's economic development and business environment. Many innovative ideas and strategies pass us by daily simply because we haven't the tools or financial resources to take advantage of them.

Reacting to this concept is what led Entergy's Teamwork Arkansas to commission this report after realizing too few local economic development organizations are sufficiently able to invest in the future of their communities due to a lack of funding. Those who have had the resources have been able to successfully attract or retain jobs because they were willing to provide the means for those investments.

This report is intended to be a resource guide for the local economic development professional. It summarizes the various methods for Arkansas cities and counties to fund economic development activities. I hope it will be a useful resource for you in directing the future of your community. Undoubtedly, having financial resources available to purchase land, build infrastructure, certify sites, develop training programs, create retention programs and provide financial incentives to close deals will better position your community for future growth.

Please don't hesitate to contact us if we can ever be of assistance.

Best Personal Regards,

Mike Maulden

Mike Maulden

The following study was funded by Entergy's Teamwork Arkansas in order to identify the available methods for cities and counties to fund economic development in Arkansas.

INTRODUCTION

THE IMPORTANCE OF ECONOMIC DEVELOPMENT FINANCING

No single agency can be entirely responsible for funding project success at the local level. Resources have to be drawn from a variety of sources to tackle the complex demands that a community/county typically faces with a given project whether that is an expansion or new location.[1]

Attracting investment and jobs is more competitive than ever and being prepared can create an advantage. By having an available and reliable source of funding for economic development, a community has more opportunity to control its own destiny. In addition, it is critical to recognize that many communities already have financing tools in place which allow them greater flexibility in structuring a deal to secure a project.[2]

The City of Crossett has been highly progressive by twice passing sales taxes to directly support economic development. In a recent deal, it was necessary for our community to make significant contributions to the project in order to access state and federal funding for infrastructure. Our dedicated funding stream proved to be an essential element in landing this $10 million project. We have discovered that regardless of how much federal and state agencies desire to assist in the development of our community, they are powerless to do so without the commitment of local resources.[3]

FUNDING OPTIONS FOR ECONOMIC DEVELOPMENT BY LOCAL GOVERNMENTS IN ARKANSAS[4]

The following is a summary of options available to Arkansas counties and municipalities to fund local economic development. This document does not contain a comprehensive list of all of the requirements and limitations of each potential funding method. You should seek assistance from an attorney experienced in municipal finance to ensure compliance with all of the legal nuances contained in the requirements for each potential method.

Generally speaking, economic development can be accomplished by financing (1) facilities, which consist of real property, site development, bricks and mortar projects and capital property, and/or (2) soft costs, which could include job training, marketing, administration and planning. As a general provision of Arkansas law specific constitutional and/or statutory authority is required in order for a local government to levy a tax or a fee or to issue bonds. Below, potential sources of economic development funding and possible uses of such funds are discussed.

SALES AND USE TAXES

Various Arkansas statutes authorize local governments to levy sales and use taxes. Sales and use taxes can be general taxes with no designated use or general taxes or specific taxes for which a specific use, such as economic development, is designated. The levy of a sales and use tax by a local government requires an election. The ballot may contain a sunset clause for the levy.

General Sales and Use Taxes With Designated Purposes

Local governments levying a general sales and use tax can use the ballot language to designate the purposes of the tax or to allocate collections among purposes. If purposes are listed on the ballot, the collections may be spent on no other purpose. The designation of specific uses can serve a political purpose because voters might be more likely to approve a sales and use tax if they know exactly what the tax collections will be used for. In addition, interested groups may want the purposes listed in order to ensure that the collections will be used for the ballot purposes.

Economic Development Sales and Use Taxes[5]

Local governments may also levy a sales and use tax which can only be used for certain economic development purposes. Specifically, local governments can levy a sales and use tax to provide funds to stimulate the local economy and to support private sector job creation by funding water and sewer system improvements, streets, bridges, drainage and other public facilities or by establishing and operating local economic development programs. Thus, an economic development sales and use tax can be levied for bricks and mortar projects as well as for soft costs such as economic and industrial development planning, marketing, advertising, public relations, supervision and operation of industrial parks, negotiation of contracts for the sale or lease of such properties and such other operating expenses as is deemed necessary, convenient or appropriate. The local government may contract with non-profit economic development corporations for these services. In addition, a sales and use tax can be used for the sole use and benefit of a Public Corporation for Economic Development (see page five, *Public Corporations for Economic Development*). Two or more municipalities in a county or two or more adjacent counties may enter into agreements to jointly perform the powers discussed in this section.

Sales and Use Tax Bonds[6]

Local governments can also issue bonds secured by a local sales and use tax to finance capital improvements of a public nature after approval by an election. Capital improvements of a public nature include streets, water and sewer systems and numerous other capital facilities. These improvements can be used to assist with economic development. As only “facilities” are authorized to be financed, bonds can only be issued for bricks and mortar projects, not for soft costs.

HOTEL & RESTAURANT TAXES

Local governments are authorized to levy gross receipts taxes on hotels and restaurants. This type of tax is commonly called a “hamburger tax.” Hamburger taxes do not have to be approved at an election.

Municipal Hotel and Restaurant Tax[7]

A municipal hamburger tax is collected by an advertising and promotion commission, and collections can be used for both facilities and for soft costs. Uses of collections include advertising and promotion of the municipality and its environs, construction and improvement of a convention center, operation of tourist promotion facilities and payment of bonds issued for convention center projects. A municipality organized as a city of the first class[8] can also use collections of a hamburger tax to finance construction and operation of tourist-oriented facilities, such as theme parks. Cities of the first class which have a city park of 1,000 acres or more can also use collections of a hamburger tax to finance construction and operation of parks. The municipal advertising and promotion commission dictates how the funds derived by a municipal hamburger tax are spent.

County Hotel and Restaurant Tax[9]

Counties are more restricted in levying hamburger taxes. Counties in which a municipality is levying a hamburger tax can also levy a hamburger tax, but the collections of the tax are deposited into the municipal advertising and promotion fund to be used as the municipal advertising and promotion commission dictates. Counties in which no municipality is levying a hamburger tax can levy a hamburger tax, but the collections of the tax can only be used to pay debt service on bonds issued by a county public facilities board to finance wildlife management areas or public recreational facilities.

Municipal Hotel and Restaurant Tax Bonds[10]

Certain capital improvements of a public nature can be financed by both municipal sales and use tax and hamburger tax bonds. These improvements include convention and meeting facilities, water theme parks, community centers and ballparks. Such facilities can be used to assist with economic development. As only “facilities” are authorized to be financed, bonds can only be issued for bricks and mortar projects, not for soft costs. As with sales and use tax bonds, an election is required in order to issue municipal hotel and restaurant tax bonds. As an example, the City of Dumas, Arkansas, has used hotel and restaurant tax bonds to finance the construction of a convention center.

PROPERTY TAX BONDS[11]

Local governments can levy property taxes and pledge the tax collections to pay bonds issued to finance capital improvements of a public nature and facilities for securing and developing industry. An election is required prior to levying the property tax and issuing the bonds. Capital improvements of a public nature include streets, water and sewer systems and numerous other capital facilities. Facilities for securing and developing industry include (i) facilities and improvements necessary or useful for securing, developing, preserving or maintaining economic activity within or near the municipality or county, including, but not limited to manufacturing facilities, (ii) warehouse and storage facilities, (iii) distribution facilities, (iv) repair and maintenance facilities, (v) communications facilities, (vi) facilities for computer and data processing equipment and related facilities, (vii) agricultural storage, processing, packaging, shipping and other agricultural facilities, (viii) transportation facilities, (ix) tourism facilities, (x) corporate and management offices for industry and (xi) industrial parks. The bonds can only be issued for bricks and mortar projects, not for soft costs. Local governments can finance facilities and lease them to private industries.

The property tax levied is only authorized to be used to pay the bonds when due. The local government is authorized to suspend the levy of the property tax if an industry is paying debt service sufficient to pay the bonds when due.

REVENUE BONDS

Local governments can issue "revenue bonds" to finance capital improvements of a public nature and for facilities for securing and developing industry or agriculture. "Revenue bonds" are bonds payable from any source other than taxes or assessments. Revenues are typically derived from sources such as franchise fees and utility systems. Generally speaking, an election is not required for the issuance of local government revenue bonds; however, an election is required when the revenue bonds are issued to finance hotels or motels, rental or professional office buildings or facilities for recreation or entertainment for one or more private business users. In addition, revenue bonds cannot be issued if the primary purpose of the bonds is to finance shopping centers or other establishments engaged in the sale of food or goods at retail for a private business user.

Industrial Development Revenue Bonds[12]

Local governments can issue revenue bonds to finance facilities for securing and developing industry and tourism. These bonds are commonly called "Act 9 Bonds." Facilities can be owned by the local government and leased to an industry. Proceeds of Act 9 Bonds can also be used to make loans to industries to finance facilities. Only facilities can be financed, so Act 9 Bond proceeds cannot be used to finance soft costs. Act 9 Bonds would be repaid through revenues derived from payments by the industry or the tourism facility. Mississippi County has recently issued Act 9 Bonds to finance land, facilities, machinery and equipment for a steel manufacturer.

Capital Improvement Revenue Bonds[13]

It should be noted that the list of capital improvements for which capital improvement revenue bonds can be issued does not specifically include "economic development facilities." However, capital improvements which may be financed include, among other facilities, ports, streets and water and sewer improvements. Certain capital improvements, such as streets and utility infrastructure, can serve as ancillary projects to economic development projects. Capital improvement revenue bonds would be repaid from specific non-tax revenues of the local government, which revenues can include franchise fees and surplus electric, water and sewer revenues. As with Act 9 Bonds, proceeds of capital improvement revenue bonds can only be used for facilities and cannot be used for soft costs.

Public Facilities Boards Revenue Bonds[14]

Public facilities boards formed by a municipality or a county can issue revenue bonds to finance, among other things, tourism facilities and facilities for the securing and developing of industry, public transportation facilities and water and sewer facilities. As with other types of revenue bonds, proceeds of revenue bonds issued by public facilities boards can only be used to finance facilities, not soft costs. Public facilities board revenue bonds would be secured and repaid by revenues of the project or other specific revenues.

FRANCHISE FEES[15]

Municipalities can levy franchise fees on utilities using public rights of way without an election. As previously noted under *Capital Improvement Revenue Bonds*, franchise fees can be pledged to municipal revenue bonds, which can generally be issued without an election. The Arkansas Supreme Court has addressed the levy of franchise fees, and its decisions suggest that franchise fees should be deposited into the municipal general fund. Thus, while municipalities can use funds in the general fund for public purposes, which could include economic development purposes, it is not advisable to specifically dedicate or pledge franchise fees to economic development or any other purpose by ordinance. It also is not advisable to increase franchise fees in response to a revenue bond issue. In either case, there is concern that the franchise fee could be construed as constituting a tax, for which an election would have been required. Franchise fees may not exceed the higher of (i) the amount in effect on January 1, 1997 or (ii) 4.25% unless agreed to by the affected utility or approved by the voters of the municipality. As an example, the City of Bryant, Arkansas has pledged franchise fees to capital improvement revenue bonds issued to finance street construction and improvements.

PUBLIC CORPORATIONS FOR ECONOMIC DEVELOPMENT[16]

Recent legislation authorizes the formation of a public corporation for economic development (a “PCED”) in order to secure and develop industry and to foster economic development. An economic development sales and use tax can be levied in order to provide funds for a PCED. Clark County has levied an economic development sales and use tax in order to fund a PCED.

A PCED has broad authority to finance facilities and programs for economic and industrial development and job creation. Moneys of the PCED, including collections of an economic development sales and use tax if the voters approve such tax, may be used for facilities and infrastructure, promotional purposes, job training for certain jobs and post-secondary education meant to provide certain jobs. A PCED can also lease facilities to businesses, sell facilities to businesses and loan funds to businesses. Thus, a PCED funded with an economic development tax provides numerous options to promote industrial and economic development with the authority to spend funds on both bricks and mortar projects and soft costs.

It should be noted that the PCED authorizing legislation provides certain limitations on the expenditure of funds based on the types of jobs expected to be created as a result of such expenditures. Specifically, the legislation contemplates the creation of “primary jobs,” which are defined as jobs at an enterprise (i) for which a majority of the products or services of that enterprise are ultimately used in regional, statewide, national or international markets infusing new dollars into the local economy and (ii) that derives less than 10% of its total Arkansas revenue from sales to the general public.

REGIONAL INTERMODAL AUTHORITIES[17]

Arkansas law allows two or more municipalities, two or more contiguous counties or one or more municipalities together with one or more contiguous counties to form a regional intermodal authority for the purpose of acquiring, equipping, constructing, maintaining and operating regional intermodal facilities, which includes facilities related to more than one mode of interconnected movement of freight, commerce or passengers. Modes include railway, highway, air, pipeline, waterway, transit and communication systems and related means of movement of freight, commerce or passengers. These facilities could be used as a economic development tool. Regional intermodal authorities can levy fees and issue revenue bonds. Regional intermodal authorities usually qualify to receive federal and state grants for projects.

RESEARCH PARK AUTHORITIES[18]

One or more municipalities, counties or state agencies, along with a sponsoring accredited institution of higher education, may create a research park authority which provides research facilities in order to assist research development and Arkansas entrepreneurs. Research park authorities have a broad range of powers to finance facilities to provide research parks, including the power to issue bonds. Research park authorities may engage in (i) research, (ii) development of certain products and services, (iii) production of certain materials and products and (iv) acting as support or resource services and suppliers in connection with certain items. A research park authority could provide economic development for technology businesses.

PAYMENTS IN LIEU OF TAXES[19]

Payments in lieu of taxes, which are commonly referred to as "PILOTs," are economic incentives whereby an industrial user of property makes certain payments to the local government as opposed to paying property taxes on such property. The property must be owned by a municipality or county and must be the subject of an Act 9 Bond issue by the municipality or county. The industrial user repays the bonds. PILOTs may be negotiated with the local governments and other taxing authorities. The PILOTs cannot be less than 35% of what the property tax payments would have been unless a lesser amount is approved by Director of the Arkansas Economic Development Commission and by the Chief Fiscal Officer of the State of Arkansas. For instance, if property tax payments were to be $100,000 per year, the PILOT payment must not be less than $35,000 per year unless a lesser amount is approved as provided in the previous sentence. PILOTs are commonly used to attract industries.

INDUSTRIAL DEVELOPMENT COMPACTS[20]

The Arkansas Constitution authorizes two or more municipalities and/or one or more counties and the school districts therein to enter into a compact and join together in a combined effort to secure and develop industries within one or more of such municipalities and counties and share in the increased revenues estimated to be received by the municipality, county or school district in which the industry or industries are to be located. An election to approve the compact and the method in sharing the increased revenues is required.

INTERLOCAL AGREEMENTS[21]

In addition to the numerous economic development tools listed above, local governments have wide authority to enter into agreements with other local governments and political subdivisions provided that each local government is authorized to engage in such activity on its own. Interlocal agreements could be entered into in order to provide funding and resources for economic development. All formal interlocal agreements must be submitted to the Arkansas Attorney General for approval. Local governments may associate and cooperate with one another on an informal basis without complying with the detailed procedure required for formal interlocal agreements.

CONCLUSION

In order to better understand the value of investing public monies in economic development initiatives, it is often a good idea to track those dollars as they circulate through the local economy. One widely recognized method is to conduct an economic impact analysis for a particular investment in a given locale or region.

In the case of Cross County Arkansas, a study was conducted to determine whether or not an increase in wealth occurred in the County based on the collection and investment of a sales tax for economic development. The study, conducted

by the Delta Center for Economic Development at Arkansas State University utilized the Impact Analysis for PLANning (IMPLAN) model of input-output. This is the same model that is used by the Arkansas Economic Development Commission to determine whether to offer (and to what extent) incentives to new and expanding industry. The study noted the revenues collected during the three year period of the tax (1999 – 2002) and the disposition of those dollars over an eight year period beginning with the initial date of collection in September, 1999 and concluding in December 2007. The study then looked at the direct jobs and investment created by the Cross County Economic Development Commission during the eight year period and calculated the indirect and induced jobs and investment utilizing the IMPLAN model. It was determined that a total of $4,636,544.74 was generated during the collection period. However, only $3,300,000 had been expended during the 8 year study cycle. Further, the study found that approximately $90,119,000 in direct and indirect economic benefits
flowed into the county as a result of the tax investment. Utilizing those figures, it was determined that Cross County realized a 27:1 Return on Investment.[22] It is clearly demonstrated from this example that when properly managed, an economic development sales tax is a solid investment in the future of a community.

Local governments in Arkansas have numerous alternatives for funding economic development projects and services. However, the vast majority of such funding authority contemplates only the financing of facilities which consist of bricks and mortar projects and other capital property. Nevertheless, there are several funding methods for soft costs which can be used for economic development.

This document intended as a summary of funding options only. A municipal finance attorney should be contacted for more information regarding each potential funding method.

ENDNOTES

1 Robert Pittman, Senior Principal, Janus Economics, LLC, 2009
2 Mark Sweeney, Senior Principal, McCallum Sweeney Consulting, 2009
3 Mike Smith, Executive Director, Crossett Economic Development Foundation, 2009
4 Benham, Paul B. III & Moyers, D. Michael, Funding Economic Development for Arkansas Local Governments. Friday, Eldredge & Clark, LLP, 2009.
5 A.C.A. § 14-174-101 et seq.
6 Arkansas Constitution, Amd. 62 and A.C.A. § 14-164-301 et seq.
7 A.C.A. § 26-75-601 et seq.
8 Defined at A.C.A. § 14-37-104.
9 A.C.A. § 14-20-112 and A.C.A. § 26-74-501 et seq.
10 Arkansas Constitution, Amd. 62 and A.C.A. § 14-164-326.
11 Arkansas Constitution, Amd. 62 and A.C.A. § 14-164-301 et seq.
12 Arkansas Constitution, Amd. 65 and A.C.A. § 14-164-201 et seq.
13 Arkansas Constitution, Amd. 65 and A.C.A. § 14-164-401 et seq.
14 Arkansas Constitution, Amd. 65 and A.C.A. § 14-137-101 et seq.
15 A.C.A. § 14-200-101.
16 A.C.A. § 14-175-101 et seq.
17 A.C.A. § 14-143-101 et seq.
18 A.C.A. § 14-144-101 et seq.
19 A.C.A. § 14-164-701 et seq.
20 Arkansas Constitution, Amd. 62, § 9.
21 A.C.A. § 25-20-101 et seq.
22 Economic Impact Analysis, A review of the economic impact of the 1999 Cross County, AR economic development funding initiative from Sept. 1999 – Dec. 2007. Prepared by The Delta Center for Economic Development at Arkansas State University, 2008.