



An Audit Report on

# **Selected Major Agreements Under the Texas Economic Development Act**

August 2020  
Report No. 20-038



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## Overall Conclusion

Under the Texas Economic Development Act (Texas Tax Code, Chapter 313), independent school districts (ISDs) have entered into agreements with businesses for limitations on the appraised values for property (agreements), and those agreements have enabled capital investments and job creation benefiting the local and state economies.

The State Auditor's Office selected and audited agreements at three ISDs. For those three selected agreements, auditors reviewed the corresponding applications and the agreements to ensure that they complied with applicable Texas Tax Code, Chapter 313, requirements and requirements of the Office of the Comptroller of Public Accounts (Comptroller's Office). In addition, auditors reviewed the ISDs' processes for:

- Approving the applications.
- Forming and executing the agreements.
- Disclosing conflicts of interest.
- Calculating and receiving payments under the agreements.
- Monitoring and reporting on compliance with the agreements.

For the agreements audited at the three ISDs, auditors determined the following:

- **Applications, Agreements, and Conflicts of Interest.** All three ISDs processed applications and formed and executed agreements as required. In addition, all three ISDs' conflict of interest policies complied with statutory requirements, and the ISDs had processes in place for disclosing conflicts of interest. While Canyon and Iraan-Sheffield ISDs asserted that they did not identify any conflicts of interest related to their agreements, Brazosport ISD identified conflicts of interest associated with its agreement. For the conflicts identified, Brazosport ISD generally followed its policy for disclosing those conflicts. In addition, according to that ISD's board meeting minutes, those board members with conflicts did not vote on matters related to the agreement.

### Background

The Texas Economic Development Act authorizes independent school districts (ISDs) to enter into agreements for limitations on appraised values of qualifying property (agreements). That property valuation limitation allows businesses under those agreements to pay a reduced amount of taxes to the ISD in return for creating jobs and capital improvements that enhance the local and state economies.

As of January 31, 2020, there were 491 active agreements with 211 ISDs. The ISDs audited were:

- Brazosport ISD.
- Canyon ISD.
- Iraan-Sheffield ISD.

See Appendix 3 for more background on the Texas Economic Development Act.

Sources: Texas Tax Code, Chapter 313; and the Office of the Comptroller of Public Accounts.

This audit was conducted in accordance with Texas Tax Code, Section 313.010.

For more information regarding this report, please contact Michael Clayton, Audit Manager, or Lisa Collier, First Assistant State Auditor, at (512) 936-9500.

- **Administrative Processes.** All three ISDs ensured that the payments under the agreements were calculated correctly. In addition, Canyon and Iraan-Sheffield ISDs received their payments in accordance with statutory and agreement requirements. However, Brazosport ISD did not receive its payments for tax year 2019 by the January 31, 2020, due date identified in the agreement. After auditors brought this to Brazosport ISD’s attention, the ISD followed up with the applicant. The ISD received the payments on May 6, 2020.
- **Compliance Monitoring and Reporting.** All three ISDs submitted all required monitoring reports to the Comptroller’s Office.

Table 1 presents a summary of the findings in this report and the related issue ratings. (See Appendix 2 for more information about the issue rating classifications and descriptions.)

Table 1

Summary of Chapters/Subchapters and Related Issue Ratings		
Chapter/ Subchapter	Title	Issue Rating <sup>a</sup>
1	Summary of the Agreements Audited	Not Rated
2-A	Processing Applications for Agreements and Developing Agreements	Low
2-B	Disclosing Conflicts of Interest	Low
3-A	Payments to ISDs Under Agreements	Medium
3-B	Compliance Monitoring and Reporting	Low
<p><sup>a</sup> A chapter/subchapter is rated <b>Priority</b> if the issues identified present risks or effects that if not addressed could critically affect the audited entity’s ability to effectively administer the program(s)/function(s) audited. Immediate action is required to address the noted concern and reduce risks to the audited entity.</p> <p>A chapter/subchapter is rated <b>High</b> if the issues identified present risks or effects that if not addressed could substantially affect the audited entity’s ability to effectively administer the program(s)/function(s) audited. Prompt action is essential to address the noted concern and reduce risks to the audited entity.</p> <p>A chapter/subchapter is rated <b>Medium</b> if the issues identified present risks or effects that if not addressed could moderately affect the audited entity’s ability to effectively administer the program(s)/function(s) audited. Action is needed to address the noted concern and reduce risks to a more desirable level.</p> <p>A chapter/subchapter is rated <b>Low</b> if the audit identified strengths that support the audited entity’s ability to administer the program(s)/function(s) audited or the issues identified do not present significant risks or effects that would negatively affect the audited entity’s ability to effectively administer the program(s)/function(s) audited.</p>		

Auditors communicated other, less significant issues separately in writing to Brazosport and Iraan-Sheffield ISDs.

### ***Summary of Management’s Response***

At the end of Chapter 3-A, auditors made a recommendation to address the issues identified during this audit, and Brazosport ISD agreed to implement that recommendation.

## ***Audit Objectives and Scope***

The objectives of this audit were to:

- Determine whether selected major agreements under the Texas Economic Development Act:
  - ◆ Accomplish the purposes of Texas Tax Code, Section 313.003.
  - ◆ Comply with the intent of the Legislature in enacting Texas Tax Code, Section 313.004.
  - ◆ Were executed in compliance with the provisions of Texas Tax Code, Chapter 313.
- Consider whether there are ways to increase the efficiency and effectiveness of the administration of the Texas Economic Development Act.

The scope of the audit covered selected applications and agreements under the Texas Economic Development Act processed from January 1, 2014, through December 31, 2019.

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# Detailed Results

Chapter 1

## Summary of the Agreements Audited

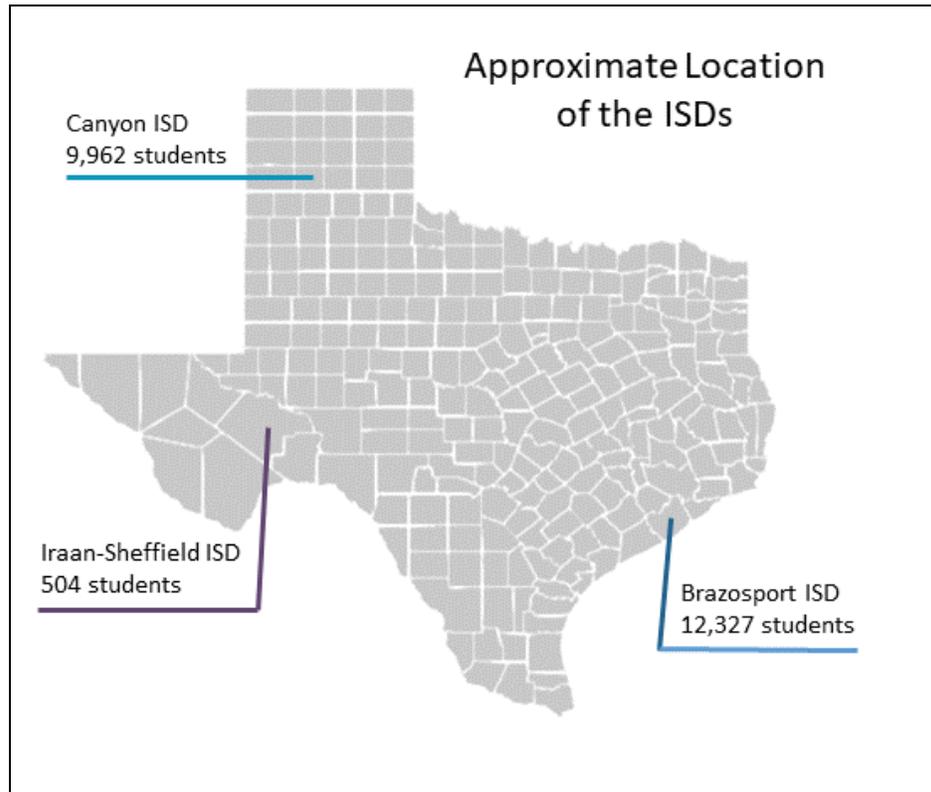
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The three agreements with businesses for limitations on appraised values of property (agreements) audited included:

- Brazosport Independent School District's (ISD) agreement with MEGlobal Americas Inc. (Application No. 1112).
- Canyon ISD's agreement with Astra Wind LLC (Application No. 1040).
- Iraan-Sheffield ISD's agreement with Midway Solar LLC (Application No. 1170).

Figure 1 shows the approximate location of those ISDs within the state.

Figure 1



Source: Based on information provided by the ISDs.

Each ISD hired a consultant to assist in the administration of the agreements selected, including (1) addressing reporting requirements and (2) performing annual calculations of revenue protection payments and supplemental payments.

Table 2 summarizes key information from the agreements audited.

Table 2

Summary of Agreements Audited			
ISD Name	Brazosport	Canyon	Iraan-Sheffield
Agreement Number	1112	1040	1170
Agreement Holder	MEGlobal Americas Inc.	Astra Wind LLC	Midway Solar LLC
Eligibility Category	Manufacturing	[Wind] Renewable Energy Electric Generation	[Non-Wind] Renewable Energy Electric Generation
County	Brazoria	Randall	Pecos
Estimated Investment Amount (in millions) <sup>a</sup>	\$1,059.3	\$211.7	\$275.9
Jobs Created <sup>b</sup>	52	5 <sup>c</sup>	2 <sup>c</sup>
Appraised Value as of December 31, 2019 (in millions)	\$490.6	\$170.8	\$131.3
Limitation per Agreement (in millions)	\$30.0	\$80.0	\$30.0
Agreement Date	March 15, 2016	April 16, 2015	June 12, 2017
Limitation Period Start Date	January 1, 2019	January 1, 2016	January 1, 2019
Limitation Period End Date	December 31, 2028	December 31, 2025	December 31, 2028
Final Termination Date	December 31, 2033	December 31, 2030	December 31, 2033
Projected Total Taxes for Agreement Period (in millions) <sup>a</sup>	\$142.7	\$28.0	\$20.5
Tax to Be Paid (Estimated in millions) <sup>a</sup>	\$58.0	\$18.9	\$8.0
Lifetime Tax Savings (Estimated in millions) <sup>a</sup>	\$84.7	\$9.1	\$12.5
Revenue Protection Payments Received Through May 31, 2020	\$512,254	\$1,340,283	\$1,002,870

Summary of Agreements Audited			
ISD Name	Brazosport	Canyon	Iraan-Sheffield
Supplemental Payments Received Through May 31, 2020	\$395,571	\$600,000	\$0

<sup>a</sup> Certain information presented in this table is based on estimates from information self-reported by the businesses and was not verified by auditors.

<sup>b</sup> Texas Tax Code, Section 313.025(f-1), allows ISDs to waive the jobs requirement if the governing body determines that the requirement exceeds the industry standard to operate a facility described in the application.

<sup>c</sup> Agreements 1040 and 1170 received waivers for the qualifying jobs requirement from the Office of the Comptroller of Public Accounts.

Sources: The Office of the Comptroller of Public Accounts' website information on Texas Tax Code, Chapter 313; Brazosport ISD; Canyon ISD; and Iraan-Sheffield ISD.

Table 3 provides information on the appraised value and the appraisal limitation value of the properties in the audited agreements through tax year 2019. The information in Table 3 provides additional background information on the audited agreements for the subsequent chapters in this report.

Table 3

Property Appraisal Values Compared to Appraisal Limitation Values for Agreements Audited January 2014 through December 2019									
Agreement Year	Brazosport ISD Agreement No. 1112 <sup>a</sup>			Canyon ISD Agreement No. 1040 <sup>a</sup>			Iraan-Sheffield ISD Agreement No. 1170 <sup>a</sup>		
	Tax Year	Appraised Value	Appraisal Limitation Value <sup>b</sup>	Tax Year	Appraised Value	Appraisal Limitation Value <sup>b</sup>	Tax Year	Appraised Value	Appraisal Limitation Value <sup>b</sup>
1	2018	\$5,000,000	No limitation <sup>a</sup>	2016	\$0	No limitation <sup>a</sup>	2018	\$0	No limitation <sup>a</sup>
2	2019	\$490,614,720	\$30,000,000	2017	\$158,791,950	\$80,000,000	2019	\$131,300,000	\$30,000,000
3				2018	\$200,301,460	\$80,000,000			
4				2019	\$170,831,310	\$80,000,000			

<sup>a</sup> All agreements have a stipulated qualifying time period to make the qualified investment. Generally, the qualifying time period begins on the date the application is approved by the ISD and ends on the last day of the second complete tax year following the agreement start date.

<sup>b</sup> Under an agreement, an ISD offers a business a limitation on the appraised value of property that allows the business to pay a reduced amount of property taxes to the ISD. The appraised value limitation amount is defined in the terms of the agreement in accordance with Texas Tax Code, Chapter 313, requirements.

Sources: Brazosport ISD, Canyon ISD, and Iraan-Sheffield ISD.

## ***Applications, Agreements, and Conflicts of Interest***

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All three ISDs had processes that were operating effectively for both processing applications and forming and executing agreements.

Additionally, all three ISDs' conflict of interest policies included all requirements in Texas Local Government Code, Chapters 171 and 176.

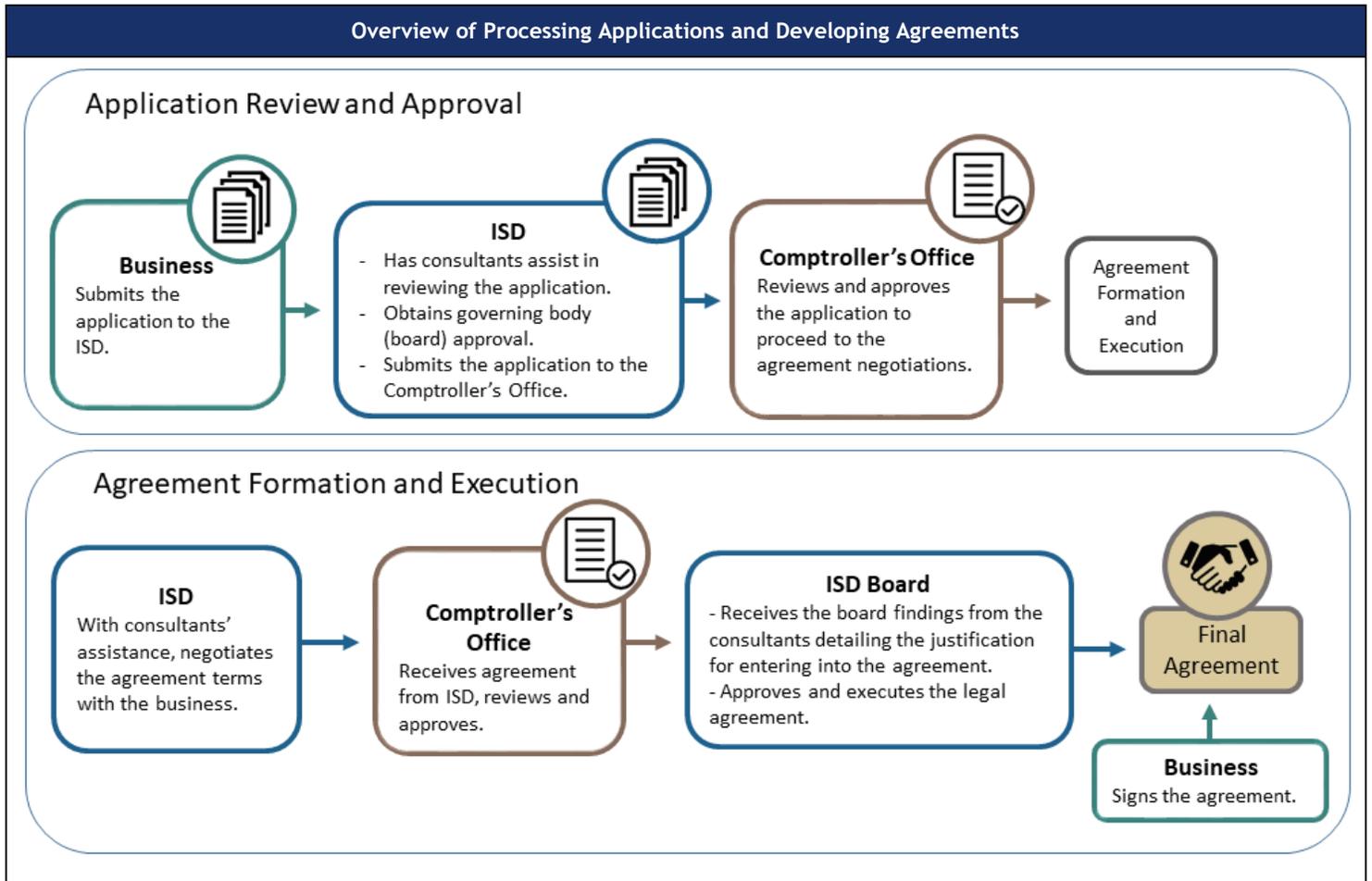
While two of the ISDs asserted that they did not identify any conflicts of interest related to their agreements, the remaining ISD identified conflicts of interest associated with its agreement. For the conflicts identified, that ISD generally followed its policy for disclosing those conflicts. However, it did not always ensure that its board members with conflicts submitted conflict of interest statements prior to the board voting on matters related to this agreement. According to the ISD's board meeting minutes, those board members with conflicts did not vote on matters related to the agreement.

### **Background on Establishing Property Value Limitation Agreements**

A business submits an application to the ISD for the ISD to consider entering into a property value limitation agreement (agreement). That agreement allows a business to pay a reduced amount of taxes to the ISD in return for creating jobs and capital investment that enhances the local and state economies. The ISD retains consultants to (1) assist in reviewing the application and (2) provide input on whether a potential agreement would be beneficial to the ISD. As part of the application review and agreement formation processes, the ISD's board holds meetings to vote on (1) accepting the application to proceed to the review process and (2) approving and executing the final agreement between the ISD and the business. See Appendix 3 for further information on how agreements are formed, including the application process.

Figure 2 on the next page shows the overview for processing applications and developing agreements.

Figure 2



Sources: Based on information provided by the ISDs and the Comptroller's Office.

## Processing Applications for Agreements and Developing Agreements

**Chapter 2-A  
Rating:**
Low<sup>1</sup>

Table 4 summarizes the results of testing of the applications that the businesses submitted and the agreements entered into by the three ISDs. Based on those testing results, the ISDs processed the applications and developed agreements appropriately.

Table 4

Testing Results - Applications for Agreements and Developing Agreements			
Attribute	Brazosport ISD (1112)	Canyon ISD (1040)	Iraan-Sheffield ISD (1170)
Did the submitted application contain sufficient information to indicate that the qualifying property met the applicable criteria established by Texas Tax Code, Section 313.021(2), and was the applicable application fee included?	Yes	Yes	Yes
Before approving the application, did the ISD properly verify the accuracy and completeness of information in the application; evaluate the application to ensure that the business project met the eligibility requirements; and determine that granting the application was in the best interest of the ISD and the State?	Yes	Yes	Yes
Did the agreement between the ISD and the business contain all provisions required by statute at the time of the agreement?	Yes	Yes	Yes

<sup>1</sup> The risk related to the issues discussed in Chapter 2-A is rated as Low because the audit identified strengths that support the audited entity's ability to administer the program(s)/function(s) audited or the issues identified do not present significant risks or effects that would negatively affect the audited entity's ability to effectively administer the program(s)/function(s) audited.

**Disclosing Conflicts of Interest**

**Chapter 2-B  
Rating:**

Low <sup>2</sup>

The audited ISDs' conflict of interest policies included all requirements in Texas Local Government Code, Chapters 171 and 176 (see text box for additional information on conflicts of interest requirements). Those policies required school board members and other related parties to submit conflict of interest statements only when a conflict existed.

Canyon and Iraan-Sheffield ISDs asserted that they did not identify any conflicts of interest associated with their agreements.

For Brazosport ISD, two board members with conflicts of interest associated with the ISD's agreement appropriately submitted conflict of interest statements prior to the board voting on the agreement, and those board members did not participate in voting related to the agreement. However, the ISD did not ensure that an additional board member with a conflict submitted a conflict of interest statement prior to the board voting on amendments related to the final executed agreement, as required by its policy. According to the ISD's board meeting minutes, that board member did not vote on the amendments to the agreement.

Additionally, while statute does not require that school board members submit conflict of interest statements when conflicts do not exist, a requirement by ISDs that board members submit statements would help reduce the risk that a conflict could exist but would not be disclosed.

**Conflicts of Interest Requirements**

Texas Local Government Code, Chapters 171 and 176, includes several requirements relating to disclosing conflicts of interest. For example, those provisions require:

- A local public official who has a substantial interest in a business entity or real property to file an affidavit stating the nature and extent of the interest and abstain from voting if the action on the matter will have a special economic effect on the business entity or the value of the real property that is distinguishable from the effect on the public.
- A local government officer who has a business or family relationship with a vendor to file a conflict disclosure statement when the local government entity enters or considers entering into a contract with that vendor.

Source: Texas Local Government Code, Sections 171.004 and 176.003.

<sup>2</sup> The risk related to the issues discussed in Chapter 2-B is rated as Low because the audit identified strengths that support the audited entity's ability to administer the program(s)/function(s) audited or the issues identified do not present significant risks or effects that would negatively affect the audited entity's ability to effectively administer the program(s)/function(s) audited.

## Payments, Compliance Monitoring, and Reporting

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All three ISDs ensured that the payments under the agreements audited were calculated correctly.

Two of the ISDs received the payments associated with their agreements by the due dates. The remaining ISD did not receive its payments for tax year 2019 by the due date identified in the agreement.

In addition, all three ISDs submitted all required monitoring reports to the Comptroller's Office.

**Chapter 3-A  
Rating:  
Medium<sup>3</sup>**

### Chapter 3-A

#### Payments to ISDs Under Agreements

All three ISDs ensured that the payments under the agreements audited were calculated correctly (see text box for information about payment types). Canyon and Iraan-Sheffield ISDs received their payments in accordance with statutory and agreement requirements.

However, Brazosport ISD did not receive a revenue protection payment of \$512,254 and a supplemental payment of \$395,571 for tax year 2019 from the applicant (business) by the due date of January 31, 2020. In addition, the ISD did not follow up with the applicant when it did not receive the payments by the due date. Brazosport ISD's agreement with MEGlobal Americas Inc. includes provisions for the ISD to provide notice to the applicant and possibly take corrective action if the applicant does not fulfill terms of the agreement. After auditors inquired about the missing payments, the ISD contacted the applicant. The ISD received the payments on May 6, 2020.

#### Selected Payment Types Under the Audited Agreements

- **Revenue Protection Payment** - The payment from the applicant to protect an ISD against losses in maintenance and operations revenue throughout the duration of the agreement.
- **Supplemental Payment** - An amount paid to an ISD for the execution of an agreement. The annual supplemental payment amount is the greater of either \$50,000 or \$100 per student per year multiplied by average daily attendance.

Source: The Comptroller's Office.

Table 5 on the next page summarizes the results of auditors' testing of payments received by the ISDs audited.

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<sup>3</sup> The risk related to the issues discussed in Chapter 3-A is rated as Medium because the issues identified present risks or effects that if not addressed could moderately affect the audited entity's ability to effectively administer the program(s)/function(s) audited. Action is needed to address the noted concern and reduce risks to a more desirable level.

Table 5

Testing Results - Payments Received by the ISDs			
Attribute	Brazosport ISD (1112)	Canyon ISD (1040)	Iraan-Sheffield ISD (1170)
Were the revenue protection payments and supplemental payments (payment in lieu of taxes) paid by the applicant by the due date?	No <sup>a</sup>	Yes	Yes
Were the calculations of the revenue protection payment and supplemental payment (payment in lieu of taxes) amounts performed correctly/accurately and in accordance with the agreement?	Yes	Yes	Yes
<sup>a</sup> Brazosport ISD did not receive the Revenue Protection and Supplemental Payments that were due from the applicant by January 31, 2020. The ISD sent an invoice to the applicant for tax year 2019 payments on October 16, 2019, and received the payments on May 6, 2020.			

### Recommendation

Brazosport ISD should ensure that it monitors payments due from applicants with which it has established tax limitation agreements and that it receives those payments by the due date.

### Management's Response

*Management has reviewed the draft report on an Audit of Selected Major Agreements Under the Texas Economic Development Act. Chapter 3-A Payments to ISDs Under Agreement identified that Brazosport ISD did not receive a revenue protection payment of \$512,254 and a supplemental payment of \$395,571 for tax year 2019 from the business by the due date of January 31, 2020. While Management agrees with the finding, our management response to this is Brazosport ISD has a reconciliation process in place and had identified the payment had not been received. Correction action will be to ensure Management timely provides notification in the future to the company when a payment is not received by the due date. Management will ensure Brazosport ISD monitors payments due from applicants with which it has established tax limitation agreements and that it receives those payments by the due date.*

## Compliance Monitoring and Reporting

**Chapter 3-B  
Rating:  
Low <sup>4</sup>**

All three ISDs submitted all required monitoring reports to the Comptroller’s Office (see text box for required monitoring reports).

All three ISDs relied on their consultants for monitoring and oversight of the agreements and for ensuring submission of the required reports.

Table 6 summarizes the results of auditors’ testing of compliance and reporting requirements.

### Required Monitoring (Eligibility and Progress) Reports

The ISDs are required to submit monitoring reports for their agreements to the Comptroller’s Office. Specifically:

- **Annual Eligibility Report (Form 50-772A)** - The form filled out annually by businesses in agreements and submitted to the ISDs by June 15 to report continued eligibility under Texas Tax Code, Chapter 313. The ISDs must submit the form to the Comptroller’s Office by August 15.
- **Biennial Progress Report (Forms 50-773A and 50-773B)** - The form filled out by businesses in agreements and submitted to the ISDs by June 15 of each even-numbered year to report business project status. The ISDs must submit the form to the Comptroller’s Office by August 15.
- **Biennial School District Cost Data Request (Forms 50-827A and 50-827B)** - The form completed by the ISDs and submitted to the Comptroller’s Office by August 15 of each even-numbered year to report payment activity and projected costs over the life of the agreement.

Source: The Comptroller’s Office’s website.

Table 6

Testing Results - Compliance Reporting			
Requirement Tested	Brazosport ISD (1112)	Canyon ISD (1040)	Iraan-Sheffield ISD (1170)
Did the ISD monitor the business’ compliance with the limitation agreement, including submitting the required monitoring reports showing that capital investments and job creation were performed as agreed?	Yes	Yes	Yes
Did the ISD’s website contain a link to the Comptroller’s Office-maintained website with all Chapter 313 limitation agreement information?	Yes	Yes	Yes

<sup>4</sup> The risk related to the issues discussed in Chapter 3-B is rated as Low because the audit identified strengths that support the audited entity’s ability to administer the program(s)/function(s) audited or the issues identified do not present significant risks or effects that would negatively affect the audited entity’s ability to effectively administer the program(s)/function(s) audited.

# Appendices

Appendix 1

## **Objectives, Scope, and Methodology**

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### **Objectives**

The objectives of this audit were to:

- Determine whether selected major agreements under the Texas Economic Development Act:
  - ♦ Accomplish the purposes of Texas Tax Code, Section 313.003.
  - ♦ Comply with the intent of the Legislature in enacting Texas Tax Code, Section 313.004.
  - ♦ Were executed in compliance with the provisions of Texas Tax Code, Chapter 313.
- Consider whether there are ways to increase the efficiency and effectiveness of the administration of the Texas Economic Development Act.

### **Scope**

The scope of the audit covered selected applications and property value limitation agreements (agreements) under the Texas Economic Development Act processed from January 1, 2014, through December 31, 2019.

### **Methodology**

The audit methodology included selecting agreements from the Office of the Comptroller of Public Accounts' (Comptroller's Office's) listing of agreements to audit at the following three independent school districts (ISDs):

- Brazosport ISD (Brazoria County).
- Canyon ISD (Randall County).
- Iraan-Sheffield ISD (Pecos County).

Auditors selected the agreements considering criteria that they determined to represent risk characteristics using information that the businesses (applicants) reported. This information included total gross tax savings for the businesses as a result of the appraisal limitation, total qualified investment, and total revenue payments. Additionally, auditors considered

factors such as eligibility category, geographic location, and school district size when selecting agreements.

The three agreements selected from the three ISDs were:

- An agreement between Brazosport ISD and MEGlobal Americas Inc. (previously Dow Chemical) for property used in manufacturing (Application 1112).
- An agreement between Canyon ISD and Astra Wind LLC for property used in renewable energy electricity generation (Application 1040).
- An agreement between Iraan-Sheffield ISD and Midway Solar LLC for property used in renewable energy electricity generation (Application 1170).

Auditors did not use a sampling methodology on this audit and instead collected, reviewed, and analyzed information related to selected agreements to perform selected tests and other procedures. Therefore, it was not appropriate for auditors to project testing results to the populations.

The audit methodology also included (1) testing applications, agreements, conflict of interest policies and procedures, and required annual and biennial reports and (2) conducting interviews with ISD personnel and consultants and management and staff at the Comptroller's Office.

Information collected and reviewed included the following:

- Agreements between the ISDs and the businesses.
- Application documentation, including certificates for limitations on appraised value and economic impact analyses issued by the Comptroller's Office; facilities impact evaluations from the Texas Education Agency; ISDs' financial projections; ISD board application review results; and correspondence from the Comptroller's Office to the ISDs.
- Minutes from the ISDs' board meetings.
- Eligibility and compliance monitoring reports including Annual Eligibility Reports; Biennial Progress Reports; Biennial School District Cost Data Requests; and Reports on Value Lost Because of Value Limitations Under Tax Code, Chapter 313.
- ISD policies and procedures.

- Conflict of interest statements signed by selected ISD board members and management.
- Supporting documentation for calculations and receipts of revenue protection and supplemental payments.
- Agreement data used to develop the Comptroller's Office's *Report of the Texas Economic Development Act*, January 2019.

Procedures and tests conducted included the following:

- Interviewed ISD board members, management, staff, and consultants; and Comptroller's Office management and staff.
- Performed analysis on the populations of agreements from the Comptroller's Office.
- Tested selected applications and associated agreements for compliance with applicable requirements.
- Reviewed calculations and tested receipts of revenue protection and supplemental payments.

Criteria used included the following:

- Texas Tax Code, Chapters 312 and 313.
- Texas Local Government Code, Chapters 171 and 176.
- Title 34, Texas Administrative Code, Chapter 9.
- Texas Education Code, Chapter 48.
- ISD policies and procedures.
- Comptroller's Office policies, procedures, and guidance with regards to Chapter 313 agreements.
- Agreements between the ISDs and the businesses.

## Project Information

Audit fieldwork was conducted from March 2020 through June 2020. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The following members of the State Auditor's staff performed the audit:

- Kelly Bratton, CFSA, CRMA, MBA (Project Manager)
- Serra Tamur, MPAff, CISA, CIA (Assistant Project Manager)
- Sarah Ore Ogunmayin
- Nakeesa Shahparasti, CPA, CFE, CISA
- Kiara White, MPP
- Ann E. Karnes, CPA (Quality Control Reviewer)
- Michael Owen Clayton, CPA, CISA, CFE, CIDA (Audit Manager)

## Issue Rating Classifications and Descriptions

Auditors used professional judgment and rated the audit findings identified in this report. Those issue ratings are summarized in the report chapters/sub-chapters. The issue ratings were determined based on the degree of risk or effect of the findings in relation to the audit objective(s).

In determining the ratings of audit findings, auditors considered factors such as financial impact; potential failure to meet program/function objectives; noncompliance with state statute(s), rules, regulations, and other requirements or criteria; and the inadequacy of the design and/or operating effectiveness of internal controls. In addition, evidence of potential fraud, waste, or abuse; significant control environment issues; and little to no corrective action for issues previously identified could increase the ratings for audit findings. Auditors also identified and considered other factors when appropriate.

Table 7 provides a description of the issue ratings presented in this report.

Table 7

Summary of Issue Ratings	
Issue Rating	Description of Rating
Low	The audit identified strengths that support the audited entity's ability to administer the program(s)/function(s) audited <u>or</u> the issues identified do not present significant risks or effects that would negatively affect the audited entity's ability to effectively administer the program(s)/function(s) audited.
Medium	Issues identified present risks or effects that if not addressed could <u>moderately affect</u> the audited entity's ability to effectively administer the program(s)/function(s) audited. Action is needed to address the noted concern(s) and reduce risks to a more desirable level.
High	Issues identified present risks or effects that if not addressed could <u>substantially affect</u> the audited entity's ability to effectively administer the program(s)/function(s) audited. Prompt action is essential to address the noted concern(s) and reduce risks to the audited entity.
Priority	Issues identified present risks or effects that if not addressed could <u>critically affect</u> the audited entity's ability to effectively administer the program(s)/function(s) audited. Immediate action is required to address the noted concern(s) and reduce risks to the audited entity.

## ***Background Information on the Texas Economic Development Act***

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In 2001, the 77th Legislature enacted the Texas Economic Development Act, Texas Tax Code, Chapter 313 (Act), which permitted independent school districts (ISDs) to offer eight-year limitations on the appraised values of property for the maintenance and operations portion of the ISDs' property taxes. Under the Act, ISDs also were entitled to receive additional state aid each tax year from the Texas Education Agency for tax credits that are associated with the agreements for limitations on the appraised values of property (agreements).

The purpose of the Act was to enhance economic development in Texas by permitting ISDs to offer incentives to attract large capital investments and new jobs. Additionally, the Act sought to attract new businesses or production to improve the Texas economy and expand the property tax base.

In 2013, the 83rd Legislature passed House Bill 3390 (HB 3390), which both reauthorized the economic development program for 10 years and made several substantive changes. Those changes included repealing the tax credit provisions; adjusting the definitions of qualified jobs, properties, and investments; requiring that all agreements use a form developed by the Comptroller's Office; and requiring that the State Auditor's Office conduct a yearly audit of selected agreements under the Act.

In addition, the Legislature expressed in HB 3390 its intent that economic development decisions involving ISD property taxes should occur locally with oversight by the State and should be consistent with identifiable statewide economic development goals. Under the Act, Texas ISDs are authorized to offer tax incentives to applicants that invest in the local community. The Act offers applicants a 10-year limitation on appraised value for a portion of the ISD property tax (ad valorem tax). In exchange for that limitation, the applicants agree to invest in new property, create jobs in the ISD, and maintain a presence in the community for a specified number of years. Local tax revenues that the ISDs forego during the limitation period are replaced with state funding, plus direct incentives from the applicant based on tax savings and school attendance as described in individual agreements developed after the applicant is approved by the ISD and the Comptroller's Office.

Further, the Act describes situations in which property owners may not receive ad valorem tax benefits under the Texas Tax Code, including prohibiting property owners from pooling investments to qualify for ad valorem tax benefits and prohibiting benefits to entities that are not subject to Texas franchise tax. The Texas Tax Code also does not allow an applicant

to assert that jobs will be eliminated if certain investments are not made, if that assertion is not true.

The Act also includes specific guidance to the ISDs and the Comptroller's Office. The ISDs are directed to approve only applications for agreements that enhance the local community, improve the local public education system, and create high-paying jobs. The Comptroller's Office is directed to certify limitations on appraised values only for applications for agreements that create high-paying jobs and provide a net long-term benefit to the State. Both the ISDs and the Comptroller's Office are directed to strictly interpret the criteria and selection guidelines of the Act and to select and certify only applications that advance the economic development goals of the State.

**Related State Auditor's Office Work**

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Related State Auditor's Office Work		
Number	Product Name	Release Date
19-046	An Audit Report on Selected Major Agreements Under the Texas Economic Development Act	July 2019
18-037	An Audit Report on Selected Major Agreements Under the Texas Economic Development Act	July 2018
17-043	An Audit Report on Selected Major Agreements Under the Texas Economic Development Act	July 2017
17-009	An Audit Report on Selected Major Agreements Under the Texas Economic Development Act	October 2016
16-021	A Report on the Implementation Status of Prior State Auditor's Office Recommendations	April 2016
15-042	An Audit Report on Selected Major Agreements Under the Texas Economic Development Act	August 2015

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