

**SUBJECT:** Broadening eligibility for and tax benefits of defense readjustment zones

**COMMITTEE:** International Relations and Economic Development — committee substitute recommended

**VOTE:** 9 ayes — Anchia, Frullo, Blanco, Cain, Larson, Metcalf, Perez, Raney, Romero

0 nays

**WITNESSES:** For — Juan Antonio Flores, Port San Antonio; Jim Brennan, Texas Coalition of Veterans Organizations; (*Registered, but did not testify:* TJ Patterson, City of Fort Worth; Christine Wright, City of San Antonio; Claudia Russell, El Paso County; Scott Norton, TexAmericas Center; James Hines, Texas Association of Business; Mike Meroney, Texas Association of Manufacturers; Shanna Igo, Texas Municipal League)

Against — None

On — Michael Treyger, Office of the Governor

**BACKGROUND:** Government Code ch. 2310 allows for the creation of defense economic readjustment zones (DERZ) in areas where a U.S. military base has been closed or downsized. A municipality or county affected by the closure or downsizing, individually or in combination with other municipalities or counties also affected, must nominate an area to become a readjustment zone. These zones must be between one and 20 square miles in size, and half of zone must be within the current or former base area. Designated zones may remain in the program for up to seven years.

Within a DERZ, a business may be designated as a defense readjustment project, provided that it hires a certain number of residents of the zone, dislocated defense workers, or economically disadvantaged individuals, and meets other criteria as specified in statute. Designation as a defense readjustment project confers certain tax benefits, including franchise tax credits and refunds on state sales tax paid for electricity usage, certain

materials, and equipment or machinery purchased for construction.

The DERZ program is administered by the Texas Economic Development Bank in the Governor's Office of Economic Development and Tourism. Individual DERZs are administered by the governing body of the municipality or county that applied to create them or jointly by a county and municipality that applied together.

There are no active zone designations and currently no active projects within the DERZ program, according to the 2018 annual report produced by the Economic Development and Tourism Division of the Governor's Office. Six zones and five projects have been approved since the program was created in 1997.

It has been suggested that the DERZ program is significantly underutilized and could be modified to increase participation and boost investment and economic growth in and around military installations.

DIGEST:

CSHB 390 would broaden the eligibility criteria for defense economic readjustment zones (DERZ), adjust DERZ-associated tax benefits, change the period of designation of a DERZ from a maximum of seven years to an indefinite period of time, and raise the limit on permitted defense readjustment zones.

The bill would eliminate the requirement for a county or municipality to nominate an area as a DERZ and apply to the Texas Economic Development Bank for acceptance as such. Instead, the entire territory of a municipality or county would automatically qualify as a DERZ if it encompassed any part of a federal military installation, facility, or mission that was functioning on May 19, 1997. Certain eligibility criteria in current statute relating to base closures or realignments would be eliminated.

The bill also would broaden eligibility for businesses to qualify as DERZ projects. Businesses could count hired veterans toward the 25 percent minimum threshold for job creation, in addition to dislocated defense

workers, residents of the zone, and economically disadvantaged individuals.

DERZ projects would no longer be limited to two per readjustment zone. Instead, six projects could be designated per biennium in cities or counties with fewer than 250,000 people, and nine projects could be designated in cities or counties with populations of 250,000 or more.

**Double and triple jumbo projects.** Businesses qualifying as defense readjustment projects would be designated "double jumbo" projects if they involved capital investment commitments of \$150 million to \$249.9 million or "triple jumbo" projects if they involved commitments of \$250 million or more. These designations would entitle businesses to enhanced tax benefits per job created or retained.

**Tax refunds.** CSHB 390 would expand the sales tax benefits of a DERZ project to include tax refunds for all taxable items purchased for use at a qualified business site related to the project or activity.

The Texas Economic Development Bank would be required to calculate tax refunds for readjustment projects based on several factors, including:

- the capital investment in a project;
- the number of new permanent jobs or retained jobs; and
- a project's double jumbo or triple jumbo designation level.

Tax refunds per job created or retained would range from \$2,500 to \$7,500, up to certain limits. In the case of double jumbo and triple jumbo projects, refunds would be counted only for new permanent jobs, not for retained jobs.

The bill would set a maximum refund that could be applied per fiscal year of \$250,000 for a standard DERZ project, \$500,000 for a double jumbo project, and \$750,000 for a triple jumbo project. If a business had earned a credit larger than the limit in a given year, it could apply the remainder of the credit in subsequent tax years, subject to the applicable limit for each

year.

**Other provisions.** The bill also would:

- eliminate a required annual report on the DERZ program and instead include certain information on the program into the Texas Economic Development Bank's annual report;
- require a DERZ administered by a county and city jointly to be governed under the terms of an interlocal agreement;
- add certain application requirements for a qualified business applying to the Texas Economic Development Bank for designation as a DERZ project; and
- allow a municipality or city to refund local sales and use tax paid by a DERZ project on all taxable items purchased.

The bill would take effect September 1, 2019.

**NOTES:**

According to the Legislative Budget Board, the bill would have an estimated negative impact of \$24.4 million on general revenue related funds through fiscal 2020-21, and a \$102 million negative impact on general revenue related funds for fiscal 2022-23.