VIRGINIA ECONOMIC (INDUSTRIAL) DEVELOPMENT AUTHORITIES:
Brief Overview of Purposes and Powers

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BRIEF OVERVIEW OF PURPOSES AND POWERS

I. CERTAIN FUNDAMENTAL LEGAL CONCEPTS

A. Dillon's Rule

1. Virginia follows Dillon's Rule in limiting the powers that may be exercised by its counties, cities, towns and other governmental entities.

2. Dillon's Rule provides that all powers of local governmental entities are granted by the state constitution or legislature and can be of only three types:

> "**First**, those granted in express words; **second**, those necessarily or fairly implied or incident to the powers expressly granted; **third**, those essential to the accomplishment of the declared objects and purposes of the corporation - not simply convenient, but indispensable. Any fair, reasonable, substantial doubt concerning the existence of power is resolved by the courts against the [municipal] corporation . . ."[1]

3. Dillon's Rule is in contrast to the concept of home rule. In home rule states local governmental entities may exercise a broad range of powers within limits prescribed by the state constitution or by statute.

4. In Virginia, one must therefore look for a grant of power in clear terms rather than be concerned with whether a provision of the Constitution of Virginia (the "Constitution") or the Code of Virginia of 1950, as amended (the "Virginia Code"), specifically denies the power.

B. Virginia Constitution - Credit Clause and Public Purpose Clause

1. The Credit Clause and the Public Purpose Clause have become increasingly important as the use of public monies for economic development has become more prevalent.

2. Credit Clause - Article X, Section 10 of the Virginia Constitution provides that neither the credit of the Commonwealth nor of any of its political subdivisions shall be "directly or indirectly, under any device or pretense whatsoever, granted to or in aid of any person, association or corporation." This provision was inserted to prevent the use of the Commonwealth's funds and credit to foster and encourage construction and

[1] John F. Dillon, Law of Municipal Corporations (2d. ed. N.Y. 1873) (emphasis added); see County Board of Arlington County v. Brown 229 Va. 341, 344 (1985).

operation of private enterprises.[2] While the Virginia Supreme Court seems to have relaxed its position in a 1984 case decided by a 4-3 majority,[3] the Credit Clause is still alive.

3. Public Purpose Clause - Article X, Section 8 of the Virginia Constitution has been interpreted to require that public money be devoted to a public purpose.[4] This requirement does not prohibit all benefit to a private party. The test developed by the Virginia Supreme Court over the years is whether the dominant purpose is to benefit the Commonwealth, or one of its political subdivisions, consistent with the legislative purposes of enabling legislation or implementing actions. If so, incidental benefit to private parties, even though such benefits may be significant, is not prohibited.[5]

II. INDUSTRIAL DEVELOPMENT AND REVENUE BOND ACT (THE "ACT")[6]

A. Purposes

The Act sets forth the specific purposes for which economic (industrial) development authorities ("EDAs") were created.[7]

1. **Business Development.** Acquire, own, lease, and dispose of properties and make loans to promote industry and develop trade by inducing manufacturing, industrial, governmental, nonprofit and commercial enterprises and institutions of higher education to locate in or remain in this Commonwealth, which powers shall be exercised for the benefit of Virginians, either through the increase of their commerce, or through the promotion of their safety, health, welfare, convenience or prosperity.

2. **Pollution Control.** Protect and promote the health of Virginians and the conservation, protection and improvement of its natural resources by exercising powers of the Act for the control or abatement of land, sewer, water, air, noise and general environmental pollution derived from the operation of any industrial or medical facility.

3. **Medical Facilities and Senior Living Facilities.** Protect and promote the health and welfare of Virginians by assisting in the acquisition, construction, equipping, expansion, enlargement and improvement of medical facilities and facilities for the residence or care of the aged in order to provide modern and efficient medical services and care of the aged and in order to reduce the costs to residents utilizing such facilities.

4. **Facilities for Non-Profits.** Protect or promote the safety, health, welfare, convenience, and prosperity of Virginians by assisting in the acquisition, construction,

[2] Almond v. Day, 197 Va. 782 (1956).
[3] Dehaan v. City of Charlottesville, 228 Va. 578 (1984).
[4] Infants v. Virginia Hous. Dev. Auth., 221 Va. 659 (1980).
[5] Almond v. Day, 197 Va. 782 (1956).
[6] Va. Code § 15.2-4900 et seq. (See Appendix A)
[7] Va. Code § 15.2-4901.

equipping, expansion, enlargement, improvement, financing, and refinancing of facilities for use by not-for-profit 501(c)(3) organizations (other than institutions organized and operated exclusively for religious or educational purposes) in order to provide operations, recreational, activity centers, and other facilities.

5. **Private Higher Education Facilities.** Protect and promote the health and welfare of Virginians by assisting in the acquisition, construction, equipping, expansion, enlargement, and improvement of facilities of private, accredited and nonprofit institutions of higher education in the Commonwealth whose primary purpose is to provide collegiate or graduate education and not to provide religious training or theological education.

6. **Governmental Facilities.** Utilize the powers contained in the Act with respect to facilities for a locality, the Commonwealth and its agencies, and governmental and nonprofit organizations.

7. **Museums.** Utilize the power contained in the Act with respect to facilities for museums and historical education, demonstration and interpretation, for use by nonprofit organizations in order to promote tourism and economic development.

8. **Equine Facilities (other than racing).** Utilize the power contained in the Act with respect to facilities devoted to the staging of equine events and activities (other than racing) for use by governmental or nonprofit, nonreligious organizations and operated by such governmental or nonprofit, nonreligious organizations in order to promote the equine industry and equine-related activities (other than racing).

9. **Industrial Parks.** Utilize the power contained in the Act with respect to acquiring, developing, owning and operating an industrial park and any utilities that are intended primarily to serve the park and to issue bonds, secured by revenues of the park, for such purposes.

10. **Housing.** Utilize the power contained in the Act, when no housing authority has been activated in the locality, with respect to facilities used primarily for single or multi-family residences in order to promote safe and affordable housing.

11. **Grants for Affordable Housing**. Utilize the power contained in the Act to make grants associated with the construction of affordable housing.

12. **Public Schools.** Utilize the power contained in the Act with respect to public school buildings and facilities.

13. **Carbon Markets**. Utilize the power contained in the Act with respect to facilitating and supporting landowner access to carbon markets through aggregation of landowners to reach a size that attracts investment of private capital.

B. Powers

The following powers are enumerated in the Act:[8]

1. To enter into contracts;

2. To acquire, whether by purchase, exchange, gift, lease or otherwise, and to improve, maintain, equip and furnish one or more authority facilities;

3. To lease to others any or all of its facilities and to charge and collect rent therefor and to terminate any such lease upon the failure of the lessee to comply with any of the obligations thereof; and to include in any such lease, if desired, a provision that the lessee thereof shall have options to renew such lease or to purchase any or all of the leased facilities, or that upon payment of all of the indebtedness of the EDA it may lease or convey any or all of its facilities to the lessee thereof with or without consideration;

4. To sell, exchange, donate, and convey any or all of its facilities or properties;

5. To issue its bonds for the purpose of carrying out any of its powers (all bonds issued by the EDA shall be payable solely from the revenues and receipts derived from the leasing or sale of authority facilities or from payments received by the EDA in connection with its loans[9]);

6. To mortgage and pledge, as security for the payment of the principal of and interest on any bonds so issued and any agreements made in connection therewith, any or all of its facilities or any part or parts thereof, whether then owned or thereafter acquired, and to pledge the revenues therefrom or from any part thereof or from any loans made by the EDA;

7. To borrow money and to accept contributions, grants and other financial assistance from the United States of America and agencies or instrumentalities thereof, the Commonwealth, or any political subdivision, agency, or public instrumentality of the Commonwealth, for or in aid of the construction, acquisition, ownership, maintenance or repair of the authority facilities, for the payment of principal of any bond of the EDA, interest thereon, or other cost incident thereto, or in order to make loans in furtherance of the purposes of the Act; and

8. To make loans or grants to any person, partnership, association, corporation, business, or governmental entity in furtherance of the purposes of the Act including for the purposes of promoting economic development, and to forgive loans or other obligations if it is deemed to further economic development.

[8] Va. Code § 15.2-4905.
[9] Va. Code § 15.2-4908.

C. The EDA and Economic Development

1. **Loans and Grants of Public Funds to Aid Private Business**

(a) The Credit Clause limits the ability of local governments to lend money or make grants to a private company. The Virginia Attorney General has found that there is no statute expressly or implicitly authorizing localities to make direct loans to private companies.[10]

(b) A locality may, however, may make gifts, donations and appropriations of money to the EDA for the purposes of promoting economic development.[11]

(c) A county may give, lend or advance funds or other county property to any authority created by it.[12]

2. **Subsidizing the Cost of Land for Economic Development**

(a) Subject to applicable requirements of the Virginia Constitution, a locality may acquire land by gift or purchase and subsequently sell the land to a private business to promote economic development provided a public hearing has been held.[13]

(b) A locality may acquire by gift, purchase, etc., pursuant to Va. Code § 15.2-1800, but not by condemnation, a facility site, and transfer such facility site to the EDA by sale, lease or gift, without regard to any other restrictions or limitations regarding acquisition or disposition or real property by localities. Such facility site may be located within or without the locality creating the EDA.[14]

3. **Limitations on the EDA**

(a) The EDA does not have power to operate any facility as a business, other than as a lessor, and does not have the power to operate any single or multi-family housing facilities.

(b) However, the EDA does have the power to establish, operate and maintain foreign-trade zones.

(c) The EDA does not have the power of eminent domain.

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[10] 1983-84 Report of Atty. Gen., 103.
[11] Va. Code § 15.2-953.
[12] Va. Code § 15.2-1205.
[13] Va. Code § 15.2-1800.
[14] Va. Code § 15.2-4917.

(d) The EDA does not have the express power to form corporations, partnerships, joint ventures, trusts or other legal entities.

4. **Economic Incentive Programs**

In order to have the greatest chance of withstanding constitutional scrutiny, the "animating purpose" of any use of financial incentives must be a public purpose. Whether a structured incentive program is adopted or incentives are provided on a case-by-case basis, the EDA will need to demonstrate several things.

(a) The EDA should demonstrate that it has made a legislative determination that the use of incentives will serve a public purpose.

(1) Some form of legislative declaration and/or study conducted by or on behalf of the EDA setting forth the rationale for using incentives and the benefits that are expected to accrue to the localities forming the EDA as a result of providing such incentives is likely to be given significant weight by a court considering the legality of the incentives.

(2) Any such declaration or study should make clear that the use of incentives is primarily for the benefit of the locality and is directly related to the locality's interest in increasing the tax base, creating employment opportunities for its citizens, diversifying the mix of industry located in the locality or whatever other public purpose is to be served by the provision of incentives and is only incidentally beneficial to the companies receiving the incentives.

(b) It is better for an economic incentive program to be fairly broadly available rather than targeted at attracting a single or very small number of select companies.

(1) The more widely available the incentives, the more likely they are to be perceived as serving, and actually will serve, a public purpose.

(2) Incentives should not, however, be offered to any and every company seeking to locate or expand in the locality. The EDA should develop a goal for its economic development efforts (e.g., creating employment with high income opportunities and attracting industries that will serve as a catalyst for further economic development) and should target the use of financial incentives to attaining that goal.

(3) To the extent specific industries do not comport closely with the EDA's economic development goals, financial incentives should be used sparingly if at all.

(c) The EDA should develop and apply clear and quantifiable standards for awarding financial incentives.

(1) The use of standards based on jobs created, wages paid and investment made by the companies receiving the incentives and the inclusion of a "payback period" or similar mechanism help demonstrate that the EDA is not seeking to benefit a particular party, but instead, is fostering the economic growth of the locality.

(2) Requiring companies that do not meet the obligations imposed by the EDA for the provision of incentives to repay the value of the incentives (or a portion thereof) would further demonstrate that the use of incentives served a public purpose.

5. **<u>Examples of Economic Incentives</u>**

(a) ***Infrastructure Improvements.*** Localities often are asked to provide a variety of infrastructure improvements as an incentive for a private business to locate in a particular jurisdiction. These improvements often take the form of roadways and the extension of water and sewer lines to and upon the property sought to be providing such improvements up to the property to be developed. Generally, any such improvements would lie solely on public property with the locality retaining ownership of the improvements. Providing improvements on privately-owned property is a somewhat closer call as the locality presumably will retain no interest in the property. However, like a current grant of property or funds, providing such improvements is likely permissible if the requisite public purpose is demonstrated and the provision of such improvements complies with the locality's adopted economic program. The viability of providing such improvements could be further enhanced if the improvements were made to public property acquired for economic development purposes prior to such property being conveyed to the private, for-profit company.

(b) ***Construction and Lease of Facilities.*** Some localities have been approached about constructing manufacturing and/or office facilities and leasing those facilities to private, for-profit companies. If structured as a traditional conduit financing through the EDA, the Virginia Supreme Court has expressly upheld the constitutionality of such a transaction.[15]

(c) ***Loans and Forgiveness of Indebtedness.*** The Act expressly empowers the EDA to make loans or grants to companies and other entities for the purpose of promoting economic development and to forgive loans or other obligations if such action is deemed to further economic development. The EDA could, therefore, make loans to private, for-profit companies for the purpose of

[15] Industrial Dev. Auth. v. Suthers, 208 Va. 51 (1967).

promoting economic development and, as an incentive to invest in the locality forgive a portion of the loan. For example, the EDA could forgive the interest component of the loan and/or a portion of the principal component for so long as the recipient complies with the obligations entered into in connection with the making of the loan (e.g., during each year that the recipient makes capital investments in the localities equal to or greater than $X, the EDA will forgive $Y dollars of that year's interest on the loan). Funding for the loans could come from the general revenues of the EDA, if any, or from current appropriations from the localities for such purposes.

(d) ***Commonwealth Development Opportunity Fund.*** Established to aid local governments and other political subdivisions in attracting economic development prospects or securing the expansion of existing industry. There are certain minimum investment and job creation criteria. The program offers a cash grant to offset or reimburse qualifying project-related costs, such as site acquisition and development, transportation access, utility extension or capacity development, construction or build-out of buildings or training. The Fund also requires the local government to provide a matching grant and the company to enter into a performance agreement.

D. Issuance of Bonds

1. **<u>General</u>**

(a) The EDA may issue bonds for any of its purposes.

(b) The EDA may issue bonds payable (i) from its revenues and receipts generally; (ii) exclusively from the revenues and receipts of a particular facility or loan; or (iii) exclusively from the revenues and receipts of certain designated facilities or loans whether or not they are financed in whole or in part from the proceeds of such bonds.

(c) Bonds, however, may be payable no later than 40 years from the date of issuance.

2. **<u>Process of Issuing Bonds</u>**

(a) ***Public Hearing.*** If a public hearing is required under federal law for purposes of a federal tax-exemption, the Act requires the EDA to conduct a public hearing in order to obtain federal tax exemption.

(b) ***Inducement Resolution.*** The EDA must generally adopt an inducement resolution including the initial approval of the project, a determination of the public purpose of the project, and a recommendation that the governing body of the locality approve the issuance of the bonds.

3. **Types of Bond Financings**

(a) ***General.*** Typically, financing structures that an EDA will be asked to approve are 1) a fixed rate financing and 2) a variable rate financing.

(b) ***Purchasers of Bonds.*** Bonds may be sold to various purchasers, including a single investor, a group of sophisticated investors, or the general retail public.

(c) ***Security for Bonds.*** Depending on whether the Bonds are fixed or variable rate, they are typically secured by the revenues pledged by the conduit borrower. The conduit borrower pledges the revenues of either the project being financed or of the borrower generally. The bonds may also have credit enhancement in the form of a letter of credit or bond insurance.

4. **Certain Other Qualifying Costs**

In the case of federally tax-exempt bonds, federal and state law generally permit the use of bond proceeds to:

(a) pay issuance expenses for the bonds, but not in excess of two percent of the principal amount of the bonds,

(b) pay interest on the bonds for the period of construction or renovation and for an additional period thereafter, and

(c) fund a reasonable reserve fund not exceeding either 10% of the bonds or one year's debt service.

(1) A reserve fund provides additional security to bondholders for payment of debt service.

(2) The reserve fund may normally be drawn upon if the borrower misses an interest or principal payment.

(3) Because of the rebate requirement, a reserve fund does not produce any direct financial benefit for the borrower, but it may be necessary or desirable in order to obtain credit enhancement or attractive or desirable in order to obtain credit enhancement or attractive interest rates.

(4) A reserve fund will usually continue to exist as long as the bonds are outstanding, but its continued existence does not hinder the use of the six-month expenditure or the twenty-four month construction expenditure rebate exceptions.

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