S T A T E O F T E N N E S S E E
OFFICE OF THE
ATTORNEY GENERAL
PO BOX 20207
NASHVILLE, TENNESSEE 37202

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Opinion No. 09-180

Use of Sales and Use Tax Revenue to Pay the Cost of Qualified Public Use Facilities

QUESTIONS

1. Are any monies diverted away from a public school system when a tourism development zone ("TDZ") is formed?

2. Can any monies from the new revenue stream generated within the TDZ go to a public school system or do all new monies have to go pay the debt of a public use facility and any qualified associated developments?

3. Is a municipal government which has a qualified TDZ and is funding the necessary public use facility and qualified associated development as prescribed by Tenn. Code Ann. §§ 7-88-101 *et seq*. entitled to receive and retain all sales tax received in the TDZ under the formula prescribed in Tenn. Code Ann. § 7-88-106, when a portion of the sales tax collected results from a subsequent local sales tax increase authorized by a countywide sales tax increase referendum which designated the tax increase for local schools?

OPINIONS

1. The increased revenue a TDZ municipality receives must be used to pay the cost of the qualified public use facility. That revenue would have gone to the public school system if the TDZ did not exist and there was no facility to pay off. On the other hand, that the increased revenue goes to pay the facility's cost does not necessarily mean it has been diverted away from the public school system because this revenue is deemed to be the result of economic activity that would not have occurred had the facility not been built.

2. The increased revenue cannot go to a public school system. The increased revenue must be used to pay the cost of the qualified public use facility, which includes qualified associated development. The cost of the facility would include public schools that constitute qualified associated development, but it is unlikely that an entire public school system could be considered such development.

3. With regard to a public facility, a municipality is entitled to the increased revenue, including revenues generated from a local sales and use tax increase, regardless of whether such an increase has been designated for local schools. With regard to a privately owned or operated amusement park or tourism attraction, a municipality may by resolution except the local sales and use tax increase from the increased revenue that is apportioned for payment of the cost of such facilities. Also, with regard to a privately owned or operated facility, one-half of any local

sales and use tax rate increase could not be lawfully apportioned to the municipality for payment of that facility, regardless of whether a local referendum designated the increase for local schools.

ANALYSIS

1. Generally, municipalities receive a percentage of the state sales and use taxes collected throughout the state. Tenn. Code Ann. § 67-6-103(a)(3)(A) (Supp. 2009). The amount allocated to a municipality is based on the population of that municipality in comparison to all other municipalities in Tennessee. *Id*. With regard to local sales and use tax, one-half of the collected revenue is "distributed in the same manner as the county property tax for school purposes is expended and distributed." Tenn. Code Ann. § 67-6-712(a)(1) (Supp. 2009). As for the other half, the revenue collected in the unincorporated areas of the county is distributed to the county and the revenue collected in the incorporated areas is distributed to those areas, or as otherwise agreed to by the county and the incorporated areas. Tenn. Code Ann. § 67-6-712(a)(2) (Supp. 2009). Except for revenue relating to a 1992 tax increase for kindergarten through grade twelve education, state and local sales and use tax revenue "shall be earmarked and allocated in accordance with" the Convention Center and Tourism Development Financing Act of 1998 (the "Act"). Tenn. Code Ann. §§ 7-88-101 *et seq*. (2005 and Supp. 2009), 67-6-103(c)(2) and (e) (Supp. 2009), and 67-6-712(d) (Supp. 2009).

For the purpose of "increas[ing] state tourism and related economic development," the Act "provid[es] a financing mechanism for the development of convention centers and other similar public use facilities" in municipalities throughout Tennessee. Tenn. Code Ann. § 7-88-102 (2005). Pursuant to the Act, a portion of the state and local sales and use tax revenue distributed to a municipality that has "financed, constructed, leased, equipped, renovated or acquired a qualified public use facility within a tourism development zone" shall be used "for payment of the cost of the public use facility, including interest and debt service on any indebtedness related to the public use facility, or the lease payments with respect to any public use facility." Tenn. Code Ann. §§ 7-88-106(a) and (b) and -108 (Supp. 2009). The definition of "qualified public use facility" includes public convention centers and associated ancillary structures or facilities, Tenn. Code Ann. § 7-88-103(7)(A)(i) and (iv) (Supp. 2009), and privately owned or operated amusement parks or tourism attractions, Tenn. Code Ann. § 7-88-103(7)(A)(ii) and (iii) (Supp. 2009), all of which must have a minimum amount of investment. The Act's definition of "qualified public use facility" also includes "qualified associated development," which is defined as follows:

> "Qualified associated development" means parks, plazas, recreational facilities, ***schools***, sidewalks, access ways, roads, drives, bridges, ramps, landscaping, signage and other public improvements ***constructed or renovated by the municipality*** or the public building authority ***in connection with the public use facility and related infrastructure and utility improvements for public or private peripheral development included in a master development plan for the tourism development zone and that is constructed, renovated or installed by the municipality*** or the public authority. The total costs of the qualified associated development shall not exceed thirty percent (30%) of the costs of the entire qualified

> public use facility. ***Qualified associated development***, except for public utility improvements, including water, sewer, electricity, or gas, associated with the qualified public use facility, ***shall be located within one and one half (1 ½) miles of the qualified public use facility and shall be considered qualified associated development if leased by a municipality or a public building authority***.

Tenn. Code Ann. § 7-88-103(6) and (7)(B) (Supp. 2009) (emphasis added).

The Act provides a formula for determining the amount of revenue that goes toward the cost of the facility. That amount is "equal to the incremental increase in state and local sales and use tax revenue derived from the sale of goods, products and services within the tourism development zone in excess of base tax revenues, excluding any increase in the state rate for sales and use tax." Tenn. Code Ann. § 7-88-106(a) (Supp. 2009). "Base tax revenues" are defined as

> the revenues generated from the collection of state and local sales and use taxes from all businesses within the applicable tourism development zone as of the end of the fiscal year of the state of Tennessee immediately prior to the year in which the municipality or public authority is entitled to receive an allocation of tax revenue pursuant to this chapter, adjusted annually after the first year by a percentage equal to the percentage of change in the collection of state and local sales and use taxes derived from the sale of goods, products and services for the entire county in which the public use facility is located for the preceding fiscal year.

Tenn. Code Ann. § 7-88-103(1) (Supp. 2009). Furthermore, with regard to privately owned or operated amusement parks or tourism attractions, this increased revenue does not include certain local sales and use tax revenue.

> [W]ith respect to any facility that elects to qualify as a qualified public use facility under § 7-88-103(7)(A)(ii) or (7)(A)(iii), ***only the portion of the incremental increase in the local sales and use tax revenue as is designated by resolution of the municipality shall be so apportioned and distributed under this section***, unless the municipality designates by resolution a lesser time period for the apportionment and distribution of the revenues; and in the event one (1) or more other local taxes are authorized for use within the tourist development zone, then the portion of the additional taxes as are designated by resolution of the municipality shall be similarly apportioned and distributed. For any facility that elects to qualify as a qualified public use facility under § 7-88-103(7)(A)(ii) or (7)(A)(iii), ***the portion of the incremental increase in the local sales and use tax revenue that is statutorily designated for local schools may not be apportioned and distributed for such a qualified public use facility***.

Tenn. Code Ann. § 7-88-106(a) (Supp. 2009) (emphasis added). The Act further specifies the time period for this increased revenue to go toward the cost of the facility.

> Apportionment and distribution of such taxes shall continue, until the earlier of:
>
> (1) The date on which the cumulative amount apportioned and distributed to the municipality equals the cost of the qualified public use facility, plus any interest on indebtedness of the municipality or public authority related to such cost;
>
> (2) The date on which the qualified public use facility ceases to be a qualified public use facility; or
>
> (3) Thirty (30) years from the date it is reasonably anticipated that the facility will commence operations as a public use facility.

Tenn. Code Ann. § 7-88-106(a) (Supp. 2009). A different time period governs the application of the increased revenue to the cost of a facility that is in a secondary tourism development zone. Tenn. Code Ann. § 7-88-106(c) (Supp. 2009).

Accordingly, a non-TDZ municipality may use its allocation of state and local sales and use tax revenue for its public school system and other purposes, while a TDZ municipality must use the increased revenue for paying off the cost of the facility. That revenue would have gone to the public school system if the TDZ did not exist and there was no facility to pay off. Although the cost of the facility would include public schools that constitute "qualified associated development," it is unlikely that an entire public school system could be considered such associated development based on the one-and-a-half mile geographic limitation alone. Tenn. Code Ann. § 7-88-103(6) (Supp. 2009). Furthermore, with regard to privately owned and operated amusement parks and tourism attractions, a municipality may designate that other local tax revenue be apportioned and distributed in the same manner as the increased revenue. Tenn. Code Ann. § 7-88-106(a) (Supp. 2009). Thus, one could argue that the increased revenue has been diverted away from the public school system. On the other hand, that the increased revenue goes to pay the facility's cost does not necessarily mean it has been diverted away from the public school system. Because this revenue is based on the difference between the taxes collected within the TDZ before and after the facility is constructed, financed, or acquired, the increased revenue is deemed to be the result of economic activity related to the facility and the TDZ. In other words, the theory is that without the facility, there would not be any increased revenue to "divert away" from the public school system.

With regard to privately owned or operated amusement parks or tourism attractions, it is more difficult to argue that revenue has been diverted away from a public school system because local sales and use tax revenue designated for local schools pursuant to Tenn. Code Ann. § 67-6-712(a)(1) (Supp. 2009) "may not be apportioned and distributed for such a qualified public use facility." Tenn. Code Ann. § 7-88-106(a) (Supp. 2009). Also, with regard to such amusement parks and attractions, a municipality may limit the amount of local sales and use tax revenue that can go toward the facility's cost. *Id*.

2. Pursuant to Tenn. Code Ann. § 7-88-106(b) (Supp. 2009), the increased revenue "shall be for the exclusive use of the municipality . . . for payment of the cost of the public use facility, including interest and debt service on any indebtedness related to the public use facility, or the lease payments with respect to any public use facility." The increased revenue also may be used to pay the cost of a facility within a "secondary tourism development zone." Tenn. Code Ann. § 7-88-106(c) (Supp. 2009).

As stated in response to the first question, the cost of the facility would include public schools that constitute "qualified associated development," but it is unlikely that an entire public school system could be considered such associated development based on the one-and-a-half mile geographic limitation alone. Accordingly, the increased revenue cannot go to a public school system. It must be used to pay the cost of the qualified public use facility.

Also, as stated in response to the first question, there is a time period for using the increased revenue to pay the cost of the facility. Tenn. Code Ann. § 7-88-106(a) and (c) (Supp. 2009). Once this period has terminated, state and local sales and use tax revenue would be apportioned and distributed to a municipality for use in the same manner as a non-TDZ municipality.

3. The Act provides a formula for determining the amount of revenue that goes toward the cost of the facility. Pursuant to Tenn. Code Ann. § 7-88-106(a) (Supp. 2009), that amount is

> equal to the incremental increase in state and local sales and use tax revenue derived from the sale of goods, products and services within the tourism development zone in excess of base tax revenues, ***excluding any increase in the state rate for sales and use tax***.

(emphasis added). With regard to a publicly-owned facility described in Tenn. Code Ann. § 7-88-103(7)(A)(i) and (iv) (Supp. 2009), there is no such exception for a local sales and use tax increase, regardless of whether such an increase has been designated for local schools. With regard to a privately owned or operated amusement park or tourism attraction, a municipality may limit the amount of the local sales and use tax increase that can be used to pay the cost of such a facility. Pursuant to Tenn. Code Ann. § 7-88-106(a) (Supp. 2009),

> with respect to any facility that elects to qualify as a qualified public use facility under § 7-88-103(7)(A)(ii) or (7)(A)(iii), ***only the portion of the incremental increase in the local sales and use tax revenue as is designated by resolution of the municipality shall be so apportioned and distributed under this section***, unless the municipality designates by resolution a lesser time period for the apportionment and distribution of the revenues.

(emphasis added).

Finally, with regard to a privately owned or operated facility, one-half of any local sales and use tax rate increase could not be lawfully apportioned to the municipality for payment of that facility, regardless of whether a local referendum designated the increase for local schools.

> For any facility that elects to qualify as a qualified public use facility under § 7-88-103(7)(A)(ii) or (7)(A)(iii), the portion of the incremental increase in the ***local sales and use tax revenue that is statutorily designated for local schools may not be apportioned*** and distributed for such a qualified public use facility.

Tenn. Code Ann. § 7-88-106(a) (Supp. 2009) (emphasis added). As noted in response to the first requested opinion, with regard to local sales and use tax, one-half of the collected revenue is "statutorily designated for local schools" pursuant to Tenn. Code Ann. § 67-6-712(a)(1) (Supp. 2009).

ROBERT E. COOPER, JR.
Attorney General and Reporter

MICHAEL E. MOORE
Solicitor General

NICHOLAS G. BARCA
Assistant Attorney General

Requested by:

The Honorable Ben West, Jr.
State Representative
108 War Memorial Building
Nashville, Tennessee 37243-0160