

SUBJECT: Continuing TDED as Texas Economic Development and Tourism Office

COMMITTEE: Economic Development — committee substitute recommended

VOTE: 5 ayes — J. Keffer, Homer, Rodriguez, Thompson, Wong

0 nays

2 absent — Isett, Hughes

SENATE VOTE: On final passage, April 24 — voice vote

WITNESSES: *(On House companion bill, HB 1233:)*

For — Paul Serff, Texas Travel Industry Association; *(Registered but did not testify:)* Dana Chiodo, American Electronics Association; Scott Joslove, Texas Hotel and Motel Association; Tom Kowalski, Texas Healthcare and Bioscience Institute; Michael Meek, Greater New Braunfels Chamber of Commerce; Amanda Oneacre, Greater Dallas Chamber of Commerce; David Pinkus, Small Business United of Texas; Carlton Schwabb, Texas Economic Development Council

Against — None

On — Jeff Moseley, Texas Department of Economic Development

BACKGROUND: The Texas Department of Economic Development (TDED), the primary state agency for promoting tourism and economic development, serves as the state's first point of contact for businesses interested in locating or expanding in the state and helps match these businesses with interested communities. TDED also helps businesses and communities obtain capital; promotes tourism in Texas; oversees the state's economic investment program for struggling communities; and serves as a central source for economic development information.

The 75th Legislature established TDED in 1997 to replace the Texas Department of Commerce. The department is governed by a nine-member board appointed to represent all regions of the state. Four members must

represent various economic interests and experience, including rural counties, tourism, international trade, and economic development practitioners. Board members are appointed by the governor, who also chooses one member to serve as chair. The board directs the activities of the department, reviews its budget, and hires the executive director.

For fiscal 2002-03, TDED's budget was approximately \$68.4 million. Hotel occupancy tax revenues make up almost 60 percent of the agency's funding. TDED is subject to the Texas Sunset Act and will expire September 1, 2003, unless continued by the Legislature.

Tourism. Tourism promotion, TDED's largest program, primarily involves advertising and marketing Texas to potential travelers outside the state. TDED also helps communities develop local tourist attractions and maintains the Internet website *TravelTex.com* with four other state agencies. TDED also works with private travel-related businesses, works with the media to generate publicity about the state, and researches travel and tourism patterns.

Business incentives. TDED operates several business incentive programs to assist economically distressed communities and encourage economic development. The programs use tax abatements, bond projects, loans, and grants and include the Industrial Revenue Bond Program, Texas Small Business Development Corporation, Texas Leverage Fund, Capital Access Program, Linked Deposit Program, Defense Economic Readjustment Zone Program, and Texas Enterprise Zone Program.

Enterprise zone program. Through the enterprise zone program, TDED can authorize abatements of state sales and franchise taxes for businesses that agree to locate and invest in communities that the department has identified as economically distressed. A business receiving incentives through the program must create or retain jobs and must fill at least 25 percent of the jobs with residents of the designated enterprise zone. To qualify for the program, a community must have more than 1.5 times the state unemployment rate, at least a 12 percent population loss for the most recent six years, and either a high poverty rate, high tax average, or increased level of juvenile criminal activity. An area is designated as an enterprise zone for a maximum of seven years.

Information clearinghouse. TDED's Economic Information Clearinghouse provides access to state economic data for businesses and the public. The clearinghouse consists of four programs: Business and Industry Data Center, Business Information and Referral, Small Business Assistance, and Economic Research and Analysis.

Market Texas Business. TDED promotes business expansion in Texas through media placement and mail campaigns. The department also responds to inquiries about doing business in the state, helps identify site locations for prospective firms, and coordinates site visits. TDED promotes international business by helping Texas companies expand international markets for their products. The department operates a Mexico City office that serves as a liaison between firms and markets in Texas and Mexico, coordinating trade shows, following trade leads, and communicating with interested companies.

Texas Economic Development Corporation. The Texas Economic Development Corporation, created in 1987, is a nonprofit corporation that raises private funds to support TDED programs and activities. TDED's governing board also serves as the corporation's board of directors. In fiscal 2001, corporate funds totaled about \$41,000.

Texas Aerospace Commission. The Texas Aerospace Commission is an independent state agency created in 1987 to foster the development of the commercial space industry in Texas. With the decline of this industry, the commission now focuses on promoting the aerospace industry in the state. Its fiscal 2002-03 budget was about \$450,000.

DIGEST:

CSSB 275 would rename TDED as the Texas Economic Development and Tourism Office (TEDTO). The office would be transferred to the Office of the Governor and continued until September 1, 2015.

The bill would abolish TDED's governing board and require the governor to appoint the TEDTO executive director, who would manage the office's affairs under the governor's direction. The governor would have to assume the duties previously held by the governing board in directing the office's activities, establishing its policies, reviewing its budget, and developing long-term plans for the office. The governor also would appoint the board of directors of the Small Business Industrial Development Corporation.

Tourism promotion. CSSB 275 would specify tourism promotion as the new office's primary duty and would establish it as the sole state governmental entity responsible for out-of-state tourism marketing efforts. TEDTO would have to enter into a memorandum of understanding with the Parks and Wildlife Department, Department of Transportation, Historical Commission, and Commission on the Arts to direct those agencies' tourism efforts. TEDTO could direct each agency's activities to meet consumer demand and minimize costs by sharing expenses and eliminating duplication of efforts.

Each agency with which TEDTO partnered would have to submit for approval any resources or activities used in tourism promotion, as well as a plan of action for tourism activities. This plan would have to include the agency's tourism priorities, proposed budget, goals, and any proposed tourism-related message, material, or other communication. TEDTO would have to develop an annual strategic plan to coordinate the effective and efficient expenditure of funds and to establish goals and performance measures for all state tourism-related efforts.

Aerospace and Aviation Office. The bill would abolish the Texas Aerospace Commission and transfer its functions into TEDTO, renaming it as the Texas Aerospace and Aviation Office. The office would be charged with fostering development of the aerospace and aviation industries in Texas by analyzing space and aviation-related research, developing business strategies to promote the retention and expansion of these industries, making recommendations to the Legislature and governor regarding the promotion of these industries, cooperating with other governmental entities with related responsibilities, and supporting state and local spaceport authorities. The director of the Aerospace and Aviation Office would be hired by TEDTO.

Small business advocate. TEDTO's executive director would have to designate a person to serve as small business advocate, the state's central official for assisting small and historically underutilized businesses. This person would have to identify state rules and policy goals that harm small business development and would have to provide support for those businesses' activities.

Identifying and supporting industry clusters. CSSB 275 would require TEDTO to work with industry associations and organizations to identify

regional and statewide “industry clusters,” or concentrations of businesses and industries in a region that are interconnected through their markets, products, suppliers, and labor pools.

TEDTO would have to identify, evaluate, and support the economic position of industry clusters by conducting focus group discussions, encouraging professional industry cluster associations, and facilitating information dissemination throughout the clusters. The office would have to work with local governments, local economic development organizations, and higher education and training institutions to strengthen the competitiveness of industry clusters. TEDTO would have to pursue strategies to diversify the economy, facilitate the transfer of technology, and increase value-added production. TEDTO would evaluate the effectiveness of its services to aid industry clusters and determine the return on those programs.

TEDTO also would have to identify and assist in the development of targeted high-priority industry sectors. Activities could include providing employees, consultants, and funding to create flexible networks; establishing research consortia; facilitating training programs; promoting cooperative market development; and evaluating the need for product testing facilities.

TEDTO would have to coordinate efforts to attract, develop, and retain high-technology industries in sectors such as semiconductors, information technology, and biotechnology. The office would have to recommend actions to promote these industries, identify specific opportunities in these fields, and engage in outreach and joint ventures with these industries.

Economic development bank. CSSB 275 would create the Texas Economic Development Bank, which would provide incentives for expanding and relocating businesses. The bank would have to ensure that communities had access to capital for economic development purposes. It would combine the functions of several current programs and funds, including:

- Texas Small Business Industrial Development Corporation;
- Texas Leverage Fund;
- Capital Access Program;
- Linked Deposit Program;
- Enterprise Zone Program;

- Industrial Revenue Bond Program;
- Defense Economic Readjustment Zone Program;
- Empowerment Zone and Enterprise Community Grant Program; and
- Renewal Community Program.

TDETO would administer the economic development bank fund, which would consist of general revenue appropriations, investment earnings, fees, and interest.

The bank would offer financial incentives to communities and businesses and would help communities obtain financing to fund local development efforts. The bank could provide tax incentives for expanding or relocating businesses. It could provide incentives to encourage lenders to make loans to near-bankable businesses and low-interest loans to qualifying businesses. It also could extend long-term bond-based debt financing for capital investment in public entities and in commercial and industrial development projects.

The bank would have to link businesses searching for investment with potential investors and would have to encourage institutional lenders to support regional economic development plans. It would provide communities with a source of financing for economic development efforts and technical assistance in their development of incentive programs. The bank also would have to serve as an information source for expanding or relocating businesses regarding financial incentives offered by the state. The bank could charge fees to beneficiaries of its services and could execute contracts and issue bonds for development projects.

Product development and small business incubators. CSSB 275 would create the Product Development and Small Business Incubator program with the authority to issue general obligation bonds. Program funds would be administered by the Economic Development Bank. The Product Development and Small Business Incubator Board would be appointed by the governor to govern the two funds. The board would comprise representatives from commercial technology development, higher education, technology industry finance, and low-income communities.

The product development fund would be a revolving fund in the state treasury, including fees, loan repayments, royalty receipts, dividend income,

appropriated general revenue, loan guarantees, and equity investments. The fund could be used to help finance the development, production, and commercialization of new or improved products in Texas. The small business incubator fund also would be a revolving fund in the treasury and would be funded similarly to the product development fund. It could be used to finance the development of small business in Texas.

The bank would have to give preference to areas of biotechnology and biomedicine with the highest potential for commercial success and for job creation and retention. The bank also would have to give preference to state and federal grantees, applicants with additional sources of funding, those receiving aid from small business development centers, and Texas residents. The bank would have to contract with the beneficiary to obtain an appropriate portion of royalties, patent rights, or equitable interests from products developed with state funds. The amount of financing to one recipient could not exceed 10 percent of the total amount of bonds issued. The board could appoint a biotechnology and biomedicine advisory committee to review projects and applications.

An application to the product development and incubator program would have to include a business plan detailing the applicant's financial history, market and market prospects, management integrity, and a statement on the feasibility and commercialization schedule of the proposed product. The bank would have to determine if the project was potentially successful and would benefit the state economy by creating jobs. The bank also would have to determine that financing for the project was not available in the private sector and that there was reasonable assurance that the state would recoup its investment. Information submitted to the bank by an applicant would be confidential.

Enterprise zones. CSSB 275 would alter the administration of the enterprise zone program and would transfer it to the Economic Development Bank. The bill would redefine an area eligible for enterprise zone designation as a block group, defined by the U.S. Census Bureau, in which at least 20 percent of residents have an income at or below 100 percent of the federal poverty level. An area designated by the federal government as a renewal community, empowerment zone, or enterprise zone also would be eligible. An area could retain its designation as an enterprise zone for as long as it qualified under these criteria.

The governing body of a municipality or county would serve as the nominating body for a project or business activity to be designated an enterprise project. A qualified business could request that a nominating body apply for designation of a project or activity as an enterprise project if the project involved an expansion or relocation from out of state. The business would have to specify a predetermined designation period with beginning and ending dates for the project. The designation period could not exceed five years, and any franchise or subsidiary would have to maintain separate books and records for activity at the site.

A business would be qualified for an enterprise project if the business had engaged in or committed to conducting business in an enterprise zone. At least 25 percent of the business's new employees would have to be residents of an enterprise zone or economically disadvantaged. A business that was not located in an enterprise zone could participate if at least 35 percent of its new employees were residents of an enterprise zone or were economically disadvantaged.

If a nominating body approved a request by a qualified business, that body would have to submit information on local incentives and other information to the Economic Development Bank before applying on behalf of the project. The governing body by ordinance or order would have to identify and summarize incentives available in the area in which the project was located. Other information would include a transcript of public meetings about local incentives and contact information for the nominating body's liaison.

After this information had been submitted, a nominating body could apply to the bank for designation of the qualified business as an enterprise project. The application would have to include an economic analysis, the number of anticipated new and retained permanent jobs during the designation period, the amount of investment by the project, and a schedule for the project's completion. The application also would have to include a description of local efforts to revitalize the jurisdiction over the project and an indication of the types of designation being sought by the project.

Designation of tax refund. The Economic Development Bank would have to allocate to an approved project the number of permanent jobs to be created or retained based on the amount of capital investment made by the business. This

designation would be used to determine the tax refund available to the project, with a refund assessed on each job created or retained, up to a maximum. The schedule for tax refunds would be determined by capital investment:

- \$40,000 to \$399,999 — a refund of \$2,500 per job, with a maximum refund of \$25,000;
- \$400,000 to \$999,000 — a refund of \$2,500 per job, with a maximum refund of \$312,500;
- \$1,000,000 to \$4,999,999 — a refund of \$2,500 per job, with a maximum refund of \$312,500;
- \$5,000,000 to \$149,999,999 — a refund of \$2,500 per job, with a maximum refund of \$1,250,000;
- \$150,000,000 to \$249,999,999 — a refund of \$5,000 per job, with a maximum refund of \$2,500,000;
- \$250,000,000 or more — a refund of \$7,500 per job, with a maximum refund of \$2,500,000.

A project with capital investment between \$150,000,000 and \$249,999,999 would be classified as a “double jumbo enterprise project” and could not receive a refund of more than \$500,000 in each fiscal year. An investment of more than \$250 million would be a “triple jumbo enterprise project” and could not receive a refund of more than \$750,000 in each fiscal year. Any other enterprise project could not receive a refund of more than \$250,000 in each fiscal year. The nominating body for a double or triple jumbo project would have to note that designation in its application to the bank. At the time of the receipt of any tax benefit from the enterprise zone program, 3 percent of the amount of the benefit would have to be transferred to the Economic Development Bank to help defer the program’s administrative costs.

The nominating body would have to audit the business to determine that it followed through on its commitments and goals. A business could obtain benefits on completion of an audit certifying hiring commitments and purchases made under the program. The business would have to submit a certified report about the number of jobs created or retained and the capital investment made or committed to the site before obtaining a state benefit.

CSSB 275 also would add standard sunset language governing conflicts of interest, standards of conflict, handling of public complaints, and training.

The bill would take effect September 1, 2003.

**SUPPORTERS
SAY:**

CSSB 275 would reorganize and streamline TDED, making it a more effective and efficient agency. The department has addressed many of the problematic issues that have plagued its operations since it was created. The bill would continue this progress by refocusing TDED's mission, redefining its relationship with other agencies involved in economic development, and building upon the successful programs it administers.

Transfer to the Governor's Office. CSSB 275 would strengthen economic development in the state by directly linking TDED to the Governor's Office. A centralized location would enable successful coordination of economic development activities across the many state agencies that play a role in the state's economic development. The Legislative Budget Board estimates that consolidating economic development into the Governor's Office would save the state more than \$1.5 million in general revenue annually.

The promise of the governor's assuming a prominent role in state economic development was demonstrated by the success in bringing the new Toyota manufacturing plant to San Antonio. As part of that effort, the governor played a key role in communicating with Toyota executives and in guiding TDED and other agencies. A strong focal point for economic development initiatives under the governor's purview would solidify the successful model employed to recruit Toyota.

Tourism promotion. CSSB 275 would refocus the TDED's mission to emphasize tourism promotion, which already makes up more than half of its budget. According to the Sunset Advisory Commission, while several state entities play a role in promoting tourism, no comprehensive plan exists to coordinate tourism efforts. The bill would require the new TEDTO to partner with the state agencies involved in tourism promotion to eliminate duplication and waste among the agencies and to develop a comprehensive plan for marketing the state to visitors. The bill would ensure efficient use of resources by requiring the office to set specific goals and performance measures to evaluate all tourism marketing efforts.

Aerospace and Aviation Office. CSSB 275 would coordinate state economic development activities further by consolidating the Aerospace Commission

into the new office. The bill would redirect the emphasis of state aerospace and aviation initiatives toward promoting and expanding these important industries.

Supporting industry clusters. The bill would engage TEDTO in identifying and promoting industry clusters across the state, strengthening the capacity of Texas industries to compete in the global marketplace. Economic development increasingly has focused on the importance of industry clusters, which can form the basis of strong local economies. To the extent that TEDTO could help businesses recognize the potential of these clusters, many Texas communities would witness substantial benefit.

Economic development bank. CSSB 275 would combine the current maze of debt financing programs into a centralized economic development bank to provide loans to qualified small and medium-sized businesses that cannot obtain financing from commercial sources. Through fees charged to loan beneficiaries, the bank eventually would become self-sufficient, removing the need for future appropriations to the fund. The fund would direct resources to high-tech sectors with the greatest potential for expansion and job creation. These provisions flow directly from a study commissioned by the department from economist Ray Perryman. The study strongly encouraged the creation of a comprehensive and centralized economic development bank to coordinate state incentive programs.

Enterprise zones. CSSB 275 would simplify and improve the enterprise zone program, which has achieved success in the past but has limited potential under the current structure. The bill would remove the application that now must be made for a community to be established as an enterprise zone and would streamline the other two applications, significantly reducing the burdensome administrative obstacles that discourage many communities and businesses from participating in the program. The bill would eliminate a double audit by the comptroller and would allow a review of jobs and expenditures to be evaluated concurrently. It would eliminate the arbitrary deadline of seven years for which a community may qualify for the program, allowing a community to be eligible until it could overcome its poverty problems. The bill also would create a schedule of refunds that would tie incentives directly to capital investment and job creation and would establish maximum refunds for each project.

OPPONENTS
SAY:

CSSB 275 essentially would relegate TDED to the minor role of promoting tourism and marketing Texas to other businesses. Other states have economic development strategies that are much more comprehensive than Texas' plan, including workforce development, labor management, industrial expansion, and permit assistance. Although they are important aspects of any economic development strategy, tourism and promotion represent a small level of state involvement in development activity. Texas can do better than the limited scope of activities planned for TDED under CSSB 275.

Transfer to the Governor's Office. CSSB 275 would give the governor too much authority over economic development for Texas. Although the governor played a key role in recruiting Toyota to San Antonio, the current structure has contributed to many of successes. The TDED board of directors serves an important purpose in representing diverse perspectives on economic development and in providing an objective forum for setting policy. An economic development office could flounder if a future governor did not show balanced or strong support of the issue.

Business incentives. CSSB 275 would not incorporate enough safeguards to ensure that business incentives issued by the Economic Development Bank would yield a return or generate new investment. Although the bill would make it easier for communities to take advantage of tax abatements and incentives, it would not ensure that incentives issued through the program would stimulate investment that would not have occurred otherwise. The requirement that only 25 to 35 percent of jobs created through incentives go to current residents would not be sufficient, as outsiders who took these jobs would use municipal and state services while the taxing entities would have to forgo tax revenue in the name of business growth. The bill should require TDED to address difficult issues related to business incentives to ensure that citizens receive the maximum benefit from these funds.

OTHER
OPPONENTS
SAY:

TDED should be abolished. Economic development is primarily a local activity, and CSSB 275 would place the state in the problematic position of awarding grants from funds collected statewide to specific local communities. State tourism functions can and should be handled by the private sector. The most effective method for attracting business and increasing productivity is to ensure that the state has strong schools, adequate transportation, a healthy environment, and necessary social services. Until those needs are met, an

independent economic development office is a luxury that the state cannot afford.

NOTES:

The Senate engrossed version of SB 275 would have renamed the new office the Texas Economic Development Office. It would not have created an economic development bank or fund, nor would it have included a small business advocate in the office. The bill also would not have changed the state enterprise zone program.

The House companion bill, HB 1233 by Solomons, et al., was reported favorably, as substituted, by the Economic Development Committee on April 23.

TDED came up for sunset review during the 77th Legislature in 2001. The sunset bill, HB 3452 by Gallego, et al., would have continued TDED for a two-year probationary period, transferred various TDED programs to the secretary of state and the comptroller, and created a Texas Tourism Coordinating Council. HB 3452 died when the House-Senate conference committee could not reconcile differences between the two versions of the bill. The Legislature continued TDED until September 1, 2003, by enacting SB 309 by Harris, but that legislation did not alter the expiration date for TDED's Smart Jobs program, which expired December 31, 2001.