



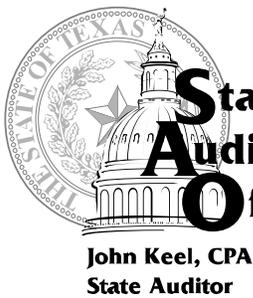
John Keel, CPA
State Auditor

An Audit Report on

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

November 2014

Report No. 15-009



State Auditor's Office

John Keel, CPA
State Auditor

An Audit Report on

Selected Major Agreements Under the Texas Economic Development Act

SAO Report No. 15-009
November 2014

Overall Conclusion

The Texas Economic Development Act (Texas Tax Code, Chapter 313) has encouraged capital investment and job creation by businesses that have appraisal limitation agreements (agreements) with school districts. Oversight of those agreements relies primarily on self-reported information that businesses certify.

County appraisal districts reported to the Office of the Comptroller of Public Accounts (Comptroller's Office) that, from tax year 2005 through tax year 2013, an estimated \$905.2 million in property tax revenue was lost as a result of agreements. In addition, as of December 31, 2013, businesses associated with approximately 242 executed agreements and 57 applications for agreements may be entitled to receive an estimated \$786 million in tax credits from tax year 2014 through tax year 2030.

To determine whether businesses with agreements complied with Texas Tax Code, Chapter 313, the four school districts audited¹ relied primarily on the certification of the annual eligibility forms and biennial progress reports that businesses submitted to confirm the businesses' capital investment and the number of jobs they committed to create or had created. Statute does not require school districts to verify that information, and the school districts audited did not perform verifications.

The Texas Economic Development Act (Texas Tax Code, Chapter 313)

In 2001, the 77th Legislature enacted House Bill 1200, which created Tax Code, Chapter 313, known as the Texas Economic Development Act (Act). The purpose of the Act, as specified in Texas Tax Code, Section 313.003, is to:

- Encourage large-scale capital investments in this state, especially in school districts that have an ad valorem tax base that is less than the statewide average ad valorem tax base of school districts in this state;
- Create new, high-paying jobs in this state;
- Attract to this state new, large-scale businesses that are exploring opportunities to locate in other states or other countries;
- Enable local government officials and economic development professionals to compete with other states by authorizing economic development incentives that meet or exceed incentives being offered to prospective employers by other states and to provide local officials with an effective means to attract large-scale investment;
- Strengthen and improve the overall performance of the economy of this state;
- Expand and enlarge the ad valorem property tax base of this state; and
- Enhance this state's economic development efforts by providing school districts with an effective local economic development option.

The Act allows a school district to attract new taxable property and create jobs by offering (1) a tax credit and (2) an eight-year limitation on the appraised value of a property for the maintenance and operations portion of the school district's property tax. The property remains fully taxable for the purposes of any school district debt service tax. Texas Education Code, Section 42.2515, entitles school districts to additional state aid from the Texas Education Agency for tax credits that are applied against the property taxes of businesses with appraisal limitation agreements (agreements) each tax year.

In January 2013, the Office of the Comptroller of Public Accounts (Comptroller's Office) reported that businesses with agreements had invested approximately \$42.2 billion in the State and created 6,994 qualifying jobs through August 2011.

As of December 31, 2013, there were 242 executed agreements between 137 school districts and 174 businesses.

Source: The Comptroller's Office.

¹ The four school districts audited included the Austin Independent School District, the Fort Stockton Independent School District, the Palacios Independent School District, and the Sterling City Independent School District.

School districts provide the information that businesses submit to the Comptroller's Office and the Texas Education Agency (TEA) as the basis for additional state aid paid to the school districts for (1) property tax revenue losses associated with agreements and (2) tax credits associated with agreements. Because school districts certify that information provided is true and correct, neither the Comptroller's Office nor TEA verifies the information.

Each of the four school districts audited hired the same consultant to compile information that businesses reported.

Based on the information in their annual eligibility forms and biennial progress reports, the businesses with agreements certified that they met certain elements and complied with various requirements of Texas Tax Code, Chapter 313. The school districts associated with the agreements accepted the submissions.

Overall accountability and transparency of agreements could be strengthened in the following areas:

- **Verification of information.** As discussed above, the school districts audited relied primarily on certifications that businesses submit. Statute does not require school districts to verify that information, and the school districts audited did not perform verifications.
- **Disclosing conflicts of interests.** The ethics policies for each school district audited varied, and the Comptroller's Office and TEA did not require their staff to disclose potential conflicts of interest or affirm that no conflicts existed with the businesses and the consultants associated with the agreements.
- **Issuing tax credits.** From tax year 2006 through tax year 2013, 47 school districts processed approximately \$26 million in tax credits to businesses with which they had agreements. At the direction of TEA, most school districts paid tax credits directly to businesses. However, as specified by Texas Tax Code, Chapter 313, their agreements required the school districts to direct their collectors of taxes to apply tax credits to a business's future property taxes.
- **Developing agreements.** The agreements audited included provisions that complied with Texas Tax Code, Chapter 313, and were approved by the members or trustees of a school district's board. However, agreements did not consistently:
 - Specify the agreed-upon investment amounts, the description and address of the property, and the anticipated number of jobs to be created. (That information was in the applications for agreements.)
 - Describe how school districts would determine and issue tax credits to businesses.
 - Require businesses to obtain written approval from the Comptroller's Office and the school district to add new property to the agreement.

- Require school districts to determine the eligibility of any new business to which an existing agreement would be transferred.

In addition, opportunities exist to improve certain administrative processes at each school district audited. While the issues identified in those processes may not be material to determining compliance with Texas Tax Code, Chapter 313, they are significant to each school district's management of agreements.

Auditors also communicated other, less significant issues separately in writing to each school district audited, the Comptroller's Office, and TEA.

Selected Recommendations

The Legislature should consider:

- Requiring an independent verification of the information that businesses with agreements submit to school districts.
- Requiring school district board members, employees, and consultants to disclose on an annual basis any business, professional, and personal relationships that could create potential conflicts of interest with agreements.

Summary of Management's Response

The Comptroller's Office agreed with the recommendations addressed to it in this report. TEA and the school districts audited did not agree with certain findings and recommendations addressed to them.

The State Auditor's Office stands by its conclusions based on the evidence presented and compiled during this audit.

Summary of Information Technology Review

Auditors performed a limited review of general controls and logical security for the Comptroller's Office network and network folders and determined that data maintained on the Comptroller's Office's network was reasonably secure.

Summary of Objectives, Scope, and Methodology

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.
- Determine whether there are ways to increase the efficiency and effectiveness of the administration of the Texas Economic Development Act.

The scope of this audit covered selected applications and agreements processed from September 1, 2003, through December 31, 2013.

The audit methodology consisted of selecting seven agreements to audit, collecting and reviewing applications, agreements, and progress reports; conducting interviews with school districts, the Comptroller's Office, and TEA management, staff, and consultants; reviewing statutes, rules, and policies and procedures of the school districts, the Comptroller's Office, and TEA; identifying and collecting information from other reports; and performing selected tests and other procedures.

Auditors determined that the data from the Comptroller's Office's Property Tax System was sufficiently reliable for the purposes of this audit. Auditors' assessment of the reliability of that data was based on reconciling it with property tax reports that county appraisal districts submitted to the Comptroller's Office.

Auditors' assessment of the reliability of additional state aid payment data from TEA's Foundation School Program System relied on prior audit work performed, and auditors determined that additional state aid payment data from that system was sufficiently reliable for the purposes of this audit.

Auditors were unable to determine whether the data processed by the software program that TEA uses to evaluate school finance projections was sufficiently reliable for the purposes of this audit. TEA did not maintain a log of the programming changes it made to that software program. Therefore, auditors did not rely on it for this audit.

Contents

Detailed Results

| | |
|---|----|
| Chapter 1 | |
| Oversight of Agreements Relies Primarily on Information That Businesses Report | 1 |
| Chapter 2 | |
| The Comptroller’s Office Should Improve Its Administration of Agreements..... | 4 |
| Chapter 3 | |
| TEA Should Improve Certain Processes for Determining Additional State Aid Provided to School Districts That Issue Tax Credits and Evaluating School District Financial Projections..... | 16 |
| Chapter 4 | |
| Austin Independent School District Agreement with Hewlett-Packard Company..... | 22 |
| Chapter 5 | |
| Fort Stockton Independent School District Agreements with SandRidge Energy, Inc. | 34 |
| Chapter 6 | |
| Palacios Independent School District Agreements with NRG South Texas 3 and NRG South Texas 4..... | 50 |
| Chapter 7 | |
| Sterling City Independent School District Agreements with Goat Mountain Wind, LP and Goat Wind, LP | 60 |

Appendices

| | |
|---|----|
| Appendix 1 | |
| Objectives, Scope, and Methodology | 77 |
| Appendix 2 | |
| Selected Information on the Seven Agreements Audited..... | 83 |

| | |
|---|-----|
| Appendix 3 | |
| Summary of Additional State Aid Paid and Projected to Be Paid from September 1, 2009, through December 31, 2030 | 87 |
| Appendix 4 | |
| Texas Tax Code, Sections 313.103 and 313.104 | 88 |
| Appendix 5 | |
| Property Tax Revenue Losses Related to Agreements for Tax Years 2005 through 2013 | 90 |
| Appendix 6 | |
| Time Line of Appraisal Value Limitations and Tax Credits Under Texas Tax Code, Chapter 313 | 93 |
| Appendix 7 | |
| Glossary of Selected Terms Related to Agreements..... | 95 |
| Appendix 8 | |
| Job-creation and Net Tax Benefit Information for the Seven Audited Agreements..... | 98 |
| Appendix 9 | |
| Texas Tax Code, Sections 313.101 through 313.105 (Repealed)..... | 99 |
| Appendix 10 | |
| House Bill 3676 (81st Legislature, Regular Session) | 101 |
| Appendix 11 | |
| Periodic Reporting Forms that Businesses with Agreements Certify | 105 |

Detailed Results

Chapter 1

Oversight of Agreements Relies Primarily on Information That Businesses Report

Oversight of appraisal limitation agreements (agreements) under the Texas Economic Development Act (Texas Tax Code, Chapter 313) relies primarily on information that businesses with agreements report. To determine whether businesses with agreements complied with Texas Tax Code, Chapter 313, the four school districts audited² relied primarily on the certification of the annual eligibility forms and biennial progress reports that businesses submitted to confirm the businesses' capital investment and the number of jobs they committed to create or had created. Texas Tax Code, Chapter 313, does not require school districts to verify that information, and the school districts audited did not perform verifications.

School districts provide the information that businesses submit to the Office of the Comptroller of Public Accounts (Comptroller's Office) and the Texas Education Agency (TEA) as the basis for additional state aid paid to the school districts for (1) property tax revenue losses associated with agreements and (2) tax credits associated with agreements. This report discusses risks in determining whether a business is in full compliance with the capital investment and job-creation requirements in Texas Tax Code, Chapter 313.

It is important to note that changes made to statute by House Bill 3390 (83rd Legislature, Regular Session) to establish additional monitoring and reporting requirements may not be applicable to older agreements that were executed before January 1, 2014.

Additional state aid provided to school districts is based primarily on information reported by businesses.

Texas Tax Code, Chapter 313, does not require that the compliance and property information that businesses with agreements report to school districts be verified for accuracy and completeness. The school districts relied primarily on information that the businesses certified to be true and correct.

The school districts provide that information to the Comptroller's Office and TEA, as needed, for those agencies' administration of additional state aid payments to school districts. Because the school districts certify that information is true and correct, neither the Comptroller's Office nor TEA verifies that information.

² The four school districts audited included the Austin Independent School District, the Fort Stockton Independent School District, the Palacios Independent School District, and the Sterling City Independent School District.

The Comptroller's Office and TEA rely primarily on the certified information that school districts provide to support the appropriateness of additional state aid paid to school districts that have agreements. Specifically:

- **Additional state aid for property tax revenue losses.** The Comptroller's Office relies primarily on certified property value reports from school districts and county appraisal districts to support property tax revenue losses for properties covered by agreements. The Comptroller's Office provides that information to TEA to include in the school finance system's formula funding calculation. Through the school finance system's formula funding, school districts are held harmless for property tax revenue losses resulting from the agreements and do not incur reductions in their state funding (see text box for more information). However, auditors identified inconsistencies between school district records for the property related to five of the seven agreements audited and county appraisal district records for the property related to those agreements. See Chapters 4-C, 5-D, and 7-D for more information.

**House Bill 1200
(77th Legislature,
Regular Session)**

House Bill 1200 amended Texas Government Code, Chapter 403, subchapter M which describes the methodology for determining property values for school districts in order to distribute state funding. Section 403.302 (d) was amended to include a provision that would allow the market value of property that would not otherwise be allowed because of an appraisal limitation agreement to be included in the determination of a school district's property value.

For tax years 2005 through 2013, county appraisal districts reported an estimated \$905.2 million in property tax revenue losses resulting from agreements. See Appendix 5 for more information on the property tax revenue losses reported.

- **Additional state aid for tax credits issued to businesses.** TEA relies primarily on information that school districts certify to support additional state aid provided to school districts for the tax credits they issue to businesses with agreements (see Chapter 3-A for more information on TEA's process for providing additional state aid for tax credits issued by school districts). However, for four of the seven agreements audited, the associated school districts relied primarily on the information that the businesses submitted in order to request additional state aid from TEA. The Comptroller's Office's rules require that, prior to issuing tax credits to businesses, school districts determine whether the businesses have complied with their agreements. As of December 31, 2013, TEA had provided a total of \$26 million in additional state aid to school districts for tax credits the school districts had issued to businesses with agreements. For tax years 2014 through 2030, businesses with agreements may be entitled to receive an estimated \$786 million in tax credits. See Appendix 3 for more information on tax credits.

Requirements to disclose potential conflicts of interest vary across school districts.

As Chapters 5 through 7 of this report discuss in more detail, requirements for school district board members, employees, and consultants to disclose business, professional, and personal relationships that could create potential conflicts of interest varied across the four school districts audited. Ensuring that those requirements are comprehensive and consistent could help to strengthen agreements' transparency and accountability.

**House Bill 3390
(83rd Legislature,
Regular Session)**

House Bill 3390 amended Texas Tax Code, Chapter 313, by (1) assigning to the Comptroller's Office additional monitoring and reporting responsibilities with regard to job-creation requirements in agreements and (2) removing provisions that allowed businesses with agreements to receive tax credits.

Those changes were limited to new agreements that would be executed on or after January 1, 2014. Agreements that were executed prior to January 1, 2014, may not be subject to those changes.

Agreements executed prior to January 1, 2014, may not be subject to statutory monitoring and reporting requirements.

House Bill 3390 (83rd Legislature, Regular Session) amended Texas Tax Code, Chapter 313, to assign additional monitoring and reporting requirements to the Comptroller's Office and remove provisions that allowed for tax credits (see text box for additional details). However, those changes may not be applicable to approximately 242 executed agreements that were executed prior to January 1, 2014. The businesses associated with those executed agreements and 57 applications for agreements submitted prior to January 1, 2014, that were processed by the Comptroller's Office may be eligible to receive the estimated \$786 million in tax credits discussed above.

Recommendations

The Legislature should consider:

- Requiring an independent verification of the information that businesses with agreements submit to school districts.
- Requiring school district board members, employees, and consultants to disclose on an annual basis any business, professional, and personal relationships that could create potential conflicts of interest with agreements.

The Comptroller's Office Should Improve Its Administration of Agreements

Opportunities exist for the Comptroller's Office to strengthen its processes to ensure that:

- Agreements are managed efficiently and effectively.
- Taxpayers' interests are protected.
- State funds are used appropriately to provide additional state aid to school districts for (1) property tax revenue losses resulting from agreements and (2) tax credits school districts issue to businesses that have agreements.

For tax years 2005 through 2013, county appraisal districts reported to the Comptroller's Office that agreements resulted in an estimated \$905.2 million in property tax revenue losses. The State does not compensate school districts on a dollar-for-dollar basis for those losses; instead, the property tax revenue loss is a component in the school finance system's formula funding calculation. TEA provides additional state aid to school districts for tax credits the school districts issue to businesses with agreements. For tax years 2014 through 2030, businesses with agreements may be entitled to receive an estimated \$786 million in tax credits. See Appendix 3 for more information on tax credits.

Chapter 2-A

The Comptroller's Office Should Strengthen and Implement Certain Processes to Improve the Accountability and Transparency of Agreements

The Comptroller's Office's rules require school districts to monitor and enforce businesses' compliance with requirements in their agreements. As discussed in Chapter 1, statute does not require school districts to verify that information, and the school districts audited did not perform verifications.

The Comptroller's Office's rules recommend that, to determine compliance with requirements, school districts should require businesses to submit (1) annual eligibility reports and (2) information they used to complete those reports.

The Comptroller's Office relies on information that school districts submit.

The Comptroller's Office's processes rely on property-related information that school districts report on agreements. That property-related information is significant to determining the amount of additional state funding that school districts with agreements will receive as compensation for property tax revenue losses.

The Comptroller's Office requires county appraisal districts to report on the property tax revenue loss on property covered by an agreement. However, the Comptroller's Office's processes do not also require school districts to provide documentation to show that property under an agreement is the same property for which county appraisal districts report property tax revenue losses.

The Comptroller's Office should ensure that school districts provide required documentation.

The Comptroller's Office's processes did not ensure that all school districts provided it with copies of documents related to agreements that the Comptroller's Office is statutorily required to post on its Web site. Specifically:

- The Comptroller's Office did not obtain copies of applications for tax credits for 47 school districts that had processed tax credits as of December 2013. School districts provided copies of those tax credit applications to TEA to support requests for additional state aid that TEA pays to school districts; however, the Comptroller's Office is not involved in that payment process. As of May 2014, the Comptroller's Office reported that it had received copies of applications for tax credits from only seven school districts, and it had not posted those applications on its Web site.
- The Comptroller's Office did not obtain a Beaumont Independent School District agreement that was associated with an application the Comptroller's Office had received. That agreement was reported to the Comptroller's Office as having been executed in tax year 2003. Comptroller's Office staff asserted that they were unable to obtain a copy through an open records request because neither the school district nor the school district's consultant provided an executed agreement when requested.
- The Comptroller's Office was uncertain about whether it had received copies of all amendments to agreements. The Comptroller's Office relied on school districts to notify it when they had amended agreements.

The Comptroller's Office should ensure that agreements include certain provisions required by statute and provisions to protect the interests of taxpayers, school districts, and the State.

Auditors reviewed a sample of 47 agreements (including the 7 agreements audited), and identified the following:

- While most statutorily required provisions were included in agreements, two statutorily required provisions were not consistently included in agreements:

- ♦ Effective June 22, 2010, statute required businesses to obtain written approval from the Comptroller's Office and school districts to add new property under an agreement. That requirement was applicable to 28 agreements tested, but none of those 28 agreements contained provisions for that requirement.
- ♦ Effective June 19, 2009, statute restricted the total amount of supplemental payments a business could pay a school district to an amount equal to \$100 per student per year in average daily attendance. That requirement was applicable to 31 agreements tested, but 3 (10 percent) of those 31 agreements did not include provisions for that requirement.
- The agreements reviewed did not consistently include provisions that ensured accountability and transparency. Specifically:
 - ♦ **Compliance.** Nineteen (40 percent) of the 47 agreements did not include a provision that described the agreed-upon performance targets for capital investment amounts, the description and address of the property, the number of jobs to be created, and the periodic deliverables that would be used to evaluate compliance with those requirements. That information was included in the applications, rather than in the agreements.
 - ♦ **Tax credits issued to businesses.** Five (11 percent) of the 47 agreements did not describe how the school districts would determine and issue tax credits to the businesses.
 - ♦ **Transferring an agreement to a new business.** Forty (85 percent) of the 47 agreements did not require the school district to determine the eligibility of any new business to which an existing agreement would be transferred. The agreements reviewed include provisions that either (1) required that the school district's board approve any transfer of an agreement to a new business or (2) required only that the school district be notified that an agreement was transferred.
 - ♦ **Access to business records.** Nineteen (40 percent) of the 47 agreements did not establish the Comptroller's Office's right to audit. In addition, 41 (87 percent) of the agreements tested did not establish the State Auditor's Office's right to audit.

The Comptroller's Office should use property tax information that it collects from county appraisal districts to verify information that businesses and school districts report.

Each tax year, county appraisal districts report information that has been certified by applicable school districts on property values, property tax rates, property tax amounts, and property tax revenue losses for properties that are

covered by agreements to the Comptroller's Office's Property Tax Assistance Division. However, the Comptroller's Office's process does not use that information to verify the accuracy and completeness of property value information that businesses and school districts included in biennial progress reports. The Comptroller's Office's economic development and analysis division uses those biennial progress reports to develop the reports that statute requires it to provide to the Legislature each session. See Chapter 2-D for more information on those required reports.

Recommendations

The Comptroller's Office should implement the following recommendations or seek legislative authority, if necessary, to:

- Obtain and reconcile information from school districts and county appraisal districts on property under agreements, including property locations, property values, and property tax payments.
- Obtain and post on its Web site copies of tax credit applications from all school districts that have processed tax credits through December 2013.
- Establish a process to obtain and post on its Web site copies of all tax credit applications that school districts have processed.
- Obtain copies of all agreements, including any amendments.
- Establish a process to ensure that all agreements include applicable required provisions.
- Adopt rules that require agreements to include provisions that:
 - ♦ Define performance requirements (1) that school districts must include in their agreements with businesses and (2) for which school districts should review compliance on an annual basis.
 - ♦ Define the process to determine tax credit amounts and the requirements a business must meet to receive a tax credit.
 - ♦ Specify that the Comptroller's Office must approve the transfer of agreements from one business to another business. That approval should be based on determining whether a business that will receive an agreement is eligible to have an agreement under Texas Tax Code, Chapter 313.
 - ♦ Ensure that the Comptroller's Office and the State Auditor's Office have access to records the business maintains.

The Comptroller's Office Should Define Its Process for Reviewing Applications for Agreements, Including Its Methodology for Evaluating Economic Impact

The Comptroller's Office should document its process for economic impact evaluation.

The Comptroller's Office reviewed each application for an agreement it received for eligibility, and it also made a recommendation to approve or disapprove each application for an agreement. However, it did not document (1) the process it used to determine whether an application was complete and (2) the factors it considered when it determined whether to recommend an application for an agreement.

Since the enactment of Texas Tax Code, Chapter 313, the Comptroller's Office has had a role in reviewing each application for an agreement and making a recommendation to the school district regarding whether an application should receive an agreement. The extent of the Comptroller's Office review has evolved since the enactment of that statute.

The Comptroller's Office should maintain documentation to show how it assessed the validity of each business's response regarding its ability to locate or relocate to another state or country.

In its economic impact evaluation, the Comptroller's Office did not document its assessment of businesses' responses to questions in applications concerning whether they had the ability to locate or relocate to another state or country. In the evaluations, the Comptroller's Office's recommendations quoted the applicants' responses to that question.

One of the purposes of Texas Tax Code, Chapter 313, is to attract new, large-scale businesses that are exploring opportunities to locate in other states or countries. However, the Comptroller's Office did not have documentation to support how it determined that an agreement with a business would fulfill that purpose.

The Comptroller's Office does not have an interagency agreement with TEA for evaluating school finance reports.

The Comptroller's Office did not document in an interagency agreement (1) its delegation of the evaluation of school finance reports to TEA and (2) the scope and methodology of TEA's school finance evaluations.

As part of its economic impact evaluation, the Comptroller's Office is required to assess a school district's projection of an agreement's effect on state funding for each year of an agreement. Documenting its understanding with TEA could help the Comptroller's Office to ensure that the criteria and other factors TEA uses align with the requirements of Texas Tax Code, Chapter 313.

Recommendations

The Comptroller's Office should document and where necessary establish:

- The procedures and criteria it uses to determine whether an application for an agreement is complete and the factors it uses to determine whether to recommend an application for an agreement.
- Its methodology for evaluating the reasonableness and validity of (1) applicants' and school districts' responses to questions on applications for agreements and (2) the associated economic impact evaluation.
- An interagency agreement describing any assistance TEA provides in reviewing applications for agreements, including the methodologies that TEA will follow.

Chapter 2-C

The Comptroller's Office Should Ensure That the Tax Credits School Districts Issue to Businesses Are Appropriate and Comply with Statute

The Comptroller's Office repealed rules that school districts were formerly required to follow when they processed tax credit applications.

Effective June 2014, the Comptroller's Office repealed rules that school districts were formerly required to follow when they issued tax credits to businesses. House Bill 3390 (83rd Legislature, Regular Session) removed provisions that allowed businesses to receive a tax credit. As a result, businesses are not entitled to tax credits on new agreements executed on or after January 1, 2014.

However, there are approximately 242 executed agreements and 57 applications for agreements that may be entitled to an estimated \$786 million in tax credits from tax year 2014 through tax year 2030. TEA must continue to provide additional state aid to school districts that are entitled to that aid for issuing tax credits to businesses. In addition, school districts that have not yet issued tax credits, but will need to issue tax credits in the future, will continue to need guidance.

Recommendation

The Comptroller's Office should document and communicate to school districts the methodology for calculating tax credits and the requirements for reporting and documenting tax credits.

Chapter 2-D

The Comptroller's Office Complied with Statutory Reporting Requirements

The Comptroller's Office's January 2013 *Report of the Texas Economic Development Act* accurately reported the information that the Comptroller's Office received from school districts for a sample of 20 agreements that auditors selected for testing.

Texas Tax Code, Chapter 313, requires the Comptroller's Office to prepare a report that assesses the progress of each agreement based on certified data that school districts and businesses provide. The Comptroller's Office submits that report to the Lieutenant Governor, the Speaker of the House of Representatives, and each member of the Legislature before the beginning of each regular session of the Legislature.

Chapter 2-E

The Comptroller's Office Should Improve Its Conflict of Interest Policy

Auditors did not identify any conflicts of interest among the Comptroller's Office staff involved in reviewing applications and agreements. However, the Comptroller's Office's ethics policy did not require staff to disclose potential conflicts of interest that they may have with staffs of school districts (including school districts' consultants) and the businesses that apply for agreements.

The Comptroller's Office's ethics policy requires staff to disclose only their outside employment. By also requiring staff to disclose other business and professional relationships that may create a conflict of interest or affirm that no conflicts exist, the Comptroller's Office could enhance the objectivity of its application review process.

Recommendation

The Comptroller's Office should require management and staff to affirm that conflicts of interests do not exist for each application and agreement they review or document any potential conflicts of interest that may exist.

Management's Response from the Comptroller's Office

| | | |
|-----------------------|-----------------------|---|
| S U S A N | C O M B S | TEXAS COMPTROLLER <i>of</i> PUBLIC ACCOUNTS |
| | | P.O. Box 13528 • AUSTIN, TX 78711-3528 |



November 10, 2014

Willie J. Hicks, CGAP, MBA
Managing Senior Auditor
State Auditor's Office
1501 N. Congress Ave.
Austin, Texas 78701-1418

Dear Mr. Hicks:

Enclosed is our response to your findings from the State Auditor's Office revised draft report on selected major agreements under the Texas Economic Development Act received Oct. 28, 2014.

We appreciate the work performed by you and your audit team. Please let us know if we can be of further assistance.

Sincerely,

A handwritten signature in black ink, appearing to read "Martin A. Hubert", is written over a horizontal line.

Martin A. Hubert
Deputy Comptroller

Enclosure

cc: Robin Smith, Director, Internal Audit
Robert Wood, Director, Economic Development & Analysis

WWW.WINDOW.STATE.TX.US

512-463-4000 • TOLL FREE: 1-800-531-5441 • FAX: 512-463-4965

Comptroller's Office Management Response to Revised SAO Draft Report Received
October 28, 2014, An Audit of Major Agreements Under the Texas Economic
Development Act

Management responses to Chapter 2-A

Management concurs with the recommendation to obtain and reconcile information from school districts and county appraisal districts on property under agreements and will propose rules to implement this recommendation.

Management concurs with the recommendation to post tax credit applications processed by districts.

Management concurs with the recommendation to establish a process to obtain and post copies of tax credit applications that school districts process.

Management concurs with the recommendation to obtain all copies of agreements, including any amendments and has partially implemented this recommendation via authority provided in HB 3390 and through amendments to TAC effective June 2, 2014. All amendments are now required to be approved by the agency prior to approval by the district. Management will provide guidance to districts to remind them to provide copies of amendments executed in the past.

Management acknowledges that Beaumont ISD has not provided an executed copy of one agreement. That agreement was executed in 2003, when the agency's responsibilities under the statute were significantly less than they are today, and prior to the Legislature authorizing the agency to require copies of the agreements between districts and companies. The agency has copies of all other agreements, and agrees to continue to seek the one missing agreement from 2003.

Responsible Party: Economic Development and Analysis Manager

Expected Implementation Date: March 1, 2015

Management concurs with the recommendation to ensure that all agreements include applicable provisions, and has implemented this recommendation via authority provided in HB 3390 and through amendments to TAC effective June 2, 2014. The agency has promulgated a form agreement containing applicable required provisions for all agreements resulting from applications received after the effective date of HB 3390, January 1, 2014.

Management concurs with the recommendation to define performance requirements (1) that school districts must include in their agreements with businesses and (2) for which school districts should review compliance on an annual basis and has implemented this recommendation via authority provided in HB 3390 and through amendments to TAC effective June 2, 2014. The agency has promulgated a form agreement containing applicable required provisions for all agreements resulting from applications received after the effective date of HB 3390, January 1, 2014.

Responsible Party: Economic Development and Analysis Manager

Actual Implementation Date: June 2, 2014

Management agrees that determining tax credit amounts and the requirements for receiving a tax credit should be clear. The agency will provide additional guidance to districts regarding their obligations under Chapter 313, and appropriate guidance for districts to determine and companies to be eligible to receive a tax credit. Agreements executed after the effective date of HB 3390 (January 1, 2014) are not eligible for a tax credit. The repeal of "Subchapter D. School Tax Credits" in the statute and subsection (k) in the rules did not affect the rights and obligations in agreements executed prior to the repeal. It is unclear whether the agency can promulgate or adopt new amendments to agency rules that pertain to a section of statute that was repealed in HB 3390. Management notes that the repealed rule is still the appropriate guide for school districts, and further action is not required in rule. School districts can still obtain the methodology and requirements from the archived rules that are easily accessible on the agency website.

Responsible Party: Economic Development and Analysis Manager

Expected Implementation Date: March 1, 2015

Management concurs with the recommendation that the Comptroller's office must approve the transfer of agreements from one business to another business, and through authority provided in HB 3390 and through amendments to TAC effective June 2, 2014, requires that all amendments, including transfers, to agreements resulting from applications received after the effective date of HB 3390, be subject to agency approval prior to approval by the district.

Responsible Party: Economic Development and Analysis Manager

Actual Implementation Date: June 2, 2014

Management concurs with the recommendation to ensure that the Comptroller's office and the State Auditor's Office have access to records the business maintains and has implemented this recommendation via authority provided in HB 3390 and through amendments to TAC effective June 2, 2014. The agency has promulgated a form agreement containing applicable required provisions for all agreements resulting from applications received after the effective date of HB 3390, January, 1, 2014.

Responsible Party: Economic Development and Analysis Manager

Actual Implementation Date: June 2, 2014

Management responses to Chapter 2-B

Management concurs with the recommendation to document the procedures and criteria it uses to determine whether an application for an agreement is complete and the factors it uses to determine whether to recommend an application for an agreement and notes that this recommendation has been implemented through TAC rules and forms effective June 2, 2014 that provide the factors used.

Management concurs with the recommendation to document its methodology for evaluating the reasonableness and validity of (1) applicants' and school districts' responses to questions on applications for agreements and (2) the associated economic impact evaluation, as they relate to evaluation of responses related to businesses' ability to locate or relocate to another state or country, and has implemented this recommendation via authority provided in HB 3390 and through amendments to TAC effective June 2, 2014.

Responsible Party: Economic Development and Analysis Manager

Actual Implementation Date: June 2, 2014

Management concurs with the recommendation to document an interagency agreement describing any assistance TEA provides in reviewing applications for agreements, including the methodologies that TEA will follow, and will enter into an interagency agreement should TEA provide assistance in application review, however, House Bill 3390 revised the requirements for Chapter 313 applications and there is no current requirement for ongoing TEA assistance in the process.

Responsible Party: N/A

Expected Implementation Date: N/A

Management responses to Chapter 2-C

Management concurs with the recommendation to document and communicate to school districts the methodology for calculating tax credits and the requirements for reporting and documenting tax credits. The agency will provide additional guidance for districts in calculating tax credits and the requirements for reporting and documenting tax credits.

Responsible Party: Economic Development and Analysis Manager

Expected Implementation Date: March 1, 2015

Management responses to Chapter 2-E

Management agrees to implement the SAO recommendation that the Comptroller's office should require management and staff to affirm that conflicts of interests do not exist for each application and agreement they review or document any potential conflicts of interest that may exist. Management notes that the audit states that auditors did not identify any conflicts of interest among the Comptroller's office staff involved in reviewing applications and agreements. Management further notes that the agency has an ethics policy in place, and requires ethics training for all employees biennially.

Responsible Party: Economic Development and Analysis Manager

Expected Implementation Date: December 31, 2014

TEA Should Improve Certain Processes for Determining Additional State Aid Provided to School Districts That Issue Tax Credits and Evaluating School District Financial Projections

TEA should maintain sufficient documentation to show that additional state aid provided to school districts was accurate and appropriate (see text box for more information on additional state aid provided to school districts). TEA

also should strengthen its conflict of interest policy and establish a methodology for evaluating the effect of agreements on school districts' facilities.

Additional State Aid for Tax Credits Issued Under Texas Tax Code, Chapter 313

TEA provides additional state aid to school districts that issue tax credits to businesses with agreements, as specified by the following:

- House Bill 1200 (77th Legislature, Regular Session) enacted the Texas Economic Development Act (Texas Tax Code, Chapter 313). Section 6 of House Bill 1200 amended Texas Education Code, Chapter 42, by adding Section 42.2515, which entitled a school district to additional state aid in an amount equal to the amount of all tax credits credited against property taxes of the school district that were subject to Texas Tax Code, Chapter 313.
- Title 34, Texas Administrative Code, Section 9.1057(c), stated that the Comptroller's Office shall investigate any determination made by the governing body of the school district or TEA that a business was not entitled to a tax credit or was entitled to a lesser amount than the business actually received. The Comptroller's Office repealed that administrative rule effective June 2014. See Chapter 2-C for more information.
- TEA's administrative rules described under Title 19, Texas Administrative Code, Section 61.1019(a), the rules for implementing Texas Education Code, Section 42.2515, and specifies that a school district must apply to TEA in order to receive additional state aid equal to the tax credits issued under Texas Tax Code, Chapter 313.

In addition, the TEA form that school districts complete to request additional state aid for property tax credits specifies that school districts must be in compliance with all the reporting requirements set forth in the rules and policies of the Comptroller's Office under the Tax Code, Section 313.031, and the administrative rules in Title 19, Texas Administrative Code, Section 61.1019.

Finally, Texas Tax Code, Section 313.103(2)(b), specified that any information that a school district provides to TEA under Texas Education Code, Section 42.2515, is not confidential. House Bill 3390 (83rd Legislature) repealed that provision effective January 1, 2014.

Chapter 3-A

TEA Should Improve Its Processes for Determining Additional State Aid Related to Tax Credits

TEA should revise the advice it previously provided to school districts to help ensure compliance with the method described in statute for issuing tax credits.

Texas Tax Code, Chapter 313, requires that tax credits be applied to the future tax bills of a business that has an agreement. Specifically, Texas Tax Code, Section 313.104(2) which was repealed by House Bill 3390 (83rd Legislature), required a school district to direct the county tax collector to assess tax credits against the property taxes owed by the business. However, TEA advised school districts to make direct payments to businesses for those tax credits. (TEA's process for reviewing requests for additional state aid also included verifying that school districts provide it with copies of checks showing the tax credits the school districts had paid to businesses.) As a result of TEA's advice, most school districts paid tax credits directly to businesses, which was not consistent with statute.

TEA's process for providing additional state aid related to tax credits should include maintaining consistent documentation to support the accuracy and appropriateness of tax credits that school districts paid to businesses.

Auditors tested 59 (49 percent) of the 120 requests for additional state aid totaling \$11.5 million that TEA paid to school districts and determined that TEA's process did not have sufficient documentation to support:

- The eligibility of school districts to receive additional state aid for all 59 requests tested. Specifically:
 - ♦ For 8 requests tested, TEA did not consistently obtain copies of school board resolutions to approve businesses' applications for tax credits as required by TEA policies.
 - ♦ For the 59 requests tested, there was no documentation to show that school districts had complied with the Comptroller's Office's reporting requirements as specified in TEA's administrative rules.
- The accuracy of payment amounts for 17 requests.
- Whether 17 requests were submitted by the required due dates. Those payments are not necessarily the same as the payments discussed immediately above.
- Validating a school district's reason for issuing a tax credit to a business with a name other than the business named on the agreement for 14 requests.
- Whether school districts made tax credit payments to the businesses for 6 requests.
- Whether businesses submitted to school districts completed or signed tax credit applications for 3 requests.

In addition, TEA relies on school districts to certify that they have complied with the Comptroller's Office's rules for tax credits. Those rules specify that a school district must determine that a business receiving a tax credit is in full compliance with the agreement. The school districts audited that made tax credit payments to businesses relied primarily on information the businesses provided. See Chapters 1, 4-D, 5-D, and 7-D for more information related to tax credits.

Recommendations

TEA should:

- Ensure that guidance concerning the issuance of tax credits that it provides to school districts that are eligible to receive additional state aid aligns with the applicable requirements in Texas Tax Code, Chapter 313.
- Obtain and maintain documentation to show that, for additional state aid paid to school districts, it verifies that tax credit amounts are accurate and issued to eligible businesses, or seek statutory changes.

TEA Should Improve Its Conflict of Interest Policy

TEA's ethics policy did not require staff involved in evaluating school financial projections or processing requests for additional state aid to disclose potential personal or financial conflicts of interest that they may have with agreements and school districts' school board members, staff, and consultants.

TEA's ethics policy requires all agency staff to disclose only family relationships and outside employment or compensation. By also requiring staff to disclose potential conflicts of interest related to personal or financial relationships, or affirm that no conflicts exist, TEA could enhance the transparency of its evaluation of application information and processing of requests for additional state aid. In addition, increased transparency would provide the Comptroller's Office with added assurance that TEA's independence and professional judgment are not impaired or influenced by personal or financial interests. The Comptroller's Office uses the evaluations that TEA staff perform in determining whether to recommend an application for an agreement.

Recommendation

TEA should review its ethics policy to determine whether enhanced disclosure would improve the transparency of the management and staff involved in evaluating applications and processing requests for additional state aid.

TEA Should Develop and Document a Methodology for Determining the Effect of an Agreement on a School District's Facilities

TEA performed evaluations to determine the effect of an agreement on a school district's facilities, as statutorily required. However, TEA relied on financial projections that school districts provided (which were developed by the school districts' consultants) to determine that effect.

Auditors tested 28 applications for which TEA relied on those financial projections and determined that TEA's methodology involved contacting the school district to confirm that the school district agreed with the financial projections that it provided to TEA.

Recommendation

TEA should develop and document a methodology to determine the reasonableness of economic conditions and other factors presented in a school district's financial projections for how an agreement may affect the school district's facilities.

Management's Response from TEA



1701 North Congress Ave. • Austin, Texas 78701-1494 • 512 463-9734 • 512 463-9838 FAX • www.tea.state.tx.us

Michael Williams
Commissioner

Texas Education Agency Management Response to the State Auditor's Office Report on Selected Major Agreements under the Texas Economic Development Act

Recommendation 3-A: TEA should improve its process for determining additional state aid related to tax credits:

- TEA should ensure that guidance concerning the issuance of tax credits that it provides to school districts that are eligible to receive additional state aid aligns with the applicable requirements in Texas Tax Code Chapter 313.

Agency staff currently advise school districts to collect full tax payments from companies and subsequently reimburse the amount of the tax credit due. This method allows for verification of the amount of the tax credit by Agency staff prior to reimbursement under §42.2515 of the Texas Education Code. Modifying the process to require a school district to direct the county tax collector to assess tax credits against the property taxes owed by the business would make it harder for TEA staff to verify accurate tax credits and therefore reimbursements, particularly given varying reporting methodologies across taxing entities.

Agency staff have not received any complaints related to the current process from either school districts or businesses and recommend statute be modified to allow the current practice to continue.

- TEA should obtain and maintain documentation to show that, for additional state aid paid to school districts, it verifies that tax credit amounts are accurate and issued to eligible businesses, or seek statutory changes.

TEA staff collect a number of documents to verify the calculation of tax credits and eligibility of districts for tax credits including a copy of the contract, a copy of the tax statement, and a copy of the tax receipt. Since 2012, TEA has also required school districts to verify that they are in compliance with comptroller rules. We have seen no evidence that an inaccurate payment has been made that needs to be corrected. TEA staff will modify processes to ensure more consistent maintenance of all documentation. TEA will also seek to modify our process by requesting verification from the Comptroller's office that districts are in compliance with Chapter 313 before making payments. TEA has no independent statutory authority to enforce compliance with Chapter 313.

TEA Staff Responsible: Nancy Kuhn and Amanda Brownson

Recommendation 3-B: TEA should improve its conflict of interest policy.

- TEA should review its ethics policy to determine whether enhanced disclosure would improve the transparency of the management and staff involved in evaluating applications and processing requests for additional state aid.

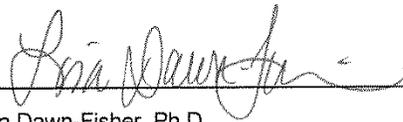
TEA has reviewed its ethics policy and determined that it currently has conflict-of-interest policies that go well beyond requirements set forth in statute, which generally require staff to disclose business interests or ownership related to an entity that is doing business with or being regulated by the state agency where the staff is employed. There are no statutory requirements that require staff to affirm that no conflicts exist.

Recommendation 3-C: TEA should develop and document a methodology for determining the effect of an agreement on a school district's facilities.

- TEA should develop and document a methodology to determine the reasonableness of economic conditions and other factors presented in financial projections for how an agreement may affect the school district's facilities.

TEA staff currently contact the board of trustees from each school district that submits an application reflecting anticipated job growth of more than 10 new jobs. Since TEA does not have data regarding the current capacity of school district facilities nor any independent information related to the economic circumstances in each school district, staff relies on information provided by local officials in making a determination of the impact of economic development projects on school district facilities. TEA will document this methodology and maintain information related to district response to facilities questions.

TEA Staff Responsible: Al McKenzie and Amanda Brownson



Lisa Dawn-Fisher, Ph.D.

Associate Commissioner

School Finance/Chief School Finance Officer

Austin Independent School District Agreement with Hewlett-Packard Company

| Background Information on the Audited Agreement with the Austin Independent School District ^a | |
|--|---|
| Business | Hewlett-Packard Company |
| Application number | 40 |
| Business category | Research and development |
| County | Travis |
| Term of agreement | January 1, 2007, through December 31, 2019 |
| Appraisal limitation | \$100,000,000 |
| Tax year 2013 appraised value | \$87,334,261 |
| Net tax benefit business received based on the 2012 Biennial Cost Data Request Form | \$133,904 |
| Number of qualifying jobs created as reported by the business (as of December 31, 2013) | 22 |
| Total tax credits business is eligible to receive | \$419,447 |
| Other tax abatements and other economic development incentives business received | Property tax abatements from Travis County and the City of Austin |
| Revenue protection payments school district received from business (as of December 31, 2013) | \$21,291 |
| Payments in lieu of taxes school district received from business (as of December 31, 2013) | \$96,964 |
| ^a See Appendix 2 for more detailed information. | |

Sources: The Office of the Comptroller of Public Accounts, Austin ISD, and the Travis Central Appraisal District.

This report chapter covers the appraisal limitation agreement (agreement) between the Austin Independent School District (Austin ISD) and Hewlett-Packard Company. Hewlett-Packard Company certified to Austin ISD through its submission of annual eligibility forms and biennial progress reports that it complied with certain requirements of Texas Tax Code, Chapter 313. Austin ISD accepted those submissions. As discussed in Chapter 1, statute does not require school districts to verify that information, and Austin ISD did not perform verifications.

Auditors determined that Austin ISD executed the agreement in compliance with Texas Tax Code, Section 313.027.

The maximum property value on which property covered by the agreement with Hewlett-Packard Company can be taxed for the maintenance and operations portion of property taxes is \$100,000,000. As of December 31, 2013, the appraised value of that property was \$87,334,261.

Table 1 provides information on the appraised value of the property under the agreement.

Table 1

| Hewlett-Packard Company Property Appraised Value Compared to Appraisal Limitation Value January 2007 through December 2013 | | | |
|--|----------------|-----------------|---|
| Tax Year | Agreement Year | Appraised Value | Appraisal Limitation Value ^a (Taxable Value for Maintenance and Operations Property Taxes Purposes) |
| 2007 | 1 | \$ 19,700,480 | No limitation |
| 2008 | 2 | \$138,873,635 | No limitation |
| 2009 | 3 | \$122,420,110 | \$100,000,000 |
| 2010 | 4 | \$100,949,551 | \$100,000,000 |
| 2011 ^b | 5 | \$ 76,451,469 | \$100,000,000 |
| 2012 | 6 | \$ 71,399,768 | \$100,000,000 |
| 2013 | 7 | \$ 87,334,261 | \$100,000,000 |

^a The appraisal limitation became effective in the third year of the agreement and applies only to the maintenance and operations portion of the school district's property tax. The property remains fully taxable for purposes of any school district debt service tax during the term of the agreement.

^b When the appraised value became less than the appraisal limitation, the appraised value was used to determine the maintenance and operations property tax amount for tax years 2011, 2012, and 2013.

Sources: The Travis Central Appraisal District and Austin ISD.

The remainder of this chapter provides information on the following:

- Processing applications for agreements.
- Developing agreements.
- Monitoring compliance.
- Processing tax credits.
- Disclosing conflicts of interest.
- Opportunities to improve certain administrative processes.

Processing Applications for Agreements

Austin ISD relied primarily on information provided in Hewlett-Packard Company's application.

Application for Appraisal Limitation

Hewlett-Packard Company submitted its application to the Austin ISD board of trustees on April 24, 2006. The application included:

- An application fee of \$75,000.
- Survey maps of the proposed property.
- A summary of the school finance impact of the proposed appraisal limitation value prepared by the school district's consultant.
- An economic impact report prepared by a subcontractor of the consultant.

Austin ISD submitted the application to the Comptroller's Office as required by statute. The Comptroller's Office issued its recommendation letter to Austin ISD on October 19, 2006.

The Austin ISD board of trustees issued its findings related to the impact of the Hewlett-Packard Company appraisal limitation on the school district as required by statute and approved the agreement on November 6, 2006.

Sources: The Comptroller's Office and Austin ISD.

Austin ISD documented its determination of how an agreement with Hewlett-Packard Company would comply with the intent and purpose of Texas Tax Code, Chapter 313. (See text box for additional information about the Hewlett-Packard Company application and Appendix 4 for specific statutory requirements.) To make that determination, Austin ISD relied primarily on certified information that Hewlett-Packard Company provided in its application for an agreement. Examples of that information included:

- The types of jobs that Hewlett-Packard Company committed to create.
- The number of each type of job.
- The wages to be paid for each job.
- The employee benefits to be offered.

- The ability of the business to locate or relocate in another state or another region of the state.

Texas Tax Code, Section 313.025(f), states that a school district may approve an application only if it finds that the information in the application is true and correct, finds that the applicant is eligible for the limitation on the appraised value, and determines that granting the application is in the best interest of the school district and the State.

Developing Agreements

The agreement did not include provisions that described the agreed-upon capital investment amount, certain property information, and the number of jobs to be created.

Austin ISD ensured that the agreement included provisions that complied with statute and that its board of trustees approved the agreement. However, the agreement did not include certain provisions to enable Austin ISD to ensure accountability and transparency.

The agreed-upon capital investment amount that Hewlett-Packard Company committed to make, the description and address of the property to be covered by the agreement, and the anticipated number of jobs to be created were documented in the application, rather than in the agreement. However, the agreement did not explicitly state that the application was part of the agreement.

Texas Tax Code, Section 313.027(e), requires agreements to describe with specificity the capital investment that a business will make on or in connection with the property that is subject to the appraisal limitation. Other property that is not specifically described in the agreement is not subject to the limitation unless the governing body of the school district, by official action, provides that the other property is subject to the limitation.

The agreement did not include a completed exhibit of agreed-upon appraisal values for property improvements.

The agreement included an exhibit that was intended to describe the agreed-upon taxable property values for improvements made to the property. Section 2.4 of the agreement stated that the exhibit would show the agreed-upon values that would be necessary to determine the appraised value of new construction that is affixed to, or is a modification or alteration of, pre-existing improvements that are separate and distinct from pre-existing improvements. However, that exhibit did not include the property values for land, improvements, and personal property for tax years 2007 through 2016 (the term of the agreement.) The fields for those amounts were left blank in the exhibit.

A provision of the agreement allowed the agreement to be transferred to a new business, but it did not specify that the new business must meet Texas Tax Code, Chapter 313, eligibility requirements.

The agreement allowed Hewlett-Packard Company to transfer the agreement to another business. Specifically, Section 6.5 of the agreement states:

[Hewlett-Packard Company] may assign [the agreement], or a portion of [the agreement], to a new applicant or lessee of the [property under agreement] upon the written approval of the District, and approval shall not be unreasonably withheld. It shall not be unreasonable for the [school district] to withhold approval if the [Hewlett-Packard Company] is liable to the District for outstanding taxes or other obligations arising under the agreement.

Although Austin ISD must approve the transfer of the agreement to a new business, the agreement did not specify that the new business must be eligible to receive an agreement. As a result, there is a risk that the agreement could be transferred to a business that does not meet the eligibility requirements in Texas Tax Code, Chapter 313.

The agreement did not include any performance standards or require periodic deliverables to enable Austin ISD to monitor compliance.

The agreement did not include provisions that would enable Austin ISD to monitor and evaluate Hewlett-Packard Company's compliance with its agreement or statutory requirements for capital investment or job creation. Without specifying performance standards or periodic deliverables to monitor progress, Austin ISD did not have a defined methodology to obtain assurances that Hewlett-Packard Company fulfilled the requirements of the agreement and complied with Texas Tax Code, Chapter 313.

Recommendations

Austin ISD should consider amending existing agreements to include:

- All required provisions and information related to the agreed-upon investment amounts, the description and address of the property, and the anticipated number of jobs to be created; alternatively, it should explicitly state in agreements that the information in the related applications is incorporated into the agreements.
- Provisions that require Austin ISD to assess the eligibility of any business to which an agreement is transferred.
- Performance standards or requirements for businesses to periodically submit deliverables that will enable it to hold businesses accountable for achieving desired results.

Chapter 4-C

Monitoring Compliance

Austin ISD relied primarily on information that Hewlett-Packard Company reported on annual eligibility reports and biennial progress reports.

Hewlett-Packard Company submitted annual eligibility reports and biennial progress reports to Austin ISD as required by the Comptroller's Office. (See Appendix 7 for more information on required progress reports that businesses submit.) As discussed in Chapter 1, statute does not require school districts to verify the information on annual eligibility reports and biennial progress reports, and Austin ISD did not perform verifications.

Examples of the information that Hewlett-Packard Company submitted included:

- The number of jobs created.

- Whether the number of jobs created complied with statutory requirements. (Businesses with agreements are required to create **qualifying jobs**. See Appendix 7 for more information on job-creation requirements.)
- Capital investment amounts. (Businesses are required to make certain capital investments, or **qualified investments**, in personal property that will be used with property under an agreement. See Appendix 7 for more information on qualified investments.)
- Property values and descriptions for real and personal property covered by the agreement. (Correctly identifying the property and property values is significant to ensuring that property tax losses resulting from agreements are calculated accurately because those tax losses affect the amount of state funding a school district receives each tax year.)

The annual eligibility reports and biennial progress reports provided inconsistent information.

Auditors identified inconsistencies among the agreement and the annual eligibility reports and biennial progress reports that Hewlett-Packard Company submitted to Austin ISD for tax years 2009 through 2012. Specifically:

- Hewlett-Packard Company reported in its biennial progress report for tax year 2010 that it had created a total of 38 qualifying jobs in tax year 2009. However, its annual eligibility report specified that it had created 6 qualifying jobs for tax year 2009. In addition, its biennial progress report for tax year 2012 specified that Hewlett-Packard Company had created 11 qualifying jobs for tax years 2009 and 2010. However, for tax year 2010, the annual eligibility report specified that Hewlett-Packard Company had created 6 qualifying jobs.
- Hewlett-Packard Company reported in its annual eligibility reports for tax years 2009, 2010, and 2011 that the property qualifying for the appraisal limitation would be used for research and development and manufacturing. However, the agreement stated that the property would be used only for research and development.

The address of the property in the application differed from the address of the property in the county appraisal district's records.

Although Austin ISD notified the Travis Central Appraisal District of the property under the agreement, there were three different property addresses associated with that property. Specifically, the application listed one address and the Travis Central Appraisal District's records showed two addresses, both of which differed from the address in the application. In addition, one of the property addresses in the Travis Central Appraisal District's documentation identified the property as personal property. As a result, it is not clear whether the property covered by the agreement is the same property

that the Travis Central Appraisal District has identified in its records as the property receiving the appraisal limitation.

Recommendation

Austin ISD should ensure that property covered by an agreement is the same property that the Travis Central Appraisal District has identified as the property that received an appraisal limitation.

Chapter 4-D

Processing Tax Credits

Hewlett-Packard Company may be eligible for \$419,447 in tax credits because, during the qualifying period of the agreement, the appraised value of its property exceeded the appraisal limitation value (and the taxes it paid were based on that appraised value). See Appendix 7 for more information on the qualifying period.

Hewlett-Packard Company has not applied to Austin ISD for payment of those tax credits, but it may be eligible to receive those tax credits after the appraisal limitation expires during the tax credit settle-up period. Because school districts may receive additional state aid for tax credits they grant to businesses with which they have agreements, those tax credits may represent liabilities to the State. See Appendix 3 for additional information on tax credits.

Chapter 4-E

Disclosing Conflicts of Interest

Austin ISD complied with its policy for ensuring that members of its board of trustees and employees disclosed business, professional, and personal relationships that could create a potential conflict of interest.

Chapter 4-F

Administrative Processes

Opportunities exist for Austin ISD to strengthen certain administrative processes. While the following issues may not be material to determining compliance with Texas Tax Code, Chapter 313, they are significant to Austin ISD's management of its agreement with Hewlett-Packard Company:

- The agreement did not include a provision describing how tax credits were to be determined and issued to Hewlett-Packard Company.

- The agreement required Hewlett-Packard Company to deposit payments in lieu of taxes into an account maintained by Hewlett-Packard Company that Austin ISD would use to purchase information technology-related products and services. Instead, however, Hewlett-Packard Company made direct payments to Austin ISD. For tax years 2007 through 2013, those payments totaled \$96,964, and Austin ISD could not provide documentation to show how it spent those funds.
- Austin ISD did not initially create a statutorily required link on its Web site to the Comptroller's Office Web site as required by Texas Tax Code, Section 313.0265(c). After auditors brought this issue to its attention, Austin ISD created the required link on its Web site.

Recommendations

Austin ISD should:

- Include in agreements provisions requiring tax credits to be applied against the future property taxes imposed on the property subject to the agreement.
- Comply with agreement provisions related to making payments in lieu of taxes or amend the agreement to reflect the actual payment terms.

Management's Response from Austin ISD

Austin Independent School District

Office of the Superintendent



Formal Management Response

Austin Independent School District

Report on the Audit of Major Agreements under
the Texas Economic Development Act

November 11, 2014

State Auditor's Office
ATTN: Mr. Willie Hicks
P.O. Box 12067
Austin, Texas 78711-2067

Dear Mr. Hicks:

In our response to your Audit of Major Agreements under the Texas Economic Development Act, we want to go on the record with some general comments of our perception of the program. We will then address the specific recommendations made to Austin ISD by topic within the Report.

General Comments:

The District is not responsible for the design of compliance mandates; it is a state responsibility.

As a preliminary matter, the District views Chapter 313 of the Texas Tax Code and the rules adopted to implement Chapter 313 as a state program which, under such rules, is administered in part by the District. In order to ensure uniformity in the administration of the program, this District does not feel it is authorized to impose new and independent obligations on the recipients of the program. Section 313.032(a) specifically authorizes the required Comptroller's report to be "...based on data certified to the Comptroller by each recipient of a limitation on appraised value under this subchapter...." In adopting such provisions, the Texas Legislature created a system designed to rely upon the disclosure of information directly from the applicant for a tax limitation.

From the tenor of the specific comments discussed below, it is apparent that the State Auditor's Office is not satisfied with the applicants' reporting requirements and has consistently sought to impose new and unauthorized verification requirements on Austin ISD. Keeping in mind the admonitions set forth in Texas Tax Code 313.004(3)(A) that school districts strictly interpret the criteria set forth in Chapter 313, Austin ISD is reluctant to impose new requirements on Chapter 313 applicants in excess of those set forth in statute or state-agency-adopted administrative rule. Please be advised that this District will enforce any requirement legitimately adopted with respect to Chapter 313 agreements. In the absence of such adoption, this District feels compelled to apply the rules and statutes as they are written.

1111 West 6th Street Austin, Texas 78703-5300 (512) 414-1700

Chapter 4-B Developing Agreements

Recommendation

Austin ISD should consider amending existing agreements to include:

- *All required provisions and information related to the agreed-upon investment amounts, the description and address of the property, and the anticipated number of jobs to be created; alternatively, it should explicitly state in agreements that the information in the related applications is incorporated into the agreements.*
- *Provisions that require Austin ISD to assess the eligibility of any business to which an agreement is transferred.*
- *Performance standards or requirements for businesses to periodically submit deliverables that will enable it to hold businesses accountable for achieving desired results.*

Management Response

Management disagrees. Agreements in place contain provisions for the implementation of all the recommendations enumerated by the State Auditor's Office.

In its finding 4-B, the State Auditor's report suggested that the District should consider amending existing agreements to include:

1. All required provisions and information related to the agreed-upon investment amounts, the description and address of the property, and the anticipated number of jobs to be created; alternatively, it should explicitly state in agreements that the information in the related applications is incorporated into the agreements.
2. Provisions that require Austin ISD to assess the eligibility of any business to which an agreement is transferred.
3. Performance standards or requirements for businesses to periodically submit deliverables that will enable it to hold businesses accountable for achieving desired results.

These issues will be discussed serially below:

1. *Provisions related to investment amounts, the description and address of the property and the number of jobs to be created:*

The Agreement already has provision related to each of these requirements. In particular, the required investment amounts are set forth in Sections 1.3 and 3.2(iv) of the agreement define the tax limitation amount as being \$100 Million. At the time of the agreement Tex. Tax Code §§ 313.022(b) and 313.023 required the applicant's minimum Qualified Investment to be \$100 Million. That was the minimum amount of Qualified Investment required by the Agreement. Exhibits 1 and 2 to the Agreement provide a complete legal description of the location of the qualified property. The Travis Central Appraisal District, which is responsible for identifying and locating the location of the Qualified Property, has expressed no difficulty in identifying the property subject to the agreement. At the time of the execution of this agreement at issue in this Audit, Comptroller's rules did not require that the applicant was bound by the number of Qualifying Jobs estimated in its application.

Instead, the applicant was bound by the statutory requirements set forth at Tex. Tax Code §313.021(2)(A)(iv)(b). The statutory requirement is incorporated into the agreement at Section 6.2(b) which requires the applicant to maintain a viable presence in the district, which in conformance with the term's definition in Section 1.3, included the maintenance, over the life of the agreement of the statutorily required number of jobs.

2. *Provisions that require Austin ISD to assess the eligibility of any business to which an agreement is transferred:*

Section 5.1 of the agreement specifically requires that the applicant "shall be obligated to provide the District and the County Appraisal District all data under the Texas Tax Code . . . necessary to determine whether all obligations under the agreement are being met. Section 6.5 requires trustee approval of a transfer. Tex. Tax Code § 313.024(a) requires that Chapter 313 Agreements apply only to "property owned by an entity to which [Tax Code] Chapter 313 applies. However, there has been no transfer of property subject to the 313 agreement in this case. In the event of such a transfer, the Trustees have ample authority to collect the data upon which continuing eligibility determinations can be made. In actual fact, such information is available on the Comptroller's website in the form of certification as active franchise tax paying companies.

3. *Performance standards or requirements for businesses to periodically submit deliverables that will enable it to hold businesses accountable for achieving desired results:*

Annual and biennial reporting requirements are set by Comptroller's rules. The reports as posted provide sufficient information to measure compliance with all current statutory mandates and the express terms of the Agreement.

Chapter 4-C Monitoring Compliance

Recommendation

Austin ISD should ensure that property covered by an agreement is the same property that the Travis County Appraisal District has identified as the property that received an appraisal limitation.

Management Response

Management believes that the property covered by an agreement is the same property that the Travis County Appraisal District has identified.

As stated above, the Travis Central Appraisal District, which is responsible for identifying and locating the location of the Qualified Property, has expressed no difficulty in identifying the property subject to the agreement. The Agreement does anticipate that both personal and real property would be subject to the value limitation, so the fact that the tax statement identified personal property should not be concerning. The Executive Director of Finance will continue to ensure that property covered in an agreement is the same property that the Travis County Appraisal District has identified as the property that received an appraisal limitation. This will be validated by December 31, 2014, and will remain an ongoing process.

Chapter 4-F Administrative Processes

Recommendation

Austin ISD should:

- *Include in agreements provisions requiring tax credits to be applied against the future property taxes imposed on the property subject to the agreement.*
- *Comply with agreement provisions related to making payments in lieu of taxes or amend the agreement to reflect the actual payment terms.*

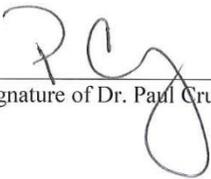
Management Response

Management disagrees. Tax Credit Reimbursement Requests are submitted in conformance with TEA requirements.

While the Hewlett Packard Company has not applied for tax credits, in order for Austin ISD to seek a state reimbursement under Section 42.2515 of the Education Code should a tax credit be owed, the TEA rule calls for the school district to submit “A copy of the tax bill sent to the taxpayer (showing the credit) or other proof that the school has reimbursed the tax credit to the taxpayer.” However, the TEA procedures for the processing of tax credits currently in place require the District to present the Agency with proof of actual payment to the company of the tax credit amount as a prerequisite for reimbursement to the District. Over time, TEA has imposed varying requirements as a precondition of reimbursement. In light of the TEA’s varying standards of compliance, it is imprudent to specify the conditions for payment of tax credit in the Agreement. The District has adopted policy CCG (Local) governing, in part, its obligations for processing tax credits. Those policies, in addition to TEA rules and procedures are sufficient to ensure verification prior to expenditure by the state and ensure that there is an appropriate “audit trail” in making state reimbursements to school districts for tax credits.

Austin ISD and other school districts have experience making tax refunds for overpayments, which is analogous to the tax credits that could be owed to the Hewlett Packard Company under its Chapter 313 Agreement. In the event that Austin ISD is required to pay tax credits to the Hewlett Packard Company in the future, the District is satisfied that the TEA approach implements the statutory goal of providing the tax credit in a manner that would be satisfactory to the District, the Company and the State.

In terms of the payment in-lieu of taxes to Austin ISD, there has been little in the way of tax savings to the Hewlett Packard Company under its Chapter 313 Agreement with Austin ISD. The supplemental payment amounts have been relatively small, especially considering the scale of the Hewlett Packard Company and Austin ISD. Direct payments have been used for administrative simplicity, as opposed to the credit provisions in the original Agreement, and agreed to by both parties to the Agreement.



Signature of Dr. Paul Cruz, Interim Superintendent

11/11/14
Date

Fort Stockton Independent School District Agreements with SandRidge Energy, Inc.

| Background Information on the Two Audited Agreements with the Fort Stockton Independent School District ^a | | |
|---|--|--|
| Business | SandRidge Energy, Inc. | SandRidge Energy, Inc. |
| Application number | 134 | 135 |
| Business category | Manufacturing | Manufacturing |
| County | Pecos | Pecos |
| Term of agreement | January 1, 2009, through December 31, 2021 | January 1, 2009, through December 31, 2021 |
| Appraisal limitation | \$20,000,000 | \$20,000,000 |
| Tax Year 2013 appraised value | \$373,711,430 | \$23,834,130 |
| Net tax benefit business received based on the 2012 Biennial Cost Data Request Form | \$7,590,537 | \$225,465 |
| Number of qualifying jobs created as reported by the business (as of December 31, 2013) | 22 | 2 |
| Total tax credits business is eligible to receive | \$798,365 | \$76,609 |
| Other tax abatements and economic incentives business received | Not reported ^b | Not reported ^b |
| Revenue protection payments school district received from business (as of December 31, 2013) | \$172,946 | \$5,787 |
| Payments in lieu of taxes school district received from business (as of December 31, 2013) | \$4,472,991 | \$98,793 |
| ^a See Appendix 2 for more detailed information. ^b The Pecos County Appraisal District did not respond to auditors' requests for information on other tax abatements and economic development incentives. | | |

Sources: The Office of the Comptroller of Public Accounts, Fort Stockton ISD, and the Pecos County Appraisal District.

This report chapter covers the appraisal limitation agreements (agreements) between the Fort Stockton Independent School District (Fort Stockton ISD) and SandRidge Energy, Inc. SandRidge Energy, Inc. certified to Fort Stockton ISD through its submission of annual eligibility forms and biennial progress reports that it complied with certain requirements of Texas Tax Code, Chapter 313. Fort Stockton ISD accepted those submissions. As discussed in Chapter 1, statute does not require school districts to verify that information, and Fort Stockton ISD did not perform verifications.

Auditors determined that Fort Stockton ISD executed the agreements in compliance with Texas Tax Code, Section 313.027.

The maximum property value on which the properties covered by each of the agreements with SandRidge Energy, Inc. can be taxed for the maintenance and operations portion of property taxes is \$20,000,000. As of December 31, 2013, the appraised values of those properties were:

- \$373,711,430 for the Century Plant property.
- \$23,834,130 for the Grey Ranch property.

Table 2 provides information on the appraised value of the properties under the agreements.

Table 2

| SandRidge Energy, Inc. Property Appraised Values Compared to Appraisal Limitation Values January 2009 through December 2013 | | | | |
|---|----------------|--|---|--|
| Tax Year | Agreement Year | Appraised Value for Century Plant Property | Appraised Value for Grey Ranch Property | Appraisal Limitation Value for Each Agreement ^a (Taxable Value for Maintenance and Operations Property Taxes Purposes) |
| 2009 | 1 | \$0 | \$20,364,510 | No limitation |
| 2010 | 2 | \$96,765,900 | \$27,001,720 | No limitation |
| 2011 | 3 | \$383,843,500 | \$33,949,670 | \$20,000,000 |
| 2012 | 4 | \$365,396,640 | \$25,532,730 | \$20,000,000 |
| 2013 | 5 | \$373,711,430 | \$23,834,130 | \$20,000,000 |

^a The appraisal limitations became effective in the third year of the agreements and applies only to the maintenance and operations portion of the school district's property tax. The property remains fully taxable for purposes of any school district debt service tax during the term of the agreement.

Sources: The Pecos County Appraisal District and Fort Stockton ISD.

The remainder of this chapter provides information on the following:

- Processing applications for agreements.
- Developing agreements.
- Monitoring compliance.
- Processing tax credits.
- Disclosing conflicts of interest.
- Opportunities to improve certain administrative processes.

Processing Applications for Agreements

Fort Stockton ISD relied primarily on information provided in SandRidge Energy, Inc.'s applications.

Applications for Appraisal Limitation

SandRidge Energy, Inc. submitted its applications to the Fort Stockton ISD board of trustees on September 2, 2008. The applications included:

- An application fee of \$87,000.
- Survey maps of the proposed property.
- A summary of the school finance impact of the proposed appraisal limitation value prepared by the school district's consultant.

Fort Stockton ISD submitted the applications to the Comptroller's Office as required by statute. The Comptroller's Office prepared an economic impact report and issued its recommendation letter to Fort Stockton ISD on November 21, 2008, that determined the applications did not meet requirements for a favorable recommendation.

The Fort Stockton ISD school board issued its findings related to the impact of the SandRidge Energy, Inc. appraisal limitations on the school district as required by statute and approved the agreements on December 22, 2008.

Sources: The Comptroller's Office and Fort Stockton ISD.

Fort Stockton ISD documented its determination of how agreements with SandRidge Energy, Inc. would comply with the intent and purpose of Texas Tax Code, Chapter 313. (See text box for additional information about the SandRidge Energy, Inc. applications and Appendix 4 for specific statutory requirements.) To make that determination, Fort Stockton ISD relied primarily on certified information that SandRidge Energy, Inc. provided in its applications for agreements. Examples of that information included:

- The types of jobs that SandRidge Energy, Inc. committed to create.
 - The number of each type of job.
 - The wages to be paid for each job.
 - The employee benefits to be offered.
- The ability of the business to locate or relocate in another state or another region of the state.

Texas Tax Code, Section 313.025(f), states that a school district may approve an application only if it finds that the information in the application is true and correct, finds that the applicant is eligible for the limitation on the appraised value, and determines that granting the application is in the best interest of the school district and the State.

The Comptroller's Office did not recommend approval of the applications.

The Comptroller's Office did not recommend that the two applications that SandRidge Energy, Inc. submitted be approved for agreements. That decision was based on the Comptroller's Office's determination that (1) SandRidge Energy, Inc. was unable to relocate the projects that were described in the applications to another state or another region of the state and (2) SandRidge Energy, Inc.'s use of the property was not one of the economic activities defined in Texas Tax Code, Chapter 313, as an eligible business activity.

At the time that Fort Stockton ISD approved the two applications for agreements, statute did not require school districts to obtain the Comptroller's Office's approval before entering into agreements. Effective January 1, 2010, Texas Tax Code, Section 313.025(i), prohibited a school district from granting

an agreement on an application that the Comptroller's Office had not recommended for an agreement.

Chapter 5-B

Developing Agreements

The agreements did not include provisions that described the agreed-upon capital investment amount, certain property information, and the number of jobs to be created.

Fort Stockton ISD ensured that the agreements included provisions that complied with statute and that its school board approved the agreements. However, the agreements did not include certain provisions that would enable Fort Stockton ISD to ensure accountability and transparency.

The agreed-upon capital investment amount that SandRidge Energy, Inc. committed to make and the anticipated number of jobs to be created were documented in the applications, rather than in the agreements. However, the agreements did not explicitly state that the applications were part of the agreements.

Texas Tax Code, Section 313.027(e), requires agreements to describe with specificity the capital investment that a business will make on or in connection with the property that is subject to the appraisal limitation. Other property that is not specifically described in the agreement is not subject to the limitation unless the governing body of the school district, by official action, provides that the other property is subject to the limitation.

The agreements were allowed to be transferred to a new business, but they did not specify that the new business meet Texas Tax Code, Chapter 313, eligibility requirements.

The agreements allowed SandRidge Energy, Inc. to transfer the agreements to another business. Specifically, Section 8.4 of each agreement stated:

The Applicant may assign this Agreement, or a portion of this Agreement, to an Affiliate or a new owner or lessee of all or a portion of the Applicant's Qualified Property and/or the Applicant's Qualified Investment, provided that the Applicant shall provide written notice of such assignment to the District. Upon such assignment, Applicant's assignee will be liable to the District for outstanding taxes or other obligations arising under this Agreement.

However, the agreements did not specify that the new business must be eligible to receive an agreement or that the Fort Stockton ISD school board approve the transfer of the agreements. As a result, there is a risk that the

agreements could be transferred to a business that does not meet the eligibility requirements in Texas Tax Code, Chapter 313.

The agreements did not include any performance standards or require periodic deliverables to enable Fort Stockton ISD to monitor compliance.

The agreements did not define performance standards that would enable Fort Stockton ISD to monitor and evaluate SandRidge Energy, Inc.'s compliance with its agreements or statutory requirements for capital investments or job creation. Without specifying performance standards or periodic deliverables to monitor progress, Fort Stockton ISD did not have a defined methodology to obtain assurances that SandRidge Energy, Inc. fulfilled the requirements of the agreements and complied with Texas Tax Code, Chapter 313.

Recommendations

Fort Stockton ISD should consider amending existing agreements to include:

- All required provisions and information related to the agreed-upon investment amounts and the anticipated number of jobs to be created; alternatively, it should explicitly state in agreements that the information in the related applications is incorporated into the agreements.
- Provisions that require Fort Stockton ISD to assess and approve the eligibility of any business to which an agreement is transferred.
- Performance standards or requirements for businesses to periodically submit deliverables that will enable it to hold businesses accountable for achieving desired results.

Chapter 5-C

Monitoring Compliance

Fort Stockton ISD relied primarily on information that SandRidge Energy, Inc. reported on annual eligibility reports and biennial progress reports.

SandRidge Energy, Inc. submitted annual eligibility reports and biennial progress reports to Fort Stockton ISD as required by the Comptroller's Office. (See Appendix 7 for more information on required progress reports that businesses submit.) As discussed in Chapter 1, statute does not require school districts to verify the information on annual eligibility reports and biennial progress reports, and Fort Stockton ISD did not perform verifications.

To assist in its administration of the agreement, Fort Stockton ISD hired a consultant that:

- Compiled and submitted information that businesses reported to the Comptroller's Office.

- Performed calculations and prepared invoices for payments that the agreements required SandRidge Energy, Inc. to make to Fort Stockton ISD.

Examples of the information that SandRidge Energy, Inc. submitted included:

- The number of jobs created.
- Whether the number of jobs created complied with statutory requirements. (Businesses with agreements are required to create **qualifying jobs**. See Appendix 7 for more information on job-creation requirements.)
- Capital investment amounts. (Businesses are required to make certain capital investment amounts, or **qualified investments**, in personal property that will be used with property under agreement. See Appendix 7 for more information on qualified investments.)
- Property values and descriptions for real and personal property covered by the agreements. (Correctly identifying the property and property values is significant to ensuring that property tax losses resulting from agreements are calculated accurately because those tax losses affect the amount of state funding a school district receives each tax year.)

Chapter 5-D

Processing Tax Credits

Fort Stockton ISD paid tax credits directly to SandRidge Energy, Inc. instead of applying tax credits to SandRidge Energy, Inc.'s future property tax bills as required.

Fort Stockton ISD did not comply with its agreement provisions regarding how tax credits should be paid to SandRidge Energy, Inc. Section 6.2 of each agreement required Fort Stockton ISD to direct the collector of taxes to comply with statute, and statute requires that county tax collectors assess tax credits against businesses' future property taxes. However, at the direction of the TEA, Fort Stockton ISD paid tax credits directly to SandRidge Energy, Inc. As of December 31, 2013, Fort Stockton ISD had paid the following tax credits directly to SandRidge Energy, Inc.:

- A total of \$114,052 for the Century Plant agreement.
- A total of \$10,944 for the Grey Ranch agreement.

See Appendix 2 for more information on the tax credits that SandRidge Energy, Inc. may be entitled to receive during the terms of the agreements.

Fort Stockton ISD had limited documentation to support the accuracy and completeness of the properties and the property values used to calculate the tax credits it paid to SandRidge Energy, Inc.

The information that SandRidge Energy, Inc. provided with its applications for tax credits did not clearly identify whether the associated properties were located within the properties described in the agreements. Specifically, there were discrepancies between (1) the property descriptions on the agreements and (2) the property descriptions on the tax receipts that SandRidge Energy, Inc. submitted to Fort Stockton ISD with its tax credit applications.

In addition, auditors identified discrepancies between (1) the property account numbers listed on the tax credit applications and information that SandRidge Energy, Inc. submitted to Fort Stockton ISD and (2) the property account numbers recorded with the Pecos County Appraisal District.

Recommendations

Fort Stockton ISD should:

- Comply with its agreements related to tax credits, and direct the collector of taxes to apply the amount of tax credits against the future property taxes imposed on the property subject to the agreements.
- Verify information reported on tax credit applications to ensure that the amount of each tax credit it issues is correct.
- Verify whether each property covered by an agreement is the same property that the Pecos County Appraisal District has identified as having received an appraisal limitation.

Chapter 5-E

Disclosing Conflicts of Interest

Fort Stockton ISD did not comply with its processes for ensuring that members of its school board disclosed business, professional, and personal relationships that could create potential conflicts of interest.

A member of Fort Stockton ISD's school board did not complete a disclosure statement regarding the member's business relationship and financial interest in SandRidge Energy, Inc., as required by Fort Stockton ISD policy. The member informed auditors that a verbal disclosure was made to the previous superintendent prior to the school board vote on the approval of the agreements. According to the member, the previous superintendent explained that the member's interest in the business was not substantial and did not require disclosure. However, Fort Stockton ISD policy requires that members of its school board file disclosure statements in instances in which a member

has a business relationship with a vendor with which the school district has a contract.

Fort Stockton ISD's policy requires disclosure only when an employee, a member of its school board, or a consultant identifies a conflict of interest. That policy does not specifically require businesses that apply for agreements, members of the school board, employees, and consultants to disclose business, professional, or personal relationships related to the agreement that may pose a conflict of interest or affirm that conflicts do not exist on an annual basis.

Recommendation

Fort Stockton ISD should ensure that members of its school board, its employees, and its consultants follow its conflict of interest policy.

Chapter 5-F

Administrative Processes

Opportunities exist for Fort Stockton ISD to strengthen certain administrative processes. While the following issues may not be material to determining compliance with Texas Tax Code, Chapter 313, they are significant to Fort Stockton ISD's management of its agreements with SandRidge Energy, Inc.:

- Fort Stockton ISD's consultant did not always accurately calculate the amounts that Fort Stockton ISD should have billed SandRidge Energy, Inc. for revenue protection payments and payments in lieu of taxes. As a result of those errors, SandRidge Energy, Inc. overpaid Fort Stockton ISD by a net total of \$57,745.
- Fort Stockton ISD did not establish a statutorily required link on its Web site to the Comptroller's Office Web site as required by Texas Tax Code, Section 313.0265(c).

Recommendations

Fort Stockton ISD should:

- Verify that its consultant's calculations for revenue protection payments and payments in lieu of taxes are accurate.
- Determine how the identified payment errors should be corrected with the business.
- Provide a link on its Web site to the Comptroller's Office's Web site where appraisal limitation-related documents are made available to the public.

Management's Response from Fort Stockton ISD



FORT STOCKTON
INDEPENDENT SCHOOL DISTRICT

101 W DIVISION
FORT STOCKTON, TEXAS 79735
432-336-4000
432-336-4008 FAX

Formal Management Response
Fort Stockton Independent School District
Report on the Audit of Major Agreements under
the Texas Economic Development Act

November 13, 2014

State Auditor's Office
ATTN: Mr. Willie Hicks
P.O. Box 12067
Austin, Texas 78711-2067

Dear Mr. Hicks:

In our response to your Audit of Major Agreements under the Texas Economic Development Act, we want to go on the record with some general comments of our perception of the program, given that we have several agreements in place and have some history with Chapter 313 in the Fort Stockton Independent School District (FSISD). We will then address the specific recommendations made to FSISD by topic within the Report.

General Comments

The District is not responsible for the design of compliance mandates; it is a state responsibility.

As a preliminary matter, the District views Chapter 313 of the Texas Tax Code and the rules adopted to implement Chapter 313 as a state program which is administered in part by the District. In order to ensure uniformity in the administration of the program, this District does not feel it is authorized to impose new obligations on the recipients of the program. Section 313.032(a) specifically authorizes the required Comptroller's report to be "...based on data certified to the Comptroller by each recipient of a limitation on appraised value under this subchapter..." In adopting such provisions, the Texas Legislature created a system designed to rely upon the disclosure of information directly from the applicant for a tax limitation.

Based on the specific comments discussed below, it is apparent that the State Auditor's Office is not satisfied with the applicants' reporting requirements and has consistently sought to impose new and unauthorized verification requirements on FSISD. Keeping in mind the admonitions set forth in Texas Tax Code 313.004(3)(A) that school districts strictly interpret the criteria set forth in Chapter 313, FSISD is reluctant to impose new requirements on Chapter 313 applicants in excess of those set forth in statute or state-agency-adopted administrative rule. FSISD will enforce any requirement legitimately adopted with respect to Chapter 313 agreements, as long as

The mission of the Fort Stockton Independent School District is to remain totally committed to the development of students as life-long learners and productive, self-sustaining contributors to society.



it does not impose uncompensated administrative costs on the District. In the absence of the adoption of new rules or other legal requirements, this District feels compelled to apply the rules and statutes as they currently exist.

Specific Statements of Facts and Responses to Recommendations

Chapter 5-A PROCESSING APPLICATIONS FOR AGREEMENTS

Management Statement of Fact

The District has a well-developed, articulated process for the processing of Chapter 313 applications which included more than relying on certified data from the companies.

The State Auditor's Office found that the District relied primarily on certified information provided by businesses in determining whether the projects would comply with the intent and purpose of Chapter 313 of the Texas Tax Code. It is significant to note that, since the inception of the program, applications have been required to be submitted under oath. Further, Chapter 313 Applications are governmental records under Tex. Penal Code § 37.01(2)(A); as a result, all statements contained therein are representations of fact within the meaning of Tex. Penal Code § 37.01(3). Since the adoption of findings and the approval of a Chapter 313 Agreement is an "official proceeding," a false statement on a Chapter 313 application constitutes perjury under Tex. Penal Code § 37.03. Sworn statements are routinely used as an acceptable verification method for reliance by fact finders in each of the three separate branches of government, including trials.

However, there District relied on independent information and analyses as well. In the case of the SandRidge Applications under review, the economic impact reviews were conducted by an independent consultant of the District, i.e., Texas Perspectives. Their report provided the factual input for many of the Board's Findings. In 2009, as a part of HB 3676, the economic analysis was transferred by law to the Comptroller. Since that time, the Comptroller's economic impact study has supplied critical data for the required board findings. While the Comptroller's office did not recommend approval of the SandRidge applications, as noted in the SAO report, the Board conducted an exhaustive review of the issues raised by the Comptroller and relied upon an independent analysis conducted by a reputable economic consulting firm as the primary basis for its determination of the appropriateness of the two projects. In recent years, the Comptroller's Office has approved a number of natural gas processing plants throughout the state, with as many as ten similar projects approved in the Barbers Hill Independent school District alone.

In summary, the District's Trustees issued explicit fact findings in accordance with the provisions of Tex. Tax Code § 313.025(e-f) after the conclusion of an orderly, well-articulated process designed to consider all of the statutorily-required criteria. In conformance with the strict construction mandate, no extraneous facts were considered. No principle of law is better settled than that acts of discretion and findings-of-fact on the part of public officers to which such power is confided by law and not subject to reversal. (See *Williams v. Castleman*, 112 Tex. 193, 247 S.W. 263, 269 (1922).) Supervisory powers over decisions made by political subdivisions can only be invoked when the body acts beyond its jurisdiction or clearly abuses discretion conferred upon it by law. (See *Yoakum County v. Gaines County*, 139 Tex. 442, 163 S.W.2d 393, 396 (1942).)

Chapter 5-B
Developing Agreements

Recommendations

Fort Stockton ISD should consider amending existing agreements to include:

- All required provisions and information related to the agreed-upon investment amounts and the anticipated number of jobs to be created in agreements, or explicitly state in agreements that the information within the related applications are incorporated into the agreements.
- Provisions that require Fort Stockton ISD to assess the eligibility of any business to which an agreement is transferred.
- Performance standards or requirements for periodic deliverables that will enable it to hold businesses accountable for achieving desired results.

Management's Response

The Agreements in place contain provisions for the implementation of all the recommendations enumerated by the State Auditor's Office.

In its finding 5-B, the State Auditor's report suggested that the District should consider amending existing agreements to include:

1. All required provisions and information related to the agreed-upon investment amounts and the anticipated number of jobs to be created in agreements, or explicitly state in agreements that the information within the related applications are incorporated into the agreements.
2. Provisions that require Fort Stockton ISD to assess the eligibility of any business to which an agreement is transferred.
3. Performance standards or requirements for periodic deliverables that will enable it to hold businesses accountable for achieving desired results.

These issues will be discussed in order below:

1. *Provisions related to investment amounts and anticipated jobs:* The Agreement already has provision related to required investment amounts. Sections 1.2 and 1.3 of both agreements define the tax limitation amount as being \$10 Million. At the time of the agreement Tex. Tax Code §§ 313.022(b) and 313.023 required the applicant's minimum Qualified Investment to be \$10 Million. That was the minimum amount of Qualified Investment required by the Agreement. Furthermore, the existing agreements do specifically incorporate the Application into the agreement. The Application is a defined term in the Agreement. The Applicant is required to create and retain the number of jobs set forth in the Application to Maintain a Viable Presence in the District. And, failure to maintain this viable presence will result in the termination of the Agreement, and subject the Applicant to penalties, including the recoupment of all tax benefit received by the Applicant from the District by virtue of entering into the Agreement.

At the time of the execution of this agreement at issue in this Audit, Comptroller's rules did not require that the applicant was bound by the number of Qualifying Jobs estimated in its application. Instead, the applicant was bound by the statutory requirements set forth at Tex. Tax Code §313.021(2)(A)(iv)(b). The statutory requirement is incorporated into the agreement at Section 6.2(b) which requires the applicant to maintain a viable presence in the district, which in conformance with the term's definition in Section 1.3, included the maintenance, over the life of the agreement of the statutorily required number of jobs.

2. *Provisions that require FSISD to assess the eligibility of any business to which an agreement is transferred:* Section 7.1 of the two Agreements t specifically require the applicant to provide the District and the County Appraisal District all data under the Texas Tax Code necessary to determine whether all obligations under the agreements are being met. Section 8.4 requires written notice of a transfer. Tex. Tax Code § 313.024(a) requires that Chapter 313 Agreements apply only to "property owned by an entity to which [Tax Code] Chapter 313 applies. In the event of such a transfer, as has occurred in the Agreements, the Trustees have amply authority to collect the data upon which continuing eligibility determinations can be made. In actual fact, such information is available on the Comptroller's website in the form of Certificates of Good Standing.

3. *Performance standards or requirements for businesses to periodically submit deliverables that will enable it to hold businesses accountable for achieving desired results:* Annual and biennial reporting requirements are set by Comptroller's rules. As stated above, the Applicant is required under the terms of the Agreement to Maintain a Viable Presence in the District. The reports as posted provide sufficient information to measure compliance with the express terms of the Agreement and all current statutory mandates.

Chapter 5-C Monitoring Compliance

Management Statement of Fact

In considering post-agreement compliance issues, the District relies upon statutorily valid sources, which produce a wide range of data, to verify information provided by companies.

The State Auditor's Office found that Sterling City ISD did not verify information provided by companies provided to demonstrate compliance with the agreements. However, the District has a process in place to verify, or requiring its consultant to verify, accuracy and completeness of information in annual eligibility reports and biennial progress report and has had such a process in place since the time it received its first compliance report. The information is reviewed to determine whether or not the company is in conformance with the investment and job creation requirements set forth in the agreements and in statute. The district also annually verifies that the companies continue to remain eligible to receive the benefit of the value limitation.

It is significant to note that, since the inception of reporting requirements, reports have been required to be submitted under oath. Further, these reports are governmental records under Tex. Penal Code § 37.01(2)(A); as a result, all statements contained therein are representations of fact

within the meaning of Tex. Penal Code § 37.01(3). Sworn statements are routinely used as an acceptable verification method for reliance by fact finders in each of the three separate branches of government, including trials. It is curious the State Auditor's Office, without citation to any other authority, would find this method of verification to be insufficient. It is curious that the State Auditor's Office, without citation to any other authority, would find this method of verification to be insufficient. See also, Tex. Tax Code 313.032.

Chapter 5-D Processing Tax Credits

Recommendations

Fort Stockton ISD should:

- Comply with its agreements related to tax credits, and direct the collector of taxes to credit the amount of the tax credits against the taxes imposed on the property covered by the agreements.
- Verify reported information on tax credit applications to help ensure that the amount of each tax credit it issues is correct.
- Verify whether each property covered by an agreement is the same property that the Pecos County Appraisal District has identified as having received an appraisal limitation.

Tax Credit Reimbursement Requests are submitted in conformance with TEA requirements.

In order for FSISD to seek a state reimbursement under Section 42.2515 of the Education Code should a tax credit be owed, the TEA rule calls for the school district to submit "A copy of the tax bill sent to the taxpayer (showing the credit) or other proof that the school has reimbursed the tax credit to the taxpayer." However, the TEA procedures for the processing of tax credits currently in place require the District to present the Agency with proof of actual payment to the company of the tax credit amount as a prerequisite for reimbursement to the District.

Over time, TEA has imposed varying requirements as a precondition of reimbursement. In light of the TEA's varying standards of compliance, it is imprudent to specify the conditions for payment of tax credit in the Agreement. The District's view is that the TEA rules and procedures are sufficient to ensure verification prior to expenditure by the state and ensure that there is an appropriate "audit trail" in making state reimbursements to school districts for tax credits.

One issue that is a concern to FSISD is that the reimbursement payments from TEA are not as timely as the District would like and have created challenges in meeting the District's cash-flow needs. But it is unlikely that direct tax credits to Chapter 313 recipients would remedy that problem.

And, the District has a process in place to annually verify and determine eligibility of a company's tax credit. The District does rely on the Appraisal District and Tax Collector in identifying the property that is the subject of each application. But, the District has no authority over either independent entity in the naming convention used to identify specific parcels of property.

Chapter 5-E Disclosing Conflicts of Interest

Recommendations

Fort Stockton ISD should:

- Ensure that members of its school board, its employees, and its consultants follow its conflict of interest policy to disclose business, professional, and personal relationships that could create potential conflicts of interest.

Management's Response

Management Response

The State Auditor's recommended actions are unnecessary in light of explicit provisions of State law and FSISD policy that are currently in place.

The State Auditor's Office found that the District did not comply with its processes regarding conflict of interest. The District disagrees with this finding. Under the Texas Local Government Code and District Board Policy, disclosure and abstention are required only when a trustee has a substantial interest in a business entity with whom the District will contract. Texas Local Gov't Code §171.004 requires disclosure of conflicts of interest by all school Trustees and any other officer, including the Superintendent and the Business Manager/Chief Financial Officer. (See, Texas Local Gov't Code §171.004(a).) Under Texas Local Gov't Code §171.001(1), a "local public official" is defined as a member of the governing body or another officer, whether elected, appointed, paid, or unpaid, of any district (including a school district), central appraisal district, or other local governmental entity who exercises responsibilities beyond those that are advisory in nature.

A school officer has a substantial interest in a business entity if such a local public official or a person related to a local public official in the first degree by either affinity or consanguinity has a substantial interest in a business entity or in real property, the local public official, before a vote or decision on any matter involving the business entity or the real property, is specifically required by State law to file an affidavit with an official Board record keeper stating the nature and extent of the interest and shall abstain from further participation in the matter if:

1. In the case of a substantial interest in a business entity, the action on the matter will have a special economic effect on the business entity that is distinguishable from the effect on the public; or
2. In the case of a substantial interest in real property, it is reasonably foreseeable that an action on the matter will have a special economic effect on the value of the property, distinguishable from its effect on the public.

Under Texas Local Gov't Code §171.002(a), a school officer has a substantial interest in a business entity if:

1. The person owns at least:
 - a. Ten percent of the voting stock or shares of the business entity, or
 - b. Either ten percent or \$15,000 of the fair market value of the business entity.
2. Funds received by the person from the business entity exceed ten percent of the person's gross income for the previous year.

Under Texas Local Gov't Code §171.002(b), a school officer has a substantial interest in real property if the interest is an equitable or legal ownership with a fair market value of \$2,500 or more.

Under Texas Local Gov't Code §171.002(c), a school officer is considered to have a substantial interest if a person related in the first degree by either affinity or consanguinity to the local public official, as determined under Government Code Chapter 573, Subchapter B, has a substantial interest as defined above.

Texas Local Gov't Code §171.003 generally provides that a local public official shall not knowingly:

1. Participate in a vote or decision on a matter involving a business entity or real property in which the local public official has a substantial interest if it is reasonably foreseeable that an action on the matter will have a special economic effect on the business entity or value of the property that is distinguishable from the effect on the public.
2. Act as surety for a business entity that has a contract, work, or business with the District.
3. Act as surety on any official bond required of an officer of the District.

Texas Local Gov't Code 176.003-.004 provides that a local government officer must file the required conflicts disclosure statement, as adopted by the Texas Ethics Commission, with a Chapter 313 Applicant, if the Applicant proposes to enter into a contract with the; and the Applicant:

1. Has an employment or other business relationship with the local government officer or a family member of the officer that results in the officer or family member receiving taxable income, other than investment income, that exceeds \$2,500 during the 12-month period preceding the date that the officer becomes aware that a contract has been executed or the District is considering entering into a contract with the person; or
2. Has given to the local government officer or a family member of the officer one or more gifts that have an aggregate value of more than \$250 in the 12-month period preceding the date the officer becomes aware that such a contract has been executed or the District is considering entering into a contract with the vendor.

A local government officer is not required to file a conflicts disclosure statement in relation to a gift accepted by the officer or a family member of the officer if the gift is:

1. Given by a family member of the person accepting the gift;
2. A political contribution as defined by Title 15, Election Code; or
3. Food, lodging, transportation, or entertainment accepted as a guest.

A local government officer shall file the conflicts disclosure statement with the records administrator of the District not later than 5:00 p.m. on the seventh business day after the date on which the officer becomes aware of the facts that require the filing of the statement. A local government officer commits a Class C misdemeanor if the officer knowingly violates this law. It is an exception to the application of the penalty that the local government officer filed the

required conflicts disclosure statement not later than the seventh business day after receiving notice from the District of the alleged violation.

Texas Local Gov't Code §176.009 requires that if the school district that maintains an Internet Web site, it shall provide access on the District's Internet Web site to the conflicts disclosure statements and questionnaires required to be filed with the records administrator. (These disclosure forms are posted on the District's website.)

Under Texas Education Code §39.083; and 19 TAC § 109.1005 a school district's annual financial management report must include summary reports of reimbursement received by each Board member, reports of certain gifts from school vendors, and reports of Board member business transactions with the District.

FSISD Board adopted policies BBFA (Local) and CFA (Local) specifically require of each Trustee the filing of the required reports and disclosures. These policies are binding on each individual Trustee. The Policies albeit having been occasionally amended to ensure compliance with amendments to State law, have been in effect at all times material to the negotiation and management of all Tax Code Chapter 313 agreements to which the District has been a party.

The finding by the State Auditor's is not supported in light of the District's compliance with these statutory and policy requirements. Any additional requirements for some form of additional and undifferentiated conflict-of-interest requirement upon individual board members who are not legal parties to a Chapter 313 Agreement is redundant to the very explicit and exacting provisions of State law and district policy; would be legally ineffective; and, would create additional and unnecessary bureaucratic hurdles in an already complex system.

Chapter 5-F Administrative Processes

Recommendations

Fort Stockton ISD should:

- Verify the consultant's calculations for revenue protection payments and payments in lieu of taxes are accurate.
- Determine how the identified payment errors should be corrected with the business.
- Provide a link on its Web site to the Comptroller's Office's Web site where appraisal limitation related documents are made available to the public.

Management Response

The revenue protection and payment in-lieu of taxes calculation issues raised in the SAO report concern calculations that were based on preliminary property value information. The District did not receive any questions about these calculations from the Companies, based on the letters of estimate provided to them. Recalculations will be provided to the Companies as called for under Section 3.9 of both Agreements. These calculations did not result in any overpayment of tax credit reimbursements to FSISD by TEA.

The District currently provides a link to the Comptroller's Chapter 313 website on the District's website.

Palacios Independent School District Agreements with NRG South Texas 3 and NRG South Texas 4

| Background Information on the Two Audited Agreements with the Palacios Independent School District | | |
|--|--|--|
| Business | NRG South Texas 3 | NRG South Texas 4 |
| Application number | 118 | 119 |
| Business category | Nuclear electric power generation | Nuclear electric power generation |
| County | Matagorda | Matagorda |
| Term of agreement | January 1, 2009, through December 31, 2029 | January 1, 2009, through December 31, 2029 |
| Appraisal limitation | \$30,000,000 | \$30,000,000 |
| Tax year 2013 appraised value | \$0 | \$0 |
| Net tax benefit business received based on the 2012 Biennial Cost Data Request Form | \$0 | \$0 |
| Number of qualifying jobs created as reported by the business (as of December 31, 2013) | 0 | 0 |
| Total tax credits business is eligible to receive | \$0 | \$0 |
| Other tax abatements and economic incentives the business received | None | None |
| Revenue protection payments school district received from the business (as of December 31, 2013) | \$0 | \$0 |
| Payments in lieu of taxes school district received from business (as of December 31, 2013) | \$1,750,000 | \$1,750,000 |
| ^a See Appendix 2 for more detailed information. | | |

Business activity related to the two audited appraisal limitation agreements (agreements) between the Palacios Independent School District (Palacios ISD) and NRG South Texas 3³ and NRG South Texas 4⁴ had not started as of December 31, 2013. As a result, the businesses had made no progress in complying with certain requirements of Texas Tax Code, Chapter 313.

Auditors determined that Palacios ISD executed the agreements in compliance with Texas Tax Code, Section 313.027.

The maximum property value on which the properties covered by each of the agreements with NRG South Texas 3 and NRG South Texas 4 can be taxed for the maintenance and operations portion of property taxes is \$30,000,000. As of December 31, 2013, no appraised value had been reported because business activity related to the agreements had not started.

Sources: The Office of the Comptroller of Public Accounts, Palacios ISD, and the Matagorda County Appraisal District.

³ The agreement is with NRG South Texas 3 LLC and NRG South Texas LP. For the purposes of this report, those two businesses collectively are referred to as NRG South Texas 3.

⁴ The agreement is with NRG South Texas 4 LLC and NRG South Texas LP. For the purposes of this report, those two businesses collectively are referred to as NRG South Texas 4.

The remainder of this chapter provides information on the following:

- Processing applications for agreements.
- Developing agreements.
- Monitoring compliance.
- Disclosing conflicts of interest.
- Opportunities to improve certain administrative processes.

Chapter 6-A

Processing Applications for Agreements

Palacios ISD relied primarily on information provided in the NRG South Texas 3 and NRG South Texas 4 applications.

Applications for Appraisal Limitation

NRG South Texas 3 and NRG South Texas 4 initially submitted a joint application and a \$175,000 application fee to the Palacios ISD board of trustees on July 30, 2007. The businesses submitted supplemental applications to separate the projects on November 1, 2007. Each application included:

- Survey maps of the proposed property.
- A summary of the school finance impact of the proposed appraisal limitation value prepared by the school district's consultant.
- An economic impact report prepared by a subcontractor of the consultant.
- Inventory of pollution control equipment.

Palacios ISD submitted the applications to the Comptroller's Office as required by statute. The Comptroller's Office issued its recommendation letters to Palacios ISD on May 7, 2008.

The Palacios ISD board of trustees issued its findings related to the impact of the NRG South Texas 3 and NRG South Texas 4 appraisal limitations on the school district as required by statute and approved the agreements on June 9, 2008.

Sources: The Comptroller's Office and Palacios ISD.

Palacios ISD documented its determination of how agreements with NRG South Texas 3 and NRG South Texas 4 would comply with the intent and purpose of Texas Tax Code, Chapter 313. (See text box for additional information about the NRG South Texas 3 and NRG South Texas 4 applications and Appendix 4 for specific statutory requirements.) To make that determination, Palacios ISD relied primarily on certified information that NRG South Texas 3 and NRG South Texas 4 provided in the applications for agreements. Examples of that information included:

- The types of jobs that NRG South Texas 3 and NRG South Texas 4 committed to create.
- The number of each type of job.
- The wages to be paid for each job.
- The employee benefits to be offered.
- The ability of the business to locate or relocate in another state or another region of the state.

Texas Tax Code, Section 313.025(f), states that a school district may approve an application only if it finds that the information in the application is true and correct, finds that the applicant is eligible for the limitation on the appraised value, and determines that granting the application is in the best interest of the school district and the State.

Developing Agreements

The agreements did not include provisions that described the agreed-upon capital investment amount, certain property information, and the number of jobs to be created.

Palacios ISD ensured that the agreements included provisions that complied with statute and that its board of trustees approved the agreements. However, the agreements did not include certain provisions that would enable Palacios ISD to ensure accountability and transparency.

The agreed-upon capital investment amount that NRG South Texas 3 and NRG South Texas 4 committed to make, the description and address of the property to be covered by the agreements, and the anticipated number of jobs to be created were documented in the applications, rather than in the agreements. However, the agreements did not explicitly state that the applications were part of the agreements.

Texas Tax Code, Section 313.027(e), requires agreements to describe with specificity the capital investment that a business will make on or in connection with the property that is subject to the appraisal limitation. Other property that is not specifically described in the agreement is not subject to the limitation unless the governing body of the school district, by official action, provides that the other property is subject to the limitation.

Provisions of the agreements allowed the agreements to be transferred to a new business, but they did not specify that the new business meet Texas Tax Code, Chapter 313, eligibility requirements.

The agreements allowed NRG South Texas 3 and NRG South Texas 4 to transfer the agreements to another business. Specifically, Section 8.4 of each agreement required that the businesses provide notification to Palacios ISD when a transfer occurs. However, the agreements did not specify that the new business must be eligible to receive an agreement or that the Palacios ISD board of trustees approve the transfer of the agreements. As a result, there is a risk that the agreements could be transferred to a business that does not meet the eligibility requirements in Texas Tax Code, Chapter 313.

The agreements did not include any performance standards or require periodic deliverables to enable Palacios ISD to monitor compliance.

The agreements did not define performance standards that would enable Palacios ISD to monitor and evaluate that NRG South Texas 3 and NRG South Texas 4 complied with their agreements or statutory requirements for capital investment or job creation. Without specifying performance standards or periodic deliverables to monitor progress, Palacios ISD did not have a defined methodology to obtain assurances that NRG South Texas 3 and NRG South Texas 4 fulfilled the requirements of their agreements and complied with Texas Tax Code, Chapter 313.

Recommendations

Palacios ISD should consider amending existing agreements to include:

- All required provisions and information related to the agreed-upon investment amounts and the anticipated number of jobs to be created; alternatively, it should explicitly state in agreements that the information within the related applications is incorporated into the agreements.
- Provisions that require Palacios ISD to assess and approve the eligibility of any business to which an agreement is transferred.
- Performance standards or requirements for businesses to periodically submit deliverables that will enable it to hold businesses accountable for achieving desired results.

Chapter 6-C

Monitoring Compliance

There has been no business activity involving Palacios ISD's agreements with NRG South Texas 3 and NRG South Texas 4. However, the businesses still must comply with the requirements in their agreements. Palacios ISD should improve its processes to ensure that the businesses comply with certain payment requirements.

Payments in Lieu of Taxes Made to Palacios ISD

Palacios ISD's agreements with NRG South Texas 3 and NRG South Texas 4 required the businesses to make two types of payments in lieu of taxes. Specifically, Article IV of each agreement required the businesses to make annual contributions to the Palacios ISD Education Foundation in the amounts listed and scheduled in each agreement. For tax years 2009, 2010, and 2011, the businesses made contributions that totaled \$3.5 million.

In addition, the businesses are required to make annual payments to Palacios ISD equal to 5 percent of the net tax benefit that they receive as a result of the agreements.

See Appendix 2 for more information on payments in lieu of taxes the businesses made to Palacios ISD.

Source: Palacios ISD.

Palacios ISD did not receive certain payments in lieu of taxes for tax years 2012 and 2013, as required by the agreements.

Palacios ISD did not receive a total of \$3.5 million in payments in lieu of taxes (through annual contributions to the Palacios ISD Education Foundation) for tax years 2012 or 2013, as required by the agreements with NRG South Texas 3 and NRG South Texas 4 (see the text box for more information).

Emails from a representative for NRG South Texas 3 and NRG South Texas 4 indicated that the businesses did not have the funds to make those payments and requested deferring the payments for one year with interest. Palacios ISD staff affirmed that they agreed to defer the payments. However, Palacios ISD staff did not have documentation to show that the Palacios ISD board of trustees approved that decision.

Table 3 shows the payments that the businesses were required to pay Palacios ISD on each agreement for tax years 2012 and 2013.

Table 3

| Contributions to the Palacios ISD Education Foundation that the Audited Agreements Required NRG South Texas 3 and NRG South Texas 4 to Pay | | | |
|--|--------------------|--------------------|--------------------|
| Tax Year | Required Payments | | Tax Year Total |
| | NRG South Texas 3 | NRG South Texas 4 | |
| 2012 | \$ 750,000 | \$ 750,000 | \$ 1,500,000 |
| 2013 | 1,000,000 | 1,000,000 | 2,000,000 |
| Totals | \$1,750,000 | \$1,750,000 | \$3,500,000 |

Source: Palacios ISD.

Recommendation

Palacios ISD should maintain documentation to show the approval of any decisions it makes that do not align with the provisions in its agreements and amend the agreements accordingly.

Chapter 6-D

Disclosing Conflicts of Interest

Palacios ISD did not comply with its policy for ensuring that members of its board of trustees disclosed business, professional, and personal relationships that could create potential conflicts of interest and abstain from matters involving those relationships.

A member of Palacios ISD’s board of trustees did not disclose being employed with South Texas Project, which is currently operating on property covered by the agreements with NRG South Texas 3 and NRG South Texas 4. That member voted with the board of trustees to approve the applications for the audited agreements. Palacios ISD’s policy requires members of the board of trustees to file conflict of interest disclosure statements if and when they identify a conflict. In addition, that policy requires members to abstain from participation in matters before the board of trustees that involve parties with which members have conflicts of interest.

Palacios ISD’s policy requires disclosure only when an employee, a member of its board of trustees, or a consultant identifies a conflict of interest. That policy does not specifically require businesses that apply for agreements, members of the board of trustees, employees, and consultants to disclose business, professional, or personal relationships related to agreements that may pose a conflict of interest or affirm that conflicts do not exist on an annual basis.

Recommendation

Palacios ISD should ensure that members of its board of trustees, its employees, and its consultants follow its conflict of interest policy.

Chapter 6-E

Administrative Processes

Opportunities exist for Palacios ISD to strengthen certain administrative processes. While the following issues may not be material to determining compliance with Texas Tax Code, Chapter 313, they are significant to Palacios ISD's management of its agreements with NRG South Texas 3 and NRG South Texas 4:

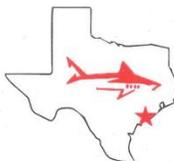
- NRG South Texas 3 and NRG South Texas 4 submitted supplemental applications containing handwritten corrections, and Palacios ISD did not have documentation to show when those revisions were made and whether it approved those revisions.
- The agreements have conflicting provisions that describe how Palacios ISD should issue tax credits to the businesses. Section 1.4 of each agreement stated that Palacios ISD would pay tax credits to NRG South Texas 3 and NRG South Texas 4. However, Section 6.2 of each agreement states that Palacios ISD would direct the collector of taxes to comply with statute regarding the payment of tax credits. Texas Tax Code, Chapter 313, requires the collector of taxes to credit a business's imposed taxes by the amount of the tax credits.
- Palacios ISD did not establish a statutorily required link on its Web site to the Comptroller's Office Web site as required by Texas Tax Code, Section 313.0265(c).

Recommendations

Palacios ISD should:

- Document the official approval of any revisions and corrections to applications.
- Include in agreements consistent provisions that describe how tax credits will be issued to businesses.
- Provide a link on its Web site to the Comptroller's Office's Web site where appraisal limitation-related documents are made available to the public.

Management's Response from Palacios ISD



PALACIOS INDEPENDENT SCHOOL DISTRICT

1209 Twelfth Street • Palacios, Texas 77465-3799
(361) 972-5491 • FAX (361) 972-3567
www.palaciosisd.org

PALACIOS ISD MANAGEMENT RESPONSES TO AUDIT RECOMMENDATIONS – 313 AGREEMENT

6B Developing Agreements

Recommendations

Palacios ISD should consider amending existing agreements to include:

- (1) All required provisions and information related to the agreed-upon investment amounts and the anticipated number of jobs to be created; alternatively, it should explicitly state in agreements that the information within the related applications is incorporated into the agreements.
- (2) Provisions that require Palacios ISD to assess and approve the eligibility of any business to which an agreement is transferred.
- (3) Performance standards or requirements for businesses to periodically submit deliverables that will enable it to hold businesses accountable for achieving desired results.

Management Response - Disagree

- (1) While the agreement does not explicitly state that the application is part of the agreement, it is referenced multiple times in both the Findings of the district and in sections of the agreement. The application is extensively identified and referenced in the Recitals section of the agreement in such a way that it is clear that the agreement is based on the application itself. In the Definitions section, "Applicant" is defined in a way that explicitly ties the agreement to the specific application submitted by NRG South Texas.
- (2) Section 8.4 which allows the applicant to assign the agreement to an affiliate or new owner, requires written notice to the district of such assignment. Section 7.1 allows the district to request information to verify that the applicant is "in compliance with its obligations under this Agreement". In the event of a transfer of the property, Section 7.1, which grants the district the authority to assess and approve the eligibility of the owner, would provide the vehicle for ensuring compliance with Chapter 313.
- (3) Section 7.2 requires the applicant to provide all required reports and filings, including the annual report to the Texas Comptroller. These reports would allow for verification of the applicant's performance.

"Keeping Students First"

6C – Monitoring Compliance

Recommendation

Palacios ISD should maintain documentation to show the approval of any decisions it makes that do not align with the provisions in its agreements and amend the agreements accordingly.

Management Response - Agree

The district will meet with NRG representatives to determine any amendments to the schedule of payments, and will officially report to its Board on the status of payments scheduled to be received from NRG as listed in the agreement.

Person Responsible: Superintendent, Vicki Adams.

Timeline for Implementation: Before the next payment due-date in January 2015.

6D – Disclosing Conflicts of Interest

Recommendation

Palacios ISD should ensure that members of its board of trustees, its employees, and its consultants follow its conflict of interest policy.

Management Response – Disagree

Palacios ISD *did* follow its legal and local policy as related to disclosures of conflicts of interest by board members. A member must disclose a conflict of interest, and abstain from any vote involving the business entity, if they have a “substantial interest” in that business entity. To the extent of the district’s knowledge, and based on the board member’s statement, the board member in question did not have a substantial interest in NRG as defined by policy and by the Texas Governmental Code.

BBFA(legal) policy:

A person has a substantial interest in a business entity if any of the following is the case:

1. *The person owns at least:*
 - a. *Ten percent of the voting stock or shares of the business entity, or*
 - b. *Either ten percent or \$15,000 of the fair market value of the business entity.*
2. *Funds received by the person from the business entity exceed ten percent of the person’s gross income for the previous year.*

Government Code Chapter 572

Sec. 572.005. DETERMINATION OF SUBSTANTIAL INTEREST. An individual has a substantial interest in a business entity if the individual:

- (1) has a controlling interest in the business entity;*
- (2) owns more than 10 percent of the voting interest in the business entity;*
- (3) owns more than \$25,000 of the fair market value of the business entity;*
- (4) has a direct or indirect participating interest by shares, stock, or otherwise, regardless of whether voting rights are included, in more than 10 percent of the profits, proceeds, or capital gains of the business entity;*
- (5) is a member of the board of directors or other governing board of the business entity;*
- (6) serves as an elected officer of the business entity; or*
- (7) is an employee of the business entity.*

Added by Acts 1993, 73rd Leg., ch. 268, Sec. 1, eff. Sept. 1, 1993.

The board member in question was employed by the South Texas Nuclear Operating Company (STP-NOC). STP-NOC is a nuclear operating company hired by the multiple owners of the South Texas Project. The project is owned by Austin Energy (16 percent), CPS Energy (40 percent), and NRG Energy, Inc. (44 percent).

Therefore, the board member does not receive compensation from NRG, and does not meet the definition of having a “substantial interest” in NRG.

6E – Administrative Processes

Recommendations

Palacios ISD should:

- (1) Document the official approval of any revisions and corrections to applications.
- (2) Include in agreements consistent provisions that describe how tax credits will be made to businesses.
- (3) Provide a link on its Web site to the Comptroller's Office's Web site where appraisal limitation related documents are made available to the public.

Management Response - Mixed

- (1) **Disagree.** The district was unaware of any handwritten notes added to the application. These apparently were added by another party after the approval of the application by Palacios ISD. They appear to be a record of updated information provided to the Comptroller's Office.
- (2) **Disagree.** The definition of a tax credit in Section 1.4 uses the word "paid" to describe the direction of flow of the value received being from the district to the applicant. It could more correctly be replaced with "granted". However, both sections 1.4 and 6.2 defer to Subchapter D of the Act for the details of how the credit is processed. There is no conflict as to how the actual tax credit, should one ever occur, would be processed.
- (3) **Agree.** Palacios ISD has added a link to its district web site, linking the appropriate section of the Comptroller's web site. This requirement was overlooked due to the fact that the requirement was added one year after the agreements were completed.

Person Responsible: Superintendent, Vicki Adams.

Timeline for Implementation: October 8, 2014.

Sterling City Independent School District Agreements with Goat Mountain Wind, LP and Goat Wind, LP

| Background Information on the Two Audited Agreements with the Sterling City Independent School District ^a | | |
|---|--|--|
| Business | Goat Mountain Wind, LP | Goat Wind, LP |
| Application number | 65 | 84 |
| Business category | Renewable energy electric generation (wind farm) | Renewable energy electric generation (wind farm) |
| County | Sterling | Sterling |
| Term of agreement | January 1, 2008, through December 31, 2020 | January 1, 2008, through December 31, 2020 |
| Appraisal value with limitation | \$10,000,000 | \$10,000,000 |
| Tax year 2013 appraised value | \$188,114,000 | \$12,446,980 |
| Net tax benefit business received based on the 2012 Biennial Cost Data Request Form | \$1,037,110 | \$110,186 |
| Number of qualifying jobs created as reported by the business (as of December 31, 2013) | 31 | 6 |
| Total tax credits business is eligible to receive | \$14,695,355 | \$48,327 |
| Other tax abatements and economic incentives business received | Property tax abatement from Sterling County | Not Reported |
| Revenue protection payments school district received from business (as of December 31, 2013) | \$864,305 | \$6,506 |
| Payments in lieu of taxes school district received from business (as of December 31, 2013) | \$9,298,549 | \$73,368 |
| ^a See Appendix 2 for more detailed information. | | |

Sources: The Office of the Comptroller of Public Accounts, Sterling City ISD, and Sterling County Appraisal District.

This report chapter covers the appraisal limitation agreements (agreements) between the Sterling City Independent School District (Sterling City ISD) and Goat Mountain Wind LP and Goat Wind LP. Goat Mountain Wind LP and Goat Wind LP certified to Sterling City ISD through their submission of annual eligibility forms and biennial progress reports that they complied with certain requirements of Texas Tax Code, Chapter 313. Sterling City ISD accepted those submissions. As discussed in Chapter 1, statute does not require school districts to verify that information, and Sterling City ISD did not perform verifications.

Auditors determined that Sterling City ISD executed those agreements in compliance with Texas Tax Code, Section 313.027.

The maximum property value on which the properties covered by the agreements with Goat Mountain Wind, LP and Goat Wind, LP can be taxed for the maintenance and operations portion of property taxes is \$10,000,000. As of December 31, 2013, the appraised values of those properties were:

- \$188,114,000 for the property covered by the agreement with Goat Mountain Wind, LP.
- \$12,446,980 for the property covered by the agreement with Goat Wind, LP.

Table 4 provides information on the appraised value of the properties under the agreements.

Table 4

| Goat Mountain Wind, LP and Goat Wind, LP Property Appraised Values Compared to Appraisal Limitation Values from January 2008 through December 2013 | | | | |
|--|----------------|---|--|--|
| Tax Year | Agreement Year | Appraised Value | | Appraisal Limitation Value for Each Agreement ^a (Taxable Value for Maintenance and Operations Property Taxes Purposes) |
| | | Property Covered by Agreement with Goat Mountain Wind, LP | Property Covered by Agreement with Goat Wind, LP | |
| 2008 | 1 | \$569,310,000 | \$ 3,877,020 | No limitation |
| 2009 | 2 | \$863,704,860 | \$14,646,850 | No limitation |
| 2010 | 3 | \$328,652,500 | \$15,650,250 | \$10,000,000 |
| 2011 | 4 | \$238,412,880 | \$14,374,350 | \$10,000,000 |
| 2012 | 5 | \$206,875,830 | \$13,811,850 | \$10,000,000 |
| 2013 | 6 | \$188,114,000 | \$12,446,980 | \$10,000,000 |

^a The appraisal limitations became effective in the third year of the agreements and applies only to the maintenance and operations portion of the school district's property tax. The property remains fully taxable for purposes of any school district debt service tax during the terms of the agreements.

Sources: Sterling County Appraisal District and Sterling City ISD.

The remainder of this chapter provides information on the following:

- Processing applications for agreements.
- Developing agreements.
- Monitoring compliance.
- Processing tax credits.
- Disclosing conflicts of interest.
- Opportunities to improve certain administrative processes.

Processing Applications for Agreements

Sterling City ISD relied primarily on information provided in Goat Mountain Wind, LP's and Goat Wind, LP's applications.

Applications for Appraisal Limitation

Goat Mountain Wind, LP submitted its application to the Sterling City ISD school board on March 19, 2007. Goat Wind, LP submitted its application to the Sterling City ISD school board on September 11, 2007. Each application included:

- An application fee of \$75,000.
- Description of the proposed property.
- A summary of the school finance impact of the proposed appraisal limitation value prepared by the school district's consultant.
- A potential economic impact report prepared by a subcontractor of the consultant.

Sterling City ISD submitted the applications to the Comptroller's Office as required by statute. The Comptroller's Office issued its recommendation letters to Sterling City ISD for Goat Mountain Wind, LP on August 24, 2007, and for Goat Wind, LP on November 16, 2007.

The Sterling City ISD school board issued its findings related to the impact of the proposed agreements on the school district as required by statute and approved the agreement with Goat Mountain Wind, LP on August 30, 2007, and its agreement with Goat Wind, LP on December 20, 2007.

Sources: The Comptroller's Office and Sterling City ISD.

Sterling City ISD documented its determination of how agreements with Goat Mountain Wind, LP and Goat Wind, LP would comply with the intent and purpose of Texas Tax Code, Chapter 313. (See text box for additional information about the applications and Appendix 4 for specific statutory language). To make that determination, Sterling City ISD relied primarily on certified information the businesses provided in their applications for an agreement. Examples of that information included:

- The types of jobs that Goat Mountain Wind, LP and Goat Wind, LP committed to create.
- The number of each type of job.
- The wages to be paid for each job.
- The employee benefits to be offered.
- The ability of the business to locate or relocate in another state or another region of the state.

Texas Tax Code, Section 313.025(f), states that a school district may approve an application only if it

finds that the information in the application is true and correct, finds that the applicant is eligible for the limitation on the appraised value, and determines that granting the application is in the best interest of the school district and the State.

Developing Agreements

The agreements did not include provisions that described the agreed-upon capital investment amount, certain property information, and the number of jobs to be created.

Sterling City ISD ensured that the agreements included provisions that complied with statute and that its school board approved the agreements. However, the agreements did not include certain provisions that would enable Sterling City ISD to ensure accountability and transparency.

The agreed-upon capital investment amounts that Goat Mountain Wind, LP and Goat Wind, LP committed to make, the description and address of the properties to be covered by the agreements, and the anticipated number of jobs to be created were documented in the applications, rather than in the agreements. However, the agreements did not explicitly state that the applications were part of the agreements.

Texas Tax Code, Section 313.027(e), requires agreements to describe with specificity the capital investment that a business will make on or in connection with the property that is subject to the appraisal limitation. Other property that is not specifically described in the agreement is not subject to the limitation unless the governing body of the school district, by official action, provides that the other property is subject to the limitation.

Provisions of the agreements allowed the agreements to be transferred to a new business, but they did not specify that the new business meet Texas Tax Code, Chapter 313, eligibility requirements.

The agreements allowed Goat Mountain Wind, LP and Goat Wind, LP to transfer the agreements to other businesses. Specifically, Section 8.4 of the agreement with Goat Mountain Wind, LP and Section 7.4 of the agreement with Goat Wind, LP allowed each business to transfer the agreement to another business upon written notification of the transfer to the Sterling City ISD. However, the agreements did not specify that the new business must be eligible to receive an agreement or that the Sterling City ISD school board approve the transfer of the agreements. As a result, there is a risk that the agreements could be transferred to a business that does not meet the eligibility requirements in Texas Tax Code, Chapter 313.

The agreements did not include any performance standards or require periodic deliverables to enable Sterling City ISD to monitor compliance.

The agreements did not define performance standards that would enable Sterling City ISD to monitor and evaluate Goat Mountain Wind, LP's and Goat Wind, LP's compliance with their agreements or statutory requirements for capital investments or job creation. Without specifying performance standards or periodic deliverables to monitor progress, Sterling City ISD did not have a defined methodology to obtain assurances that Goat Mountain Wind, LP and Goat Wind, LP fulfilled the requirements of their agreements and complied with Texas Tax Code, Chapter 313.

Recommendations

Sterling City ISD should consider amending existing agreements to include:

- All required provisions and information related to the agreed-upon investment amounts and the anticipated number of jobs to be created;

alternatively, it should explicitly state in agreements that the information in the related applications is incorporated into the agreements.

- Provisions that require Sterling City ISD to assess and approve the eligibility of any business to which an agreement is transferred.
- Performance standards or requirements for businesses to periodically submit deliverables that will enable it to hold businesses accountable for achieving desired results.

Chapter 7-C

Monitoring Compliance

Sterling City ISD relied primarily on information that Goat Mountain Wind, LP and Goat Wind, LP reported on annual eligibility reports and biennial progress reports.

Goat Mountain Wind, LP and Goat Wind, LP submitted annual eligibility reports and biennial progress reports to Sterling City ISD as required by the Comptroller's Office. (See Appendix 7 for more information on required progress reports that businesses submit.) As discussed in Chapter 1, statute does not require school districts to verify the information on annual eligibility reports and biennial progress reports, and Sterling City ISD did not perform verifications.

To assist in its administration of the agreement, Sterling City ISD hired a consultant that:

- Compiled and submitted information that the businesses reported to the Comptroller's Office.
- Performed calculations and prepared invoices for payments that the agreements required Goat Mountain Wind, LP and Goat Wind, LP to make to Sterling City ISD.

Examples of the information that Goat Mountain Wind, LP and Goat Wind, LP submitted included:

- The number of jobs created.
- Whether the number of jobs created complied with statutory requirements. (Businesses with agreements are required to create **qualifying jobs**. See Appendix 7 for more information on job-creation requirements.)
- Capital investment amounts. (Businesses are required to make certain capital investment amounts, or **qualified investments**, into personal property that will be used with property under agreement. See Appendix 7 for more information on qualified investments.)

- Property values and descriptions for real and personal property covered by the agreements. (Correctly identifying the property and property values is significant to ensuring that property tax losses resulting from agreements are calculated accurately because those tax losses affect the amount of state funding a school district receives each tax year.)

Chapter 7-D

Processing Tax Credits

Sterling City ISD paid tax credits directly to Goat Mountain Wind, LP and Goat Wind, LP, instead of applying tax credits to the businesses' future property tax bills as required.

Sterling City ISD did not comply with its agreements when it paid tax credits to Goat Mountain Wind, LP and Goat Wind, LP. Section 6.2 of the agreement with Goat Mountain Wind, LP and Section 5.1 of the agreement with Goat Wind, LP require Sterling City ISD to direct its collector of taxes to comply with statute, and statute requires that county tax collectors assess tax credits against businesses' future property taxes. However, at the direction of the TEA, Sterling City ISD paid tax credits directly to Goat Mountain Wind, LP and Goat Wind, LP. As of December 31, 2013, Sterling City ISD had paid the following tax credits directly to Goat Mountain Wind, LP and Goat Wind, LP:

- A total of \$1.1 million for the Goat Mountain Wind, LP agreement.
- A total of \$13,808 for the Goat Wind, LP agreement.

See Appendix 2 for more information on the tax credits that Goat Mountain Wind, LP and Goat Wind, LP may be entitled to receive during the terms of the agreements.

Sterling City ISD did not have documentation to support the accuracy and completeness of the properties and the property values used to calculate the tax credits it paid to Goat Mountain Wind, LP and Goat Wind, LP.

The information that Goat Mountain Wind, LP and Goat Wind, LP provided with their applications for tax credits did not clearly identify whether the associated properties were located within the properties described in the agreements. Specifically, there were discrepancies between (1) the property descriptions on the agreements and (2) the property descriptions on the tax receipts that the businesses submitted to Sterling City ISD with their tax credit applications.

Recommendations

Sterling City ISD should:

- Comply with its agreements related to tax credits, and direct the collector of taxes to apply the amount of the tax credits against the future property taxes imposed on the property subject to the agreements.
- Verify reported information on tax credit applications to help ensure that the amount of each tax credit it issues is correct.
- Verify whether each property covered by an agreement is the same property that the Sterling County Appraisal District has identified as having received an appraisal limitation.

Chapter 7-E

Disclosing Conflicts of Interest

Sterling City ISD did not have a process to ensure that members of its school board, employees, and consultants disclosed conflicts of interest when it approved the applications for agreements.

At the time the Sterling City ISD school board approved the agreements with Goat Mountain Wind, LP and Goat Wind, LP, Sterling City ISD did not have a process that ensured the members of its school board, employees, and consultants disclosed business, professional, and personal relationships that may represent potential conflicts of interest, in accordance with Texas Local Government Code, Chapter 176. Members of the school board did not sign disclosure statements related to Sterling City ISD's agreements with Goat Mountain Wind, LP and Goat Wind, LP until a process was implemented approximately two years after the approval of those agreements. After Sterling City ISD created a disclosure process, three members of the school board disclosed that they had interests in land covered by the agreement with Goat Mountain Wind, LP.

Sterling City ISD's policy requires disclosure only when an employee, a member of its school board, or a consultant identifies a conflict of interest. That policy does not specifically require businesses that apply for agreements, members of the school board, employees, and consultants to disclose business, professional, or personal relationships related to the agreements that may pose a conflict of interest or affirm that conflicts do not exist on an annual basis.

Recommendations

Sterling City ISD should ensure that members of its school board, its employees, and its consultants follow its conflict of interest policy.

Administrative Processes

Opportunities exist for Sterling City ISD to strengthen certain administrative processes. While the following issues may not be material to determining compliance with Texas Tax Code, Chapter 313, they are significant to Sterling City ISD's management of its agreements with Goat Mountain Wind, LP and Goat Wind, LP:

- Sterling City ISD granted a job waiver for the Goat Wind, LP agreement in compliance with Texas Tax Code, Chapter 313, requirements. However, Sterling City ISD's documentation for that waiver did not include sufficient detail to show that Goat Wind, LP met the statutory criteria for receiving that waiver.
- Sterling City ISD's consultant accurately calculated the \$870,811 in revenue protection payments that Goat Mountain Wind, LP and Goat Wind, LP paid to Sterling City ISD. However, Sterling City ISD's use of those revenue protection payments may not be in accordance with Texas Tax Code, Chapter 313. The agreements with Goat Mountain Wind, LP and Goat Wind, LP and Texas Tax Code, Section 313.027(f)(1), specify that revenue protection payments are designed to offset future state revenues that the Sterling City ISD would have received for the school year if it had not entered into the agreements. However, Sterling City ISD deposited the revenue protection payments into an account held by its education foundation.
- Sterling City ISD did not establish a statutorily required link on its Web site to the Comptroller's Office Web site as required by Texas Tax Code, Section 313.0265(c).

Recommendations

Sterling City ISD should:

- For future agreements, require businesses that request a job waiver to provide detailed documentation that shows that the proposed number of jobs statutorily required to be created exceeds industry standards.
- Determine whether the current use of revenue protection payments complies with Texas Tax Code, Chapter 313.
- Provide a link on its Web site to the Comptroller's Office's Web site where appraisal limitation-related documents are made available to the public.

Management's Response from Sterling City ISD

BOARD PRESIDENT JASON COX
BOARD VICE PRESIDENT SCOT LONG
BOARD SECRETARY RANDY PARRISH

BOARD MEMBER JOSH GAINES
BOARD MEMBER WESLEY GLASS
BOARD MEMBER HEATH HUGHES
BOARD MEMBER OMEGA PENA

STERLING CITY INDEPENDENT SCHOOL DISTRICT

BOB RAUCH, Superintendent of Schools
P.O. BOX 786
Sterling City, Texas 76951

TY STEVENS – J.H. / High School
Principal

Telephone - 325-378-4781

MICHELE GUETERSLOH - Elementary
Principal

Fax - 325-378-2283

Formal Management Response **Sterling City Independent School District** Report on the Audit of Major Agreements under the Texas Economic Development Act

November 11, 2014

State Auditor's Office
ATTN: Mr. Willie Hicks
P.O. Box 12067
Austin, Texas 78711-2067

Dear Mr. Hicks:

In our response to your Audit of Major Agreements under the Texas Economic Development Act, we want to go on the record with some general comments of our perception of the program, given that we have several agreements in place and have some history with Chapter 313 in the Sterling City Independent School District (SCISD). We will then address the specific recommendations made to SCISD by topic within the Report.

General Comments

The District is not responsible for the design of compliance mandates; it is a state responsibility.

As a preliminary matter, the District views Chapter 313 of the Texas Tax Code and the rules adopted to implement Chapter 313 as a state program which is administered in part by the District. In order to ensure uniformity in the administration of the program, this District does not feel it is authorized to impose new obligations on the recipients of the program. Furthermore, the process of relying on "...data certified to the Comptroller by each recipient of a limitation on appraised value under this subchapter..." is set forth in Section 313.032(a) of the Texas Tax Code. In adopting such provisions, the Texas Legislature created a system designed to rely upon the disclosure of information directly from the applicant for a tax limitation. The District has therefore adopted this as its method of verifying compliance with the agreements.

Based on the specific comments discussed below, it is apparent that the State Auditor's Office is not satisfied with the applicants' reporting requirements and has consistently sought to impose new and unauthorized verification requirements on SCISD. Keeping in mind the admonitions set forth in Texas Tax Code 313.004(3)(A) that school districts strictly interpret the criteria set forth in Chapter 313, SCISD is reluctant to impose new requirements on Chapter 313 applicants in excess of those set forth in statute or state-agency-adopted administrative rule. SCISD will enforce any requirement legitimately adopted with respect to Chapter 313 agreements, as long as it does not impose uncompensated administrative costs on the District. In the absence of the adoption of new rules or other legal requirements, this District feels compelled to apply the rules and statutes as they currently exist.

With regard to the use of consultants, SCISD and similar school districts rely upon consultants to assist us in making the required calculations and reports to the Comptroller's Office. Given our limited resources, the 13-year duration of the prior agreements and turnover that does occur occasionally in terms of staff, having outside experts assist our District is critical to meeting our requirements under Chapter 313 for agreements with projects that have a very positive economic benefit.

Specific Statements of Facts and Responses to Recommendations

Chapter 7-A Processing Applications for Agreements

Management Statement of Fact

The District has a well-developed, articulated process for the processing of Chapter 313 applications which included more than relying on certified data from the companies.

The State Auditor's Office found that the District relied primarily on certified information provided by businesses in determining whether the projects would comply with the intent and purpose of Chapter 313 of the Texas Tax Code. It is significant to note that, since the inception of the program, applications have been required to be submitted under oath. Further, Chapter 313 Applications are governmental records under Tex. Penal Code § 37.01(2)(A); as a result, all statements contained therein are representations of fact within the meaning of Tex. Penal Code § 37.01(3). Since the adoption of findings and the approval of a Chapter 313 Agreement is an "official proceeding," a false statement on a Chapter 313 application constitutes perjury under Tex. Penal Code § 37.03. Sworn statements are routinely used as an acceptable verification method for reliance by fact finders in each of the three separate branches of government, including trials.

However, the District relied on independent information as well. In the case of the Goat Mountain Wind, LP, and Goat Wind, LP Applications under review, the economic impact review for each project was conducted by an independent consultant of the District, Texas Perspectives. Their reports provided the factual input for many of the Board's Findings. In 2009, as a part of HB 3676, the economic analysis was transferred by law to the Comptroller. Since that time, the Comptroller's economic impact study has supplied critical data for the required board findings.

In summary, the District's Trustees issued explicit fact findings in accordance with the provisions of Tex. Tax Code § 313.025(e-f) after the conclusion of an orderly, well-articulated process designed to consider all of the statutorily-required criteria. In

conformance with the strict construction mandate, no extraneous facts were considered. No principle of law is better settled than that that acts of discretion and findings-of-fact on the part of public officers to which such power is confided by law and not subject to reversal. (See *Williams v. Castleman*, 112 Tex. 193, 247 S.W. 263, 269 (1922).) Supervisory powers over decisions made by political subdivisions can only be invoked when the body acts beyond its jurisdiction or clearly abuses discretion conferred upon it by law. (See *Yoakum County v. Gaines County*, 139 Tex. 442, 163 S.W.2d 393, 396 (1942).)

Chapter 7-B Developing Agreements

Recommendations

Sterling City ISD should consider amending existing agreements to include:

- All required provisions and information related to the agreed-upon investment amounts and the anticipated number of jobs to be created; alternatively, it should explicitly state in agreements that the information in the related applications is incorporated into the agreements.
- Provisions that require Sterling City ISD to assess and approve the eligibility of any business to which an agreement is transferred.
- Performance standards or requirements for businesses to periodically submit deliverables that will enable it to hold businesses accountable for achieving desired results.

Management Response

Agreements in place contain provisions for the implementation of all the recommendations enumerated by the State Auditor's Office.

In its finding 7-B, the State Auditor's report suggested that the District should consider amending existing agreements to include:

1. All required provisions and information related to the agreed-upon investment amounts and the anticipated number of jobs to be created; alternatively, it should explicitly state in agreements that the information in the related applications is incorporated into the agreements;
2. Provisions that require Sterling City ISD to assess and approve the eligibility of any business to which an agreement is transferred.
3. Performance standards or requirements for businesses to periodically submit deliverables that will enable it to hold businesses accountable for achieving desired results.

These issues will be discussed in order below:

1. *Provisions related to investment amounts and anticipated jobs:* As an initial matter, the existing agreements **do** specifically incorporate the Application into the agreement. The Application is a defined term in the Agreement. The Applicant is required to create and retain the number of jobs set forth in the Application to Maintain a Viable Presence in the

District. And, failure to maintain this viable presence will result in the termination of the Agreement, and subject the Applicant to penalties, including the recoupment of all tax benefit received by the Applicant from the District by virtue of entering into the Agreement.

And, the applicant was bound by the statutory requirements set forth at Tex. Tax Code §313.021(2)(A)(iv)(b). The statutory requirement is incorporated into the agreement at Section 6.2(b) which requires the applicant to maintain a viable presence in the district, which in conformance with the term's definition in Section 1.3, included the maintenance, over the life of the agreement of the statutorily required number of jobs.

Also, the Agreement already has provisions related to required investment amounts. Sections 1.2 and 1.3 of both agreements define the tax limitation amount as being \$10 Million. At the time of the agreement Tex. Tax Code §§ 313.022(b) and 313.023 required the applicant's minimum Qualified Investment to be \$10 Million. That was the minimum amount of Qualified Investment required by the Agreement. T

2. *Provisions that require SCISD to assess the eligibility of any business to which an agreement is transferred:* Section 6.1 of the Goat Wind, LP agreement and Section 7.1 of the Goat Mountain Wind, LP agreement specifically require the applicant to provide the District and the County Appraisal District all data under the Texas Tax Code necessary to determine whether all obligations under the agreements are being met. Tex. Tax Code § 313.024(a) requires that Chapter 313 Agreements apply only to "property owned by an entity to which [Tax Code] Chapter 313 applies." In the event of such a transfer, the Trustees have ample authority to collect the data upon which continuing eligibility determinations can be made. In actual fact, such information is available on the Comptroller's website in the form of Certificates of Good Standing.

3. *Performance standards or requirements for businesses to periodically submit deliverables that will enable it to hold businesses accountable for achieving desired results:* As stated above, the Applicant is required under the terms of the Agreement to Maintain a Viable Presence in the District. Annual and biennial reporting requirements are set by Comptroller's rules. The reports as posted provide sufficient information to measure compliance with all current statutory mandates and the express terms of the Agreement.

Chapter 7-C Monitoring Compliance

Management Statement of Fact

In considering post-agreement compliance issues, the District relies upon statutorily valid sources, which produce a wide range of data, to verify information provided by companies.

The State Auditor's Office found that Sterling City ISD did not verify information provided by companies to demonstrate compliance with the agreements. However, the District has a process in place to verify, or requiring its consultant to verify, accuracy and completeness of information in annual eligibility reports and biennial progress report and has had such a process in place since the time it received its first compliance report. The information is reviewed to determine whether or not the company is in conformance with the investment and job creation requirements set forth in the agreements and in statute. The district also

annually verifies that the companies continue to remain eligible to receive the benefit of the value limitation.

It is significant to note that, since the inception of reporting requirements, reports have been required to be submitted under oath. Further, these reports are governmental records under Tex. Penal Code § 37.01(2)(A); as a result, all statements contained therein are representations of fact within the meaning of Tex. Penal Code § 37.01(3). Sworn statements are routinely used as an acceptable verification method for reliance by fact finders in each of the three separate branches of government, including trials. It is curious the State Auditor's Office, without citation to any other authority, would find this method of verification to be insufficient. See also, Tex. Tax Code 313.032.

Chapter 7-D Processing Tax Credits

Recommendations

Sterling City ISD should:

- Comply with its agreements related to tax credits, and direct the collector of taxes to apply the amount of the tax credits against the future property taxes imposed on the property subject to the agreements.
- Verify reported information on tax credit applications to help ensure that the amount of each tax credit it issues is correct.
- Verify whether each property covered by an agreement is the same property that the Sterling County Appraisal District has identified as having received an appraisal limitation.

Management Response

Tax Credit Reimbursement Requests are submitted in conformance with TEA requirements.

The District has a process in place to annually verify and determine eligibility of a company's tax credit. The District does rely on the Appraisal District and Tax Collector in identifying the property that is the subject of each application. But, the District has no authority over either independent entity in the naming convention used to identify specific parcels of property.

In order for SCISD to seek a state reimbursement under Section 42.2515 of the Education Code should a tax credit be owed, the TEA rule calls for the school district to submit "A copy of the tax bill sent to the taxpayer (showing the credit) or other proof that the school has reimbursed the tax credit to the taxpayer." However, the TEA procedures for the processing of tax credits currently in place require the District to present the Agency with proof of actual payment to the company of the tax credit amount as a prerequisite for reimbursement to the District, in lieu of a copy of a tax bill.

Over time, TEA has imposed varying requirements as a precondition of reimbursement. In light of the TEA's varying standards of compliance, it is imprudent to specify the conditions for payment of tax credit in the Agreement. The District's view is that the TEA rules and procedures are sufficient to ensure verification prior to expenditure by the state and ensure

that there is an appropriate “audit trail” in making state reimbursements to school districts for tax credits.

One issue that is a concern to SCISD is that the reimbursement payments from TEA are not as timely as the District would like and have created challenges in meeting our cash-flow needs. But it is unlikely that direct tax credits to Chapter 313 recipients would remedy that problem.

Chapter 7-E Disclosing Conflicts of Interest

Recommendations

- Sterling City ISD should ensure that members of its school board, its employees, and its consultants follow its conflict of interest policy

Management Response

The State Auditor’s recommended actions are unnecessary in light of explicit provisions of State law and SCISD policy that are currently in place.

Texas Local Gov’t Code §171.004 requires disclosure of conflicts of interest by all school Trustees and any other officer, including the Superintendent and the Business Manager/Chief Financial Officer. (See, Texas Local Gov’t Code §171.004(a).) Under Texas Local Gov’t Code §171.001(1), a “local public official” is defined as a member of the governing body or another officer, whether elected, appointed, paid, or unpaid, of any district (including a school district), central appraisal district, or other local governmental entity who exercises responsibilities beyond those that are advisory in nature.

A school officer has a substantial interest in a business entity if such a local public official or a person related to a local public official in the first degree by either affinity or consanguinity has a substantial interest in a business entity or in real property, the local public official, before a vote or decision on any matter involving the business entity or the real property, is specifically required by State law to file an affidavit with an official Board record keeper stating the nature and extent of the interest and shall abstain from further participation in the matter if:

1. In the case of a substantial interest in a business entity, the action on the matter will have a special economic effect on the business entity that is distinguishable from the effect on the public; or
2. In the case of a substantial interest in real property, it is reasonably foreseeable that an action on the matter will have a special economic effect on the value of the property, distinguishable from its effect on the public.

Under Texas Local Gov’t Code §171.002(a), a school officer has a substantial interest in a business entity if:

1. The person owns at least:
 - a. Ten percent of the voting stock or shares of the business entity, or
 - b. Either ten percent or \$15,000 of the fair market value of the business entity.
2. Funds received by the person from the business entity exceed ten percent of the person’s gross income for the previous year.

Under Texas Local Gov’t Code §171.002(b), a school officer has a substantial interest in real property if the interest is an equitable or legal ownership with a fair market value of \$2,500 or more.

Under Texas Local Gov't Code §171.002(c), a school officer is considered to have a substantial interest if a person related in the first degree by either affinity or consanguinity to the local public official, as determined under Government Code Chapter 573, Subchapter B, has a substantial interest as defined above.

Texas Local Gov't Code §171.003 generally provides that a local public official shall not knowingly:

1. Participate in a vote or decision on a matter involving a business entity or real property in which the local public official has a substantial interest if it is reasonably foreseeable that an action on the matter will have a special economic effect on the business entity or value of the property that is distinguishable from the effect on the public.
2. Act as surety for a business entity that has a contract, work, or business with the District.
3. Act as surety on any official bond required of an officer of the District.

Texas Local Gov't Code 176.003–.004 provides that a local government officer must file the required conflicts disclosure statement, as adopted by the Texas Ethics Commission, with a Chapter 313 Applicant, if the Applicant proposes to enter into a contract with the; and the Applicant:

1. Has an employment or other business relationship with the local government officer or a family member of the officer that results in the officer or family member receiving taxable income, other than investment income, that exceeds \$2,500 during the 12-month period preceding the date that the officer becomes aware that a contract has been executed or the District is considering entering into a contract with the person; or
2. Has given to the local government officer or a family member of the officer one or more gifts that have an aggregate value of more than \$250 in the 12-month period preceding the date the officer becomes aware that such a contract has been executed or the District is considering entering into a contract with the vendor.
3. A local government officer is not required to file a conflicts disclosure statement in relation to a gift accepted by the officer or a family member of the officer if the gift is:
 1. Given by a family member of the person accepting the gift;
 2. A political contribution as defined by Title 15, Election Code; or
 3. Food, lodging, transportation, or entertainment accepted as a guest.

A local government officer shall file the conflicts disclosure statement with the records administrator of the District not later than 5:00 p.m. on the seventh business day after the date on which the officer becomes aware of the facts that require the filing of the statement.

A local government officer commits a Class C misdemeanor if the officer knowingly violates this law. It is an exception to the application of the penalty that the local government officer filed the required conflicts disclosure statement not later than the seventh business day after receiving notice from the District of the alleged violation.

Texas Local Gov't Code §176.009 requires that if the school district that maintains an Internet Web site, it shall provide access on the District's Internet Web site to the conflicts disclosure statements and questionnaires required to be filed with the records administrator. (These disclosure forms are posted on the District's website.)

Under Texas Education Code §39.083; and 19 TAC § 109.1005 a school district's annual financial management report must include summary reports of reimbursement received by each Board member, reports of certain gifts from school vendors, and reports of Board member business transactions with the District.

SCISD Board adopted policies BBFA (Legal) and CFA (Legal) specifically require of each Trustee the filing of the required reports and disclosures. These policies are binding on each individual Trustee. The Policies albeit having been occasionally amended to ensure compliance with amendments to State law, have been in effect at all times material to the

negotiation and management of all Tax Code Chapter 313 agreements to which the District has been a party.

In sum, the State Auditor's suggestion that the District include some form of additional and undifferentiated conflict-of-interest requirement upon individual board members who are not legal parties to a Chapter 313 Agreement is redundant to the very explicit and exacting provisions of State law and district policy; would be legally ineffective; and, would create additional and unnecessary bureaucratic hurdles in an already complex system.

Chapter 7-F Administrative Processes

Recommendations

Sterling City ISD should:

- For future agreements, require businesses that request a job waiver to provide detailed documentation that shows that the proposed number of jobs statutorily required to be created exceeds industry standards.
- Determine whether the current use of revenue protection payments complies with Texas Tax Code, Chapter 313.
- Provide a link on its Web site to the Comptroller's Office's Web site where appraisal limitation related documents are made available to the public.

Management Response

The job-waiver requests were approved on the basis of what were industry standards at the time of the adoption of the agreements.

The requirement to provide detailed information already exists. For example, at the time the applications were approved, the District was informed by industry sources and District consultants that the industry standard was one permanent job for every 15 wind turbines. That was the basis for the District deliberations on this issue. Plus, the District had the Comptroller determination that the waiver met industry standards.

The use of the revenue-protection payments complies with Chapter 313 of the Tax Code.

One concern raised by the State Auditor's Office is that revenue protection funds were deposited directly into the District's foundation rather than its General Fund. The use of the revenue-protection payments is not specified under Chapter 313. Section 313.027(f) specifies provisions that provide for revenue protection but do not direct the use of these funds:

Subsection 313.027 (f): In addition, the agreement:

- (1) must incorporate each relevant provision of this subchapter and, to the extent necessary, include provisions for the protection of future school district revenues through the adjustment of the minimum valuations, the payment of revenue offsets, and other mechanisms agreed to by the property owner and the school district.

The District budgeted sufficient funds in expectation that the funds from the Agreement would be deposited into the foundation. Any revenue offset funds from a third-party that are deposited in the District's foundation must be used for educational and instructional purposes that benefit the students of SCISD. The terms of the statute have been met.

In response to the Auditor's finding, the Superintendent directed that the District's webmaster provide a link to the Comptroller's Chapter 313 website on the District's website. The link is currently available on the District's website, under the "Required Postings" Directory.

Appendices

Appendix 1

Objectives, Scope, and Methodology

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.
- Determine whether there are ways to increase the efficiency and effectiveness of the administration of the Texas Economic Development Act.

Scope

The scope of this audit covered selected applications and appraisal limitation agreements (agreements) processed from September 1, 2003, through December 31, 2013.

Methodology

The audit methodology included selecting seven agreements for audit. Auditors selected the agreements based on which agreements had the largest estimated net tax benefit reported for each business category eligible to have an agreement. For the agreements selected, auditors also considered whether the related school district had (1) additional agreements with the business or (2) granted a job waiver on any other agreements. The seven agreements selected included:

- One agreement between the Austin Independent School District (Austin ISD) and Hewlett-Packard Company for property used in research and development.
- Two agreements between the Fort Stockton Independent School District (Fort Stockton ISD) and SandRidge Energy, Inc. for property used in manufacturing.

- Two agreements with the Palacios Independent School District (Palacios ISD). One agreement was between Palacios ISD and NRG South Texas 3 LLC and NRG South Texas LP. The other agreement was between Palacios ISD and NRG South Texas 4 LLC and NRG South Texas LP. Both agreements involved property used in nuclear electric power generation.
- Two agreements with the Sterling City Independent School District (Sterling City ISD). One agreement was between Sterling City ISD and Goat Mountain Wind, LP. The other agreement was between Sterling City ISD and Goat Wind, LP. Both agreements involved property used in renewable energy electric generation (wind farms). Sterling City ISD approved a job waiver for its agreement with Goat Wind, LP.

The audit methodology also included testing applications, agreements, progress reports, tax credit documentation, and conducting interviews with the members of the school boards and boards of trustees, county appraisers, consultants, management, and staff.

In addition, the audit methodology included collecting information and documentation, performing selected tests and other procedures, analyzing and evaluating the results of the tests, and conducting interviews with the Office of the Comptroller of Public Accounts' (Comptroller's Office) and the Texas Education Agency's (TEA) management and staff.

Sampling

To test compliance with disclosure requirements for conflicts of interest for management and staff involved in the review and approval of applications and processing school districts' requests for additional state aid for tax credits issued, auditors obtained from the four selected school districts, the Comptroller's Office, and TEA a list of management and staff involved in those review and approval processes. Auditors tested those individuals' compliance with applicable disclosure requirements.

For the samples discussed below, auditors applied a nonstatistical methodology. The sample items generally were not representative of the entire population and, therefore, it would not be appropriate to extrapolate results to the population. Auditors selected the following samples:

- To test compliance and processing controls for applications at the Comptroller's Office, auditors used professional judgment to select 80 applications that were processed during the audit scope. The sample included the seven selected agreements for which auditors performed a site visit at the associated school district.
- To test compliance and processing controls for applications at TEA, auditors used professional judgment to select 80 applications that were

processed during the audit scope. The sample included the applications for the seven selected agreements for which auditors performed a site visit at the associated school district.

- To test compliance with requirements that specify the provisions that must be included in agreements, auditors used professional judgment to select 48 agreements that were executed during the audit scope. The sample included the seven agreements for which auditors performed a site visit at the associated school district.
- To test TEA's internal controls for processing requests for additional state aid to school districts that issued tax credits, auditors used professional judgment to select 59 payments during the audit scope. The sample included payments to the four school districts that auditors visited.
- To test processing controls for developing the Comptroller's Office's *Report of the Texas Economic Development Act*, January 2013, auditors used professional judgment to select 20 agreements executed during the audit scope. The sample included the seven agreements for which auditors performed a site visit at the associated school district.

Data Reliability

Auditors' assessment of the reliability of property tax data from the Comptroller's Office's Property Tax System was based on reconciling that data to county appraisal districts' property tax reports submitted to the Comptroller's Office. Auditors determined that data was sufficiently reliable for the purposes of this audit.

Auditors' assessment of the reliability of additional state aid payment data from TEA's Foundation School Program System relied on prior audit work performed. Auditors determined that data was sufficiently reliable for the purposes of this audit.

Auditors assessed the reliability of data processed by the software program that TEA uses to evaluate school finance projections. Auditors were unable to determine whether that data was sufficiently reliable for the purposes of this audit. TEA did not maintain a log of the changes it made to that software program. Therefore, auditors did not rely on it for this audit.

Information collected and reviewed included the following:

- Agreements between school districts and businesses.
- Application documentation, including economic impact evaluations, school district financial projections, school board findings, recommendations, and correspondence from the Comptroller's Office to school districts and from TEA to the Comptroller's Office.

- Minutes from school districts' school board meetings.
- Annual eligibility reports, biennial progress reports, biennial cost data request reports, and *Report on Value Loss Because of Value Limitations Under Tax Code Chapter 313*.
- Conflict of interest statements signed by selected school districts' school board members, trustees, management, and staff.
- Tax credit applications, requests for additional state aid, property tax bills, property tax receipts, and tax credit payments.
- Agreements between school districts and consultants.
- Property tax data reported to the Comptroller's Office for tax years 2005 to 2013.
- Biennial progress data used to develop the *Report of the Texas Economic Development Act*, January 2013.

Procedures and test conducted included the following:

- Interviewed members of each selected school districts' school board, management, staff, and consultants.
- Interviewed management and staff of the Comptroller's Office and TEA.
- Reviewed school district policies and procedures.
- Reviewed school board meeting minutes.
- Reviewed conflict of interest statements prepared by members of school boards and school district management and staff.
- Reviewed application documentation.
- Reviewed agreement terms and conditions.
- Reviewed consultant contracts with school districts.
- Tested a sample of applications the Comptroller's Office reviewed from January 1, 2003, through December 31, 2013.
- Tested a sample of agreements executed between January 1, 2003, and December 31, 2013.
- Reviewed annual eligibility reports, biennial progress reports, and biennial cost data request reports for selected agreements.

- Reviewed tax credit applications, tax receipts, tax bills, and tax credit payments.

Criteria used included the following:

- Texas Tax Code, Chapters 171 and 313.
- Texas Local Government Code, Chapters 171 and 176.
- Texas Education Code, Chapters 41 and 42.
- Title 34, Texas Administrative Code, Chapter 9.
- Title 19, Texas Administrative Code, Chapter 61.
- Comptroller's Office policies and procedures.
- TEA policies and procedures.
- Selected school districts' contracts with consultants.
- Selected school districts' policies, procedures, and board meeting minutes.
- Comptroller's Office's Report of the Texas Economic Development Act, January 2013.

Project Information

Audit fieldwork was conducted from March 2014 through July 2014. 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:

- Willie J. Hicks, MBA, CGAP (Project Manager)
- Jennifer Lehman, MBA, CIA, CFE, CGAP (Assistant Project Manager)
- Pamela A. Bradly, CPA
- Cheryl Durkop
- John Paul Hicks, MBA
- Kyle Ketry
- Joe Kozak, CPA, CISA

- Thomas Mahoney, CGAP
- Sarah Miller
- Tessa Mlynar, CFE
- Shelby Rounsaville
- Jacqueline Thompson
- Tammie Wells, MBA
- Richard Wyrick, MBA
- Julia Youssefnia, MPA, CPA
- Dennis Ray Bushnell, CPA (Quality Control Reviewer)
- Verma Elliott, MBA, CPA, CIA, CGAP (Audit Manager)

Selected Information on the Seven Agreements Audited

Table 5 shows selected background and financial information related to the seven appraisal limitation agreements (agreements) audited. Specifically:

- Austin Independent School District's (Austin ISD) agreement with Hewlett-Packard Company.
- Fort Stockton Independent School District's (Fort Stockton ISD) two agreements with SandRidge Energy, Inc.
- Palacios Independent School District's (Palacios ISD) agreements with NRG South Texas 3⁵ and NRG South Texas 4.⁶
- Sterling City Independent School District's (Sterling City ISD) agreements with Goat Mountain Wind, LP and Goat Wind, LP.

Table 5

| Background Information on Appraisal Limitation Agreements Audited | | | | | | | |
|---|--------------------------|------------------------|------------------------|-----------------------------------|-----------------------------------|--|--|
| Business with Agreement | School Districts | | | | | | |
| | Austin ISD | Fort Stockton ISD | | Palacios ISD | | Sterling City ISD | |
| | Hewlett-Packard Company | SandRidge Energy, Inc. | SandRidge Energy, Inc. | NRG South Texas 3 | NRG South Texas 4 | Goat Mountain Wind, LP | Goat Wind, LP |
| Application Number | 40 | 134 | 135 | 118 | 119 | 65 | 84 |
| Business Category | Research and development | Manufacturing | Manufacturing | Nuclear electric power generation | Nuclear electric power generation | Renewable energy electric generation (wind farm) | Renewable energy electric generation (wind farm) |
| County | Travis | Pecos | Pecos | Matagorda | Matagorda | Sterling | Sterling |
| Type of School District | Non-rural | Rural | Rural | Rural | Rural | Rural | Rural |
| Agreement Execution Date | November 6, 2006 | December 22, 2008 | December 22, 2008 | June 9, 2008 | June 9, 2008 | December 17, 2007 | December 20, 2007 |

⁵ The agreement is with NRG South Texas 3 LLC and NRG South Texas LP. For the purposes of this report, those two businesses collectively are referred to as NRG South Texas 3.

⁶ The agreement is with NRG South Texas 4 LLC and NRG South Texas LP. For the purposes of this report, those two businesses collectively are referred to as NRG South Texas 4.

**Background Information on
Appraisal Limitation Agreements Audited**

| Business with Agreement | School Districts | | | | | | |
|---|--|--|--|--|--|--|--|
| | Austin ISD | Fort Stockton ISD | | Palacios ISD | | Sterling City ISD | |
| | Hewlett-Packard Company | SandRidge Energy, Inc. | SandRidge Energy, Inc. | NRG South Texas 3 | NRG South Texas 4 | Goat Mountain Wind, LP | Goat Wind, LP |
| Length of Agreement | January 1, 2007, through December 31, 2019 | January 1, 2009, through December 31, 2021 | January 1, 2009, through December 31, 2021 | January 1, 2009, through December 31, 2029 | January 1, 2009, through December 31, 2029 | January 1, 2008, through December 31, 2020 | January 1, 2008, through December 31, 2020 |
| Appraisal Limitation | \$100,000,000 | \$20,000,000 | \$20,000,000 | \$30,000,000 | \$30,000,000 | \$10,000,000 | \$10,000,000 |
| Tax Year 2013 Appraised Value | \$87,334,261 | \$373,711,430 | \$23,834,130 | \$0 | \$0 | \$188,114,000 | \$12,446,980 |
| Net Tax Benefit to Business (reported on the 2012 Biennial Cost Data Request Form) | \$133,904 | \$7,590,537 | \$225,465 | \$0 | \$0 | \$1,037,110 | \$110,186 |
| Number of Qualifying Jobs Created as Reported by the Business (as of December 31, 2012) | 22 | 22 | 2 | 0 | 0 | 31 | 6 |
| Projected Qualified Jobs to Be Created | 140 | 35 | 16 | 250 | 250 | 10 | 8 |
| Total Tax Credits Paid (as of December 31, 2013) | \$0 | \$114,052 | \$10,944 | \$0 | \$0 | \$1,610,590 | \$20,712 |
| Total Projected Investment | \$710,900,000 | \$835,200,000 | \$367,000,000 | \$4,036,235,990 | \$4,306,316,835 | \$800,000,000 | \$189,300,000 |
| Qualified Investment (as of December 31, 2013) | \$307,610,119 | \$556,827,840 | \$26,775,805 | \$0 | \$0 | \$272,624,306 | \$25,000,000 |

**Background Information on
Appraisal Limitation Agreements Audited**

| Business with Agreement | School Districts | | | | | | |
|--|---|---------------------------|---------------------------|--------------------------|--------------------------|---|---------------------------|
| | Austin ISD | Fort Stockton ISD | | Palacios ISD | | Sterling City ISD | |
| | Hewlett-Packard Company | SandRidge Energy, Inc. | SandRidge Energy, Inc. | NRG South Texas 3 | NRG South Texas 4 | Goat Mountain Wind, LP | Goat Wind, LP |
| Projected Total Net Tax Benefit to Business | \$4,137,264 | \$55,211,977 | \$23,059,446 | \$146,131,026 | \$140,483,818 | \$68,039,903 | \$675,507 |
| Total Tax Credits the Business is Eligible to Receive | \$419,447 | \$798,365 | \$76,609 | \$0 | \$0 | \$14,695,355 | \$48,327 |
| Revenue Protection Payments School District Received from Business (as of December 31, 2013) | \$21,291 | \$172,946 | \$5,787 | \$0 | \$0 | \$864,305 | \$6,506 |
| Supplemental Payments School District Received from Business (as of December 31, 2013) | \$96,964 ^a | \$4,472,991 ^b | \$98,793 ^c | \$1,750,000 ^d | \$1,750,000 ^e | \$9,298,549 ^f | \$73,368 ^g |
| Other Tax Abatements and Other Economic Development Incentives Business Received | Property Tax Abatement-Travis County ^h Property Tax Abatement-City of Austin ⁱ | Not Reported ^j | Not Reported ^j | None | None | Property Tax Abatement-Sterling County ^k | Not Reported ^l |

**Background Information on
Appraisal Limitation Agreements Audited**

| Business with Agreement | School Districts | | | | | | |
|-------------------------|-------------------------|------------------------|------------------------|-------------------|-------------------|------------------------|---------------|
| | Austin ISD | Fort Stockton ISD | | Palacios ISD | | Sterling City ISD | |
| | Hewlett-Packard Company | SandRidge Energy, Inc. | SandRidge Energy, Inc. | NRG South Texas 3 | NRG South Texas 4 | Goat Mountain Wind, LP | Goat Wind, LP |

- ^a Article IV of the agreement required Hewlett-Packard Company to make a one-time contribution of \$70,000 and annual payments to Austin ISD equal to 15 percent of the net taxable benefit that it receives as determined by Austin ISD’s consultant during the term of the agreement.
- ^b Article IV of the agreement required SandRidge Energy, Inc. to make annual payments to Fort Stockton ISD equal to 40 percent of the net tax benefit that it receives as a result of the agreement for tax years 2011 through 2021.
- ^c Article IV of the agreement required SandRidge Energy, Inc. to make annual payments to Fort Stockton ISD equal to 40 percent of the net tax benefit that it receives as a result of the agreement for tax years 2011 through 2021.
- ^d Article IV of the agreement required NRG South Texas 3 to make annual contributions to the Palacios ISD Education Foundation in the amounts listed and scheduled in the agreement. In addition, NRG South Texas 3 was required to make annual payments to Palacios ISD equal to 5 percent of the net tax benefit that it receives as a result of the agreement. Amounts reported are for total payments received for tax years 2009, 2010, and 2011.
- ^e Article IV of the agreement required NRG South Texas 4 to make annual contributions to the Palacios ISD Education Foundation in the amounts listed and scheduled in the agreement. In addition, NRG South Texas 4 was required make annual payments to Palacios ISD equal to 5 percent of the net tax benefit that it receives as a result of the agreement. Amounts reported are for total payments received for tax years 2009, 2010, and 2011.
- ^f Article IV of the agreement required Goat Mountain Wind, LP to make annual payments to Sterling City ISD equal to 40 percent of the net tax benefit that it receives as a result of the agreement for tax years 2010 through 2020.
- ^g Article IV of the agreement required Goat Wind, LP to make annual payments to Sterling City ISD equal to 40 percent of the net tax benefit that it receives as a result of the agreement for tax years 2010 through 2020.
- ^h Travis County provides an additional 60 percent property tax abatement on the property under the agreement. The Travis Central Appraisal District reported that the tax abatement is for a 10-year period that started in tax year 2008.
- ⁱ The City of Austin provides an additional 40 percent property tax abatement on the property under the agreement. The Travis Central Appraisal District reported that the tax abatement is for a 10-year period that started in tax year 2007.
- ^j The Pecos County Appraisal District did not respond to requests for information on other tax abatements and economic development incentives given to the property under the agreement.
- ^k Sterling County provides an additional 10-year property tax abatement on the property under the agreement. The amount of the tax abatement may range from 60 percent to 70 percent during the first five years of the agreement and from 30 percent to 40 percent during the last five years of the agreement. The percentage of the property tax abatement depends on the amount of electricity generated by the property each tax year. The Sterling County Appraisal District reported that the tax abatements for Goat Mountain Wind, LP started in tax year 2009.
- ^l The Sterling County Appraisal District did not provide information on whether the property under the agreement had received property tax abatements or other economic development incentives.

Sources: Information from school districts, county appraisal districts, and the Office of the Comptroller of Public Accounts.

Summary of Additional State Aid Paid and Projected to Be Paid from September 1, 2009, through December 31, 2030

According to Texas Education Code, Section 42.2515, the Texas Education Agency (TEA) may provide additional state aid payments to school districts through the school finance system for tax credits that school districts issue to businesses with which they have appraisal limitation agreements (agreements). Those tax credits total an estimated \$812 million from tax year 2009 through tax year 2030.

The Office of the Comptroller of Public Accounts (Comptroller's Office) had processed 242 executed agreements and 57 applications as of December 31, 2013. The financial information the Comptroller's Office collected indicated the following:

- An estimated \$202 million in tax credits may be issued to businesses associated with 127 agreements executed from tax year 2003 through tax year 2011.
- An estimated \$411 million in tax credits may be issued to businesses associated with 115 agreements executed from January 2012 through December 2013.
- An estimated \$199 million in tax credits may be issued to businesses associated with 57 applications that the Comptroller's Office had recommended for agreements but did not have executed agreements as of December 2013.

As of December 31, 2013, TEA had paid a total of \$26 million to 47 school districts that had requested additional state aid for tax credits paid to businesses with agreements from tax year 2006 through tax year 2013. Approximately \$786 million in additional state aid may be paid to school districts with the agreements that may be owed tax credits from tax year 2014 to tax year 2030.

Texas Tax Code, Sections 313.103 and 313.104

Texas Tax Code, Sections 313.103 and 313.104, below describe the purpose and intent, respectively, for Texas Tax Code, Chapter 313, as of December 31, 2013.

Sec. 313.003. PURPOSES. The purposes of this chapter are to:

- (1) encourage large-scale capital investments in this state, especially in school districts that have an ad valorem tax base that is less than the statewide average ad valorem tax base of school districts in this state;
- (2) create new, high-paying jobs in this state;
- (3) attract to this state new, large-scale businesses that are exploring opportunities to locate in other states or other countries;
- (4) enable local government officials and economic development professionals to compete with other states by authorizing economic development incentives that meet or exceed incentives being offered to prospective employers by other states and to provide local officials with an effective means to attract large-scale investment;
- (5) strengthen and improve the overall performance of the economy of this state;
- (6) expand and enlarge the ad valorem property tax base of this state; and
- (7) enhance this state's economic development efforts by providing school districts with an effective local economic development option.

Sec. 313.004. LEGISLATIVE INTENT. It is the intent of the legislature in enacting this chapter that:

- (1) economic development decisions should occur at the local level and be consistent with identifiable statewide economic development goals;
- (2) this chapter should not be construed or interpreted to allow:
 - (A) property owners to pool investments to create sufficiently large investments to qualify for an ad valorem tax benefit or financial benefit provided by this chapter;
 - (B) an applicant for an ad valorem tax benefit or financial benefit provided by this chapter to assert that jobs will be eliminated if certain investments are not made if the assertion is not true; or

(C) a sole proprietorship, partnership, or limited liability partnership to receive an ad valorem tax benefit or financial benefit provided by this chapter; and

(3) in implementing this chapter, school districts should:

(A) strictly interpret the criteria and selection guidelines provided by this chapter; and

(B) approve only those applications for an ad valorem tax benefit or financial benefit provided by this chapter that:

(i) enhance the local community;

(ii) improve the local public education system;

(iii) create high-paying jobs; and

(iv) advance the economic development goals of this state as identified by the Texas Strategic Economic Development Planning Commission.

Property Tax Revenue Losses Related to Agreements for Tax Years 2005 through 2013

The tables below summarize (1) property values that all county appraisal districts in Texas reported to the Office of the Comptroller of Public Accounts (Comptroller's Office) and (2) property values that county appraisal districts with appraisal limitation agreements (agreements) reported to the Comptroller's Office. For tax years 2005 through 2013, the county appraisal districts reported that property tax revenue losses for properties covered by agreements totaled an estimated \$905.2 million. Tables 6 and 7 show the property tax revenue losses reported for tax years 2011 through 2013. Tables 8 and 9 show the property tax revenue losses reported for tax years 2005 through 2010. Prior to tax year 2011, property tax losses were calculated based on the weighted average loss between the taxable value for maintenance and operations purposes and the taxable value for interest and sinking fund purposes.

Table 6 summarizes the property values that all county appraisal districts reported for tax years 2011 through 2013. Table 7 summarizes the property values that county appraisal districts with agreements reported for those same tax years.

Table 6

| Statewide Property Values Reported by All County Appraisal Districts in Texas Tax Year 2011 through Tax Year 2013 | | | | | | |
|--|---------------------|---|--|-------------------------|---|--|
| Tax Year | Appraisal Value | Taxable Value for Maintenance and Operations Purposes | Taxable Value for Interest and Sinking Fund Purposes | Property Tax Revenue | Property Tax Revenue Lost from Agreements | Percent of Property Tax Revenue Lost According to County Appraisal District (calculated by auditors) |
| 2013 | \$2,326,066,320,168 | \$1,880,119,552,001 | \$1,899,812,042,303 | \$24,854,671,461 | \$222,578,432 | 0.90% |
| 2012 | \$2,208,817,007,702 | \$1,752,926,534,827 | \$1,769,849,324,749 | 23,072,781,962 | 221,572,866 | 0.96% |
| 2011 | \$2,120,439,535,886 | \$1,673,870,904,780 | \$1,688,998,383,088 | 22,002,289,358 | 196,651,641 | 0.89% |
| Totals | | | | \$69,929,742,781 | \$640,802,939 | |

Source: Comptroller's Office.

Table 7

| Property Values Reported by County Appraisal Districts with Agreements in Texas Tax Year 2011 Through Tax Year 2013 | | | | | | | |
|--|-------------------|---|--|------------------------|---|--|--|
| Tax Year | Appraisal Value | Taxable Value for Maintenance and Operations Purposes | Taxable Value for Interest and Sinking Fund Purposes | Property Tax Revenue | Property Tax Revenue Lost from Agreements | Percent of Property Tax Revenue Lost According to County Appraisal District (calculated by auditors) | Average Percent of School District Revenue Loss (calculated by auditors) |
| 2013 | \$155,664,829,687 | \$124,154,987,365 | \$141,018,649,658 | \$1,920,441,112 | \$222,578,432 | 11.59% | 26.52% |
| 2012 | \$144,640,754,718 | \$115,639,533,513 | \$132,562,323,435 | 1,542,029,240 | 221,572,866 | 14.37% | 64.32% |
| 2011 | \$123,550,406,163 | \$98,375,414,115 | \$113,502,892,423 | 1,326,753,181 | 196,651,641 | 14.82% | 68.18% |
| Totals | | | | \$4,789,223,533 | \$640,802,939 | | |

Source: Comptroller's Office.

Table 8 summarizes the property appraisal values that all county appraisal districts reported for tax years 2005 through 2010. Table 9 summarizes the property appraisal values that county appraisal districts with agreements reported for those same tax years.

Table 8

| Statewide Property Values Reported by All County Appraisal Districts in Texas Tax Year 2005 through Tax Year 2010 | | | | | |
|--|---------------------|---------------------|--------------------------|--|--|
| Tax Year | Appraisal Value | Taxable Value | Property Tax Revenue | Property Tax Revenue Lost from Agreements (calculated by auditors) | Percent of Property Tax Revenue Lost According to County Appraisal District (calculated by auditors) |
| 2010 | \$2,094,207,272,645 | \$1,655,152,584,816 | \$ 21,558,289,126 | \$117,276,160 | 0.54% |
| 2009 | \$2,120,661,300,153 | \$1,683,700,155,921 | 21,751,400,885 | 66,577,117 | 0.31% |
| 2008 | \$2,086,830,275,980 | \$1,663,375,273,082 | 21,149,319,188 | 40,796,278 | 0.19% |
| 2007 | \$1,876,060,708,651 | \$1,500,811,983,249 | 18,817,215,656 | 23,664,901 | 0.13% |
| 2006 | \$1,673,514,101,939 | \$1,348,691,120,811 | 20,811,701,140 | 10,597,708 | 0.05% |
| 2005 | \$1,490,671,558,947 | \$1,198,525,740,074 | 20,150,818,051 | 5,529,909 | 0.03% |
| Totals | | | \$124,238,744,046 | \$264,442,073 | |

Source: Comptroller's Office.

Table 9

| Property Values Reported by County Appraisal Districts with Agreements in Texas Tax Year 2005 Through Tax Year 2010 | | | | | | |
|--|-------------------|-------------------|------------------------|---|--|--|
| Tax Year | Appraisal Value | Taxable Value | Tax Levy | Property Tax Revenue Lost from Agreements | Percent of Property Tax Revenue Lost According to County Appraisal District (calculated by auditors) | Average Percent of School District Revenue Loss (calculated by auditors) |
| 2010 | \$175,730,901,354 | \$150,622,155,575 | \$1,922,644,398 | \$117,276,160 | 6.10% | 6.10% |
| 2009 | \$151,297,694,986 | \$131,127,734,455 | 1,631,057,616 | 66,577,117 | 4.08% | 4.08% |
| 2008 | \$78,916,982,668 | \$67,752,556,214 | 867,518,962 | 40,796,278 | 4.70% | 4.70% |
| 2007 | \$67,814,965,270 | \$59,179,390,554 | 731,319,717 | 23,664,901 | 3.24% | 3.24% |
| 2006 | \$24,918,316,302 | \$21,223,540,136 | 294,425,873 | 10,597,708 | 3.60% | 3.60% |
| 2005 | \$14,068,655,865 | \$11,688,382,889 | 183,598,621 | 5,529,909 | 3.01% | 3.01% |
| Totals | | | \$5,630,565,187 | \$264,442,073 | | |

Source: Comptroller's Office.

Table 10 summarizes the total reported property tax revenue lost from agreements for tax years 2005 through 2013.

Table 10

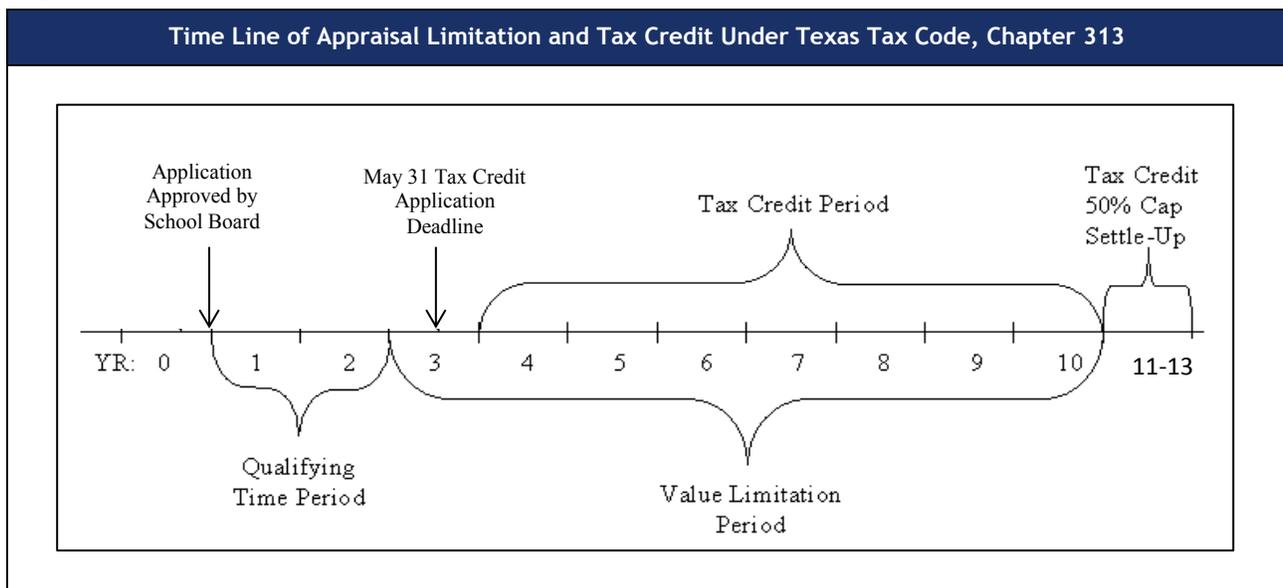
| Total Reported Property Tax Revenue Lost from Agreements | |
|--|---------------------------|
| Tax Years | Property Tax Revenue Lost |
| 2011 through 2013 | \$ 640,802,939 |
| 2005 through 2010 | 264,442,073 |
| Total | \$905,245,012 |

Source: Comptroller's Office.

Time Line of Appraisal Value Limitations and Tax Credits Under Texas Tax Code, Chapter 313

Figure 1 shows an example of a time line for an appraisal limitation and tax credit under Texas Tax Code, Chapter 313, as illustrated by the Office of the Comptroller of Public Accounts (Comptroller's Office). It describes appraisal limitation agreements (agreements) for which the Comptroller's Office reviewed applications from January 1, 2002, through December 31, 2013.

Figure 1



Source: Comptroller's Office.

Each year on the time line starts on January 1, the beginning of a new tax year. The agreement begins on January 1 of year 1 on the time line. There is a two-year qualifying time period (the qualifying time period may be longer for an agreement involving advanced clean energy and nuclear electric power generation as allowed by statute), followed by an eight-year appraisal limitation period. After the third year, the next seven years of the agreement is also a tax credit period. The three years after the appraisal limitation period expires is the tax credit settle-up period during which a business is entitled to any tax credit remaining from an agreement. The tax credit received during any tax year cannot exceed 50 percent of the property taxes paid in that tax year.

The time line reflects changes the Legislature made to Texas Tax Code, Chapter 313. Specifically:

- House Bill 1470 (80th Legislature, Regular Session) expanded the tax credit settle-up period from one year to three years. That change was effective on June 15, 2007.

- House Bill 3676 (81st Legislature, Regular Session) changed the default beginning of the qualifying time period from January 1 of the year following school board approval of the application to the execution date of the agreement (unless otherwise deferred). That change was effective June 19, 2009.

Glossary of Selected Terms Related to Agreements

Table 11 lists the definitions for certain terms used in the administration of appraisal limitation agreements (agreements).

Table 11

| Glossary of Selected Terms Related to Agreements | |
|--|--|
| Term | Definition |
| Annual Eligibility Report | <p>The Office of the Comptroller of Public Accounts (Comptroller's Office) requires each agreement holder or its authorized representative to submit <i>Annual Eligibility Reports</i> to the school district by May 15 of every year and to use information from the previous tax year in those reports. See Appendix 11 for an example of the reporting form that is used.</p> <p>School districts are required to review those reports, retain the original reports, and submit PDF versions of the completed and signed reports and any attachments to the Comptroller's Office by June 15 of every year.</p> |
| Biennial Progress Report | <p>The Comptroller's Office requires each agreement holder or its authorized representative to submit <i>Biennial Progress Reports</i> to the school district by May 15 of each even-numbered year. See Appendix 11 for an example of the reporting form that is used.</p> <p>The Comptroller's Office requests that that agreement holder complete the spreadsheet version of the <i>Biennial Progress Report</i> and submit both an unsigned electronic version and a signed hard-copy version (with any attachments) to the school district. School districts are required to forward those reports to the Comptroller's Office by June 15 of each even-numbered year.</p> |
| Biennial School District Cost Data Request Form | <p>The Comptroller's Office requires school districts to submit the Biennial School District Cost Data Request Form to the Comptroller's Office by July 15 of each even-numbered year. That form indicates, for each project that is the subject of an agreement, actual and estimated property values, tax rates, payments in lieu of taxes, extraordinary educational expenses, and revenue protection payments.</p> |
| Payments in lieu of taxes | <p>The terms of the agreements audited specified that payments in lieu of taxes are intended to support a school district as a result of its consideration in executing an agreement with a business. The business pays the school district an annual payment that is based on a percentage of the net tax benefit the business receives each tax year.</p> |
| Revenue protection payments | <p>Revenue protection payments are intended to protect a school district against any loss of maintenance and operations tax revenues as a result of an agreement. They also may include any costs that the school district incurs during the term of the agreement, which include but are not limited to:</p> <ul style="list-style-type: none"> ▪ Tax credits for which a school district does not receive additional state aid from the State. ▪ Any loss in the event of a judgment involving an agreement. ▪ Attorney fees or other costs incurred in any legal defense of an agreement. <p>Agreements may require that the payment calculation be based on annual certified tax roll data prepared by the county appraisal district.</p> |
| Qualifying investment | <p>As of December 31, 2013, Texas Tax Code, Section 313.021(1), defined qualifying investment as:</p> <ul style="list-style-type: none"> ▪ Tangible personal property that is first placed in service in Texas during the applicable qualifying time period that begins on or after January 1, 2002, without regard to whether the property is affixed to or incorporated into real property, and that is described as Section 1245 property by Section 1245(a) of the U.S. Internal Revenue Code of 1986. ▪ Tangible personal property that is first placed in service in Texas during the applicable qualifying time period that begins on or after January 1, 2002, without regard to whether the property is affixed to or incorporated into real property, and that is used in connection with the manufacturing, processing, or fabrication in a |

Glossary of Selected Terms Related to Agreements

| Term | Definition |
|------------------------|--|
| | <p>cleanroom environment of a semiconductor product, without regard to whether the property is actually located in the cleanroom environment, including:</p> <ul style="list-style-type: none"> ◆ Integrated systems, fixtures, and piping. ◆ All property necessary or adapted to reduce contamination or to control airflow, temperature, humidity, chemical purity, or other environmental conditions or manufacturing tolerances. ◆ Production equipment and machinery, moveable cleanroom partitions, and cleanroom lighting. <ul style="list-style-type: none"> ■ Tangible personal property that is first placed in service in Texas during the applicable qualifying time period that begins on or after January 1, 2002, without regard to whether the property is affixed to or incorporated into real property, and that is used in connection with the operation of a nuclear electric power generation facility, including: <ul style="list-style-type: none"> ◆ Property, including pressure vessels, pumps, turbines, generators, and condensers, used to produce nuclear electric power. ◆ Property and systems necessary to control radioactive contamination. ■ Tangible personal property that is first placed in service in Texas during the applicable qualifying time period that begins on or after January 1, 2002, without regard to whether the property is affixed to or incorporated into real property, and that is used in connection with operating an integrated gasification combined cycle electric generation facility, including: <ul style="list-style-type: none"> ◆ Property used to produce electric power by means of a combined combustion turbine and steam turbine application using synthetic gas or another product produced by the gasification of coal or another carbon-based feedstock. ◆ Property used in handling materials to be used as feedstock for gasification or used in the gasification process to produce synthetic gas or another carbon-based feedstock for use in the production of electric power in the manner described by statute. ■ Tangible personal property that is first placed in service in Texas during the applicable qualifying time period that begins on or after January 1, 2010, without regard to whether the property is affixed to or incorporated into real property, and that is used in connection with operating an advanced clean energy project, as defined by Texas Health and Safety Code, Section 382.003; ■ A building or a permanent, nonremovable component of a building that is built or constructed during the applicable qualifying time period that begins on or after January 1, 2002, and that houses tangible personal property described by statute. |
| Qualifying time period | <p>As of December 31, 2013, Texas Tax Code, Section 313.021(4), defined a qualifying time period as:</p> <ul style="list-style-type: none"> ■ The period that begins on the date that an application for an agreement is approved by the governing body of the school district and ends on December 31 of the second tax year that begins after that date, except as provided by Texas Tax Code, Section 313.021(4)(B) or (C), or Texas Tax Code, Section 313.027(h). ■ In connection with a nuclear electric power generation facility, the first seven tax years that begin on or after the third anniversary of the date the school district approves an application for an agreement, unless a shorter time period is agreed to by the governing body of the school district and the property owner. ■ In connection with an advanced clean energy project, as defined by Texas Health and Safety Code, Section 382.003, the first five tax years that begin on or after the third anniversary of the date the school district approves an application for an agreement, unless a shorter time period is agreed to by the governing body of the school district and the property owner. |
| Qualifying job | <p>As of December 31, 2013, Texas Tax Code, Section 313.021(3), defined a qualifying job as a permanent, full-time job that meets all of the following:</p> <ul style="list-style-type: none"> ■ Requires at least 1,600 hours of work a year. ■ Is not transferred from one area in Texas to another area in Texas. ■ Is not created to replace a previous employee. |

Glossary of Selected Terms Related to Agreements

| Term | Definition |
|------|--|
| | <ul style="list-style-type: none">▪ Is covered by a group health benefit plan for which a business offers to pay at least 80 percent of the premiums or other charges assessed for employee-only coverage under the plan, regardless of whether an employee may voluntarily waive the coverage.▪ Pays at least 110 percent of one of the following:<ul style="list-style-type: none">♦ The county average weekly wage for manufacturing jobs in the county where the job is located.♦ The county average weekly wage for all jobs in the county where the job is located, if the property owner creates more than 1,000 jobs in that county. |

Sources: Texas Tax Code, Chapter 313; school districts; and the Comptroller's Office.

Job-creation and Net Tax Benefit Information for the Seven Audited Agreements

Table 12 shows the net tax benefit (property tax savings, including tax credits and deductions for revenue protection payments and payments made in lieu of taxes to school districts) for each qualified job created as reported by the businesses associated with the seven audited appraisal limitation agreements (agreements) through tax year 2012.

Table 12

| Job-creation Summary for the Audited Agreements | | | | |
|---|--|--|---|---|
| School District and Business with Agreement | Type of Business | Number of Qualifying Jobs The Business Reported It Had Created (through tax year 2012) | Net Tax Benefit Business Reported It Had Received (through tax year 2012) | Net Tax Benefit per Qualifying Job Created (calculated by auditors) |
| Austin ISD and Hewlett-Packard Company | Research and development | 22 | \$133,904 | \$6,087 |
| Fort Stockton ISD and SandRidge Energy, Inc. | Manufacturing | 22 | \$7,590,537 | \$345,024 |
| Fort Stockton ISD and SandRidge Energy, Inc. | Manufacturing | 2 | \$225,465 | \$112,732 |
| Palacios ISD and NRG South Texas 3 ^a | Nuclear electric power generation | 0 | \$0 | \$0 |
| Palacios ISD and NRG South Texas 4 ^a | Nuclear electric power generation | 0 | \$0 | \$0 |
| Sterling City ISD and Goat Mountain Wind, LP | Renewable energy electric generation (wind farm) | 31 | \$1,037,110 | \$33,455 |
| Sterling City ISD and Goat Wind, LP | Renewable energy electric generation (wind farm) | 6 | \$110,186 | \$18,364 |

^a There had been no business activity related to the two agreements audited between Palacios ISD and NRG South Texas 3 and NRG South Texas 4 as of December 31, 2013. See Chapter 6 for more information on Palacios ISD and its agreements.

Sources: School districts and the Office of the Comptroller of Public Accounts.

Texas Tax Code, Sections 313.101 through 313.105 (Repealed)

Below are the statutory requirements of Texas Tax Code, Chapter 313, Subchapter D, School Tax Credits, that were repealed by House Bill 3390 (83rd Legislature, Regular Session), effective January 1, 2014.

Businesses with agreements that were entitled to and qualified for a tax credit before the repeal of Subchapter D are still subject to those statutory requirements. Texas Tax Code, Section 313.171(b), states that the repeal of Subchapter D does not affect a property owner's entitlement to a tax credit granted under Subchapter D if the property owner qualified for the tax credit before the repeal of Subchapter D.

SUBCHAPTER D. SCHOOL TAX CREDITS

Sec. 313.101. DEFINITION. In this subchapter, "qualifying time period" has the meaning assigned by Section 313.021.

Sec. 313.102. ELIGIBILITY FOR TAX CREDIT; AMOUNT OF CREDIT. (a) In addition to the limitation on the appraised value of the person's qualified property under Subchapter B or C, a person is entitled to a tax credit from the school district that approved the limitation in an amount equal to the amount of ad valorem taxes paid to that school district that were imposed on the portion of the appraised value of the qualified property that exceeds the amount of the limitation agreed to by the governing body of the school district under Section 313.027(a)(2) in each year in the applicable qualifying time period.

(b) If the person relocates the person's business outside the school district, the person is not entitled to the credit in or after the year in which the relocation occurs.

Sec. 313.103. APPLICATION. (a) An application for a tax credit under this subchapter must be made to the governing body of the school district to which the ad valorem taxes were paid. The application must be:

(1) made on the form prescribed for that purpose by the comptroller and verified by the applicant; and

(2) accompanied by:

(A) a tax receipt from the collector of taxes for the school district showing full payment of school district ad valorem taxes on the qualified property for the applicable qualifying time period; and

(B) any other document or information that the comptroller or the governing body considers necessary for a determination of the applicant's eligibility for the credit or the amount of the credit.

(b) An application for a tax credit under this subchapter or any information provided by the school district to the Texas Education Agency under Section 42.2515, Education Code, is not confidential.

Sec. 313.104. ACTION ON APPLICATION; GRANT OF CREDIT. Before granting the application for a tax credit, the governing body of the school district shall:

(1) determine the person's eligibility for a tax credit under this subchapter; and

(2) if the person's application is approved, by order or resolution direct the collector of taxes for the school district:

(A) in the second and subsequent six tax years that begin after the date the application is approved, to credit against the taxes imposed on the qualified property by the district in that year an amount equal to one-seventh of the total amount of tax credit to which the person is entitled under Section 313.102, except that the amount of a credit granted in any of those tax years may not exceed 50 percent of the total amount of ad valorem school taxes imposed on the qualified property by the school district in that tax year; and

(B) in the first three tax years that begin on or after the date the person's eligibility for the limitation under Subchapter B or C expires, to credit against the taxes imposed on the qualified property by the district an amount equal to the portion of the total amount of tax credit to which the person is entitled under Section 313.102 that was not credited against the person's taxes under Paragraph (A) in a tax year covered by Paragraph (A), except that the amount of a tax credit granted under this paragraph in any tax year may not exceed the total amount of ad valorem school taxes imposed on the qualified property by the school district in that tax year.

Sec. 313.105. REMEDY FOR ERRONEOUS CREDIT. (a) If the comptroller and the governing body of a school district determine that a person who received a tax credit under this subchapter for any reason was not entitled to the credit received or was entitled to a lesser amount of credit than the amount of the credit received, an additional tax is imposed on the qualified property equal to the full credit or the amount of the credit to which the person was not entitled, as applicable, plus interest at an annual rate of seven percent calculated from the date the credit was issued.

(b) A tax lien attaches to the qualified property in favor of the school district to secure payment by the person of the additional tax and interest imposed by this section and any penalties incurred. A person delinquent in the payment of an additional tax under this section may not submit a subsequent application or receive a tax credit under this subchapter in a subsequent year.

House Bill 3676 (81st Legislature, Regular Session)

Table 13 lists the changes that House Bill 3676 (81st Legislature, Regular Session) made to Texas Tax Code, Chapter 313. House Bill 3676 was intended to clarify certain provisions of Texas Tax Code, Chapter 313, related to appraisal limitation agreements between school districts and property owners.

Table 13

| Summary of House Bill 3676 (81st Legislature, Regular Session) | |
|--|---|
| Bill Section | Summary of Section |
| Section 1 | Amended Section 313.007, Texas Tax Code, to provide that Subchapters B (Limitation on Appraised Value of Certain Property), C (Limitation on Appraised Value of Property in Certain Rural School Districts), and D (School Tax Credits) expire December 31, 2015, rather than 2011. |
| Section 2 | Amended Section 313.021, Texas Tax Code, to redefine "qualified investment," "qualified property," "qualifying job," "qualifying time period," and "county average weekly wage for manufacturing jobs." |
| Section 3 | Amended Section 313.024(b), Texas Tax Code, to require the entity, to be eligible for a limitation on appraised value under this subchapter, to use the property in connection with certain activities, including a computer center primarily used in connection with one or more activities described by Subdivisions (1) through (7) (relating to requiring an entity, to be eligible for a limitation on appraised value, to use property in connection with certain industries and industries related to electric power) conducted by the entity. |
| Section 4 | Amended Section 313.024(e), Texas Tax Code, by amending Subdivision (1) and adding Subdivisions (5) and (6), to redefine "manufacturing," and define "research and development" and "computer center." |
| Section 5 | <p>Amended Section 313.025, Texas Tax Code, by amending Subsections (a), (b), and (d) and adding Subsections (a-1), (d-1), (h), and (i), as follows:</p> <p>(a) Authorizes the owner or lessee of, or the holder of another possessory interest in, any qualified property described by Section 313.021(2)(A) (relating to the definition of "qualified property" as it relates to "land"), (B) (relating to the definition of "qualified property" as it relates to new buildings or a certain other new improvement), or (C) (relating to the definition of "qualified property" as it relates to tangible personal property) to apply to the governing body of the school district in which the property is located for a limitation on the appraised value for school district maintenance and operations ad valorem tax purposes of the person's qualified property.</p> <p>(a-1) Requires the school district, within seven days of the receipt of each document, to submit to the comptroller of public accounts (comptroller) a copy of the application and the agreement between the applicant and the school district. Requires the school district, if an economic analysis of the proposed project is submitted to the school district, to submit a copy of the analysis to the comptroller. Requires the school district, in addition, to submit to the comptroller any subsequent revision of or amendment to any of those documents within seven days of its receipt. Requires the comptroller to publish each document received from the school district under this subsection on the comptroller's Internet website. Requires the school district, if the school district maintains a generally accessible Internet website, to provide on its website a link to the location of those documents posted on the comptroller's website in compliance with this subsection. Provides that this subsection does not require the comptroller to post information that is confidential under Section 313.028.</p> <p>(b) Requires the governing body of a school district to approve or disapprove an application before the 151st, rather than 121st, day after the date the application is filed, unless the economic impact evaluation has not been received or an extension is agreed to by the governing body and the applicant.</p> <p>(d) Requires the comptroller, before the 91st, rather than 61st, day after the date the comptroller receives the copy of the application, to submit a recommendation to the governing body of the school district as to whether the application should be approved or disapproved.</p> <p>(d-1) Authorizes the governing body of a school district to approve an application that the comptroller has recommended should be disapproved only if the governing body holds a public hearing the sole purpose of which is to consider the application and the comptroller's recommendation, and at a subsequent meeting of the governing body held after the date of the public hearing, at least two-thirds of the members of the governing body vote to approve the application.</p> <p>(h) Requires the comptroller, after receiving a copy of the application, to determine whether the property meets the requirements of Section 313.024 (Eligible Property) for eligibility for a limitation on appraised</p> |

Summary of House Bill 3676 (81st Legislature, Regular Session)

| Bill Section | Summary of Section |
|--------------|---|
| | <p>value under this subchapter. Requires the comptroller to notify the governing body of the school district of the comptroller's determination and provide the applicant an opportunity for a hearing before the determination becomes final. Provides that a hearing under this subsection is a contested case hearing and is required to be conducted by the State Office of Administrative Hearings in the manner provided by Section 2003.101 (Tax Division), Government Code. Provides that the applicant has the burden of proof on each issue in the hearing. Authorizes the applicant to seek judicial review of the comptroller's determination in a Travis County district court under the substantial evidence rule as provided by Subchapter G (Contested Cases; Judicial Review), Chapter 2001 (Administrative Procedure), Government Code.</p> <p>(i) Provides that the comptroller is not required to provide an economic impact evaluation of the application or to submit a recommendation to the school district as to whether the application should be approved or disapproved, and the governing body of the school district is prohibited from granting the application, if the comptroller's determination under Subsection (h) that the property does not meet the requirements of Section 313.024 for eligibility for a limitation on appraised value under this subchapter becomes final.</p> |
| Section 6 | <p>Amended Sections 313.026(a) and (b), Texas Tax Code, as follows:</p> <p>Requires the economic impact evaluation of the application to include certain information, including the name of the school district; the name of the applicant; the general nature of the applicant's investment; the number of qualifying jobs to be created by the applicant; the impact the project will have on this state and individual local units of government, rather than the impact the added infrastructure will have on the region, including tax and other revenue gains, direct or indirect, that would be realized during the qualifying time period, the limitation period, and a period of time after the limitation period considered appropriate by the comptroller, rather than revenue gains that would be realized by the school district, and economic effects of the project, including the impact on jobs and income, during the qualifying time period, the limitation period, and a period of time after the limitation period considered appropriate by the comptroller, rather than subsequent economic effects on the local and regional tax bases; the projected market value of the qualified property of the applicant as determined by the comptroller; the proposed limitation on appraised value for the qualified property of the applicant; the projected dollar amount of the taxes that would be imposed on the qualified property, for each year of the agreement, if the property does not receive a limitation on appraised value with assumptions of the projected appreciation or depreciation of the investment and projected tax rates clearly stated; the projected dollar amount of the taxes that would be imposed on the qualified property, for each tax year of the agreement, if the property receives a limitation on appraised value with assumptions of the projected appreciation or depreciation of the investment clearly stated; the projected effect on the Foundation School Program of payments to the district for each year of the agreement; the projected future tax credits if the applicant also applies for school tax credits under Section 313.103 (Application); and the total amount of taxes projected to be lost or gained by the district over the life of the agreement computed by subtracting the projected taxes stated in Subdivision (17) from the projected taxes stated in Subdivision (16). (b) Requires the comptroller's recommendations to be based on the criteria listed in Subsections (a)(5)-(20), rather than (a)(2)-(9) and on any other information available to the comptroller, including information provided by the governing body of the school district under Section 313.025(b) (relating to requirements for an application for a limitation on appraised value that is filed with the governing body of a school district; requirements for information on an economic impact evaluation of that limitation; authorizing the collection of fees for an economic impact evaluation; and timelines for approval or disapproval of an application for a limitation on appraised value.).</p> |
| Section 7 | <p>Amended Subchapter B, Chapter 313, Texas Tax Code, by adding Section 313.0265, as follows:</p> <p>Sec. 313.0265. DISCLOSURE OF APPRAISED VALUE LIMITATION INFORMATION. (a) Requires the comptroller to post on the comptroller's Internet website each document or item of information the comptroller designates as substantive before the 15th day after the date the document or item of information was received or created. Requires each document or item of information to continue to be posted until the appraised value limitation expires. (b) Requires the comptroller to designate as substantive each application requesting a limitation on appraised value, the economic impact evaluation made in connection with the application, and each application requesting school tax credits under Section 313.103. (c) Requires the school district, if a school district maintains a generally accessible Internet website, to maintain a link on its Internet website to the area of the comptroller's Internet website where information on each of the district's agreements to limit appraised value is maintained.</p> |
| Section 8 | <p>Amended Section 313.027, Texas Tax Code, by amending Subsection (f) and adding Subsections (h) and (i), as follows:</p> <p>(f) Authorizes the agreement, in addition, to adhere to certain requirements and authorizations, including to provide that the property owner will protect the school district in the event the district incurs extraordinary education-related expenses related to the project that are not directly funded in state aid formulas, including expenses for the purchase of portable classrooms and the hiring of additional personnel to accommodate a temporary increase in student enrollment attributable to the project. Makes nonsubstantive changes. (h) Authorizes the agreement between the governing body of the school district and the applicant to provide for a</p> |

Summary of House Bill 3676 (81st Legislature, Regular Session)

| Bill Section | Summary of Section |
|--------------|--|
| | <p>deferral of the date on which the qualifying time period for the project is to commence or, subsequent to the date the agreement is entered into, be amended to provide for such a deferral. Prohibits this subsection from being construed to permit a qualifying time period that has commenced to continue for more than the number of years applicable to the project under Section 313.021(4) (relating to the definition of "qualifying time period"). (i) Prohibits a person and the school district from entering into an agreement under which the person agrees to provide supplemental payments to a school district in an amount that exceeds an amount equal to \$100 per student per year in average daily attendance, as defined by Section 42.005 (Average Daily Attendance), Education Code, or for a period that exceeds the period beginning with the period described by Section 313.021(4) and ending with the period described by Section 313.104(2)(B) (relating to requiring the governing body of the school district, before a certain date the application for a tax credit is filled, if the person's application is approved, by order or resolution direct the collector of taxes for the school district, in a certain amount of time, to credit against the taxes imposed on the qualified property by the school district a certain amount and proving certain exceptions) of this code. Provides that this limit does not apply to amounts described by Subsection (f)(1) (relating to the agreement requiring to incorporate certain relevant provisions and payment of revenue offsets, and certain other mechanisms) or (2) (relating to authorizing the agreement to provide that the property owner will protect the school district in the event the district incurs certain extraordinary education-related expenses related to the project that are not directly funded in state aid formulas) of this section.</p> |
| Section 9 | <p>Amended Subchapter B, Chapter 313, Texas Tax Code, by adding Section 313.0275, as follows:</p> <p>Sec. 313.0275. RECAPTURE OF AD VALOREM TAX REVENUE LOST. (a) Requires a person with whom a school district enters into an agreement under this subchapter to make the minimum amount of qualified investment during the qualifying time period and create the required number of qualifying jobs during each year of the agreement, notwithstanding any other provision of this chapter to the contrary. (b) Provides that the property owner is liable to this state for a penalty equal to the amount computed by subtracting from the market value of the property for that tax year the value of the property as limited by the agreement and multiplying the difference by the maintenance and operations tax rate of the school district for that tax year, if in any tax year a property owner fails to comply with Subsection (a). (c) Provides that a penalty imposed under Subsection (b) becomes delinquent if not paid on or before February 1 of the following tax year. Provides that Section 33.01 (Penalties and Interest) applies to the delinquent penalty in the manner that section applies to delinquent taxes.</p> |
| Section 10 | <p>Amended Section 313.028, Texas Tax Code, as follows:</p> <p>Sec. 313.028. CERTAIN BUSINESS INFORMATION CONFIDENTIAL. Requires information provided to a school district in connection with an application for a limitation on appraised value under this subchapter that describes the specific processes or business activities to be conducted or the specific tangible personal property to be located on real property covered by the application to be segregated in the application from other information in the application and is confidential and not subject to public disclosure unless the governing body of the school district approves the application. Prohibits other information in the custody of a school district or the comptroller in connection with the application, including information related to the economic impact of a project or the essential elements of eligibility under this chapter, such as the nature and amount of the projected investment, employment, wages, and benefits, from being considered confidential business information if the governing body of the school district agrees to consider the application. Provides that information in the custody of a school district or the comptroller if the governing body approves the application is not confidential under this section.</p> |
| Section 11 | <p>Amended Section 313.051(a), Texas Tax Code, as follows:</p> <p>(a) Provides that this subchapter applies only to a certain school district, including a school district that has territory in an area that qualified as a strategic investment area under Subchapter O, Chapter 171 (Franchise Tax), immediately before that subchapter expired, rather than a strategic investment area, as defined by Section 171.721. Deletes existing text related to a school district applying to this subchapter if a county that is not partially or wholly located in a metropolitan statistical area. Makes a nonsubstantive change.</p> |
| Section 12 | <p>Amended Sections 313.103 and 313.104, Texas Tax Code, as follows:</p> <p>Sec. 313.103. APPLICATION. (a) Creates this subsection from existing text. Deletes existing text related to requiring the application to be filed before September 1 of the year immediately following the applicable qualifying time period. (b) Provides that an application for a tax credit under this subchapter or any information provided by the school district to the Texas Education Agency under Section 42.2515 (Additional State Aid for Ad Valorem Tax Credits under Texas Economic Act), Education Code, is not confidential. Sec. 313.104. ACTION ON APPLICATION; GRANT OF CREDIT. Requires the governing body of the school district, before granting, rather than before the 90th day after the date, the application for a tax credit, to determine the person's eligibility for a tax credit under this subchapter and if the person's application is approved, by order or resolution direct the collector of taxes for the school district to take certain actions.</p> |

| Summary of House Bill 3676 (81st Legislature, Regular Session) | |
|--|---|
| Bill Section | Summary of Section |
| Section 13 | Amended Section 403.302(d), Texas Government Code, to redefine "taxable value" for the purposes of this section. |
| Section 14 | Repealed: Section 313.029 (Tax Limitation), Texas Tax Code. |
| Section 15 | Provides that Sections 313.021(1)(A), (2), and (5), 313.024(e), and 313.025(a), Texas Tax Code, as amended by this Act, are intended to clarify rather than change existing law. Provides that the clarification made by Section 313.021(5), Tax Code, as amended by this Act, is necessary to allow the Texas Workforce Commission to implement that subdivision in conformance with the data collection requirements imposed by the federal government. |
| Section 16 | (a) Effective date, except as provided by Subsection (b) of this section: upon passage or September 1, 2009. (b) Effective date, Sections 313.025(a-1), (h), and (i) and 313.0265, Texas Tax Code, as added by this Act: January 1, 2010. |

Source: House Bill 3676 (81st Legislature, Regular Session).

Periodic Reporting Forms that Businesses with Agreements Certify

The Office of the Comptroller of Public Accounts requires each business with an appraisal limitation agreement to submit the (1) Chapter 313 Annual Eligibility Report Form and (2) the Biennial Progress Report for Texas Economic Development Act, which are presented below.

Chapter 313 Annual Eligibility Report Form

| Chapter 313 Annual Eligibility Report Form | |  Form 50-772 (Revised July 2013) |
|---|--|--|
| Tax Year Covered in This Report _____ | | |
| School District Name _____ | I&S Tax Rate _____ | M&O Tax Rate _____ |
| Project Name _____ | Company Name _____ | |
| Company Address _____ | Company Contact Information _____ | |
| NOTE: This form must be completed by an authorized representative of each approved applicant and each entity with property subject to the limitation agreement. It must be submitted to the school district by May 15th of every year using information from the previous tax (calendar) year. For limitation agreements where there are multiple company entities that receive a part of the limitation provided by the agreement: 1) each business entity not having a full interest in the agreement should complete a separate form for their proportionate share of required employment and investment information; and, 2) separately, the school district is required to complete an Annual Eligibility Report that provides for each question in this form a sum of the individual answers from reports submitted by each entity so that there is a cumulative Annual Eligibility Report reflecting the entire agreement. | | |
| Texas Taxpayer ID of Applicant _____ | Texas Taxpayer ID Reporting Entity (if appropriate) _____ | |
| Date of Agreement Approval _____ | Original Applicant Name _____ | |
| First Complete Tax Year of the Qualifying Time Period _____ | Last Tax Year of the Qualifying Time Period _____ | |
| First Tax Year of the Limitation _____ | Amount of the Limitation at the Time of Application Approval _____ | |
| QUALIFIED PROPERTY INFORMATION | | |
| Market Value _____ | I&S Taxable Value _____ | M&O Taxable Value _____ |
| Is the business entity in good standing with respect to Tax Code, Chapter 171? (Attach printout from Comptroller Web site: http://www.window.state.tx.us/taxinfo/coasintr.html) <input type="checkbox"/> Yes <input type="checkbox"/> No | | |
| Is the business entity current on all taxes due to the State of Texas? <input type="checkbox"/> Yes <input type="checkbox"/> No | | |
| Is the business activity of the project an eligible business activity under Section 313.024(b)? <input type="checkbox"/> Yes <input type="checkbox"/> No | | |
| Please identify business activity: _____ | | |
| What was the application review start date for your application (the date your application was determined to be complete)? _____ (This question must only be answered for projects with applications approved after June 1, 2010.) | | |
| How many new jobs were based on the qualified property in the year covered by this report? (See note on page 3.) _____ | | |
| What is the number of new jobs required for a project in this school district according to 313.021(2)(A)(iv)(b), 313.051(b), as appropriate? _____ | | |
| If the applicant requested a waiver of minimum jobs requirement, how many new jobs must the approved applicant create under the waiver? _____ | | |
| 80 percent of New Jobs (0.80 x number of new jobs based on the qualified property in the year covered by this report.) _____ | | |
| For more information, visit our website: www.texasahead.org/tax_programs/chapter313/ | | |
| | | 50-772 - 07-13/3 |



What is the minimum required annual wage for each qualifying job in the year covered by the report?

For agreements executed prior to June 19, 2009, please identify which of the two Tax Code sections is used to determine the wage standard required by the agreement: §313.021(5)(A) or §313.051(b). For agreements executed after June 19, 2009, please identify which of the four Tax Code sections is used to determine the wage standard required by the agreement: §313.021(5)(A), §313.021(5)(B), §313.021(3)(E)(ii), or §313.051(b).

Attach calculations and cite (or attach) exact Texas Workforce Commission data sources.

How many qualifying jobs (employees of this entity and employees of a contractor with this entity) were based on the qualified property in the year covered by the report?

Of the qualifying job-holders last year, how many were employees of the approved applicant?

Of the qualifying job-holders last year, how many were employees of an entity contracting with the approved applicant?

If any qualifying job-holders were employees of an entity contracting with the applicant, does the approved applicant or assignee have documentation from the contractor supporting the conclusion that those jobs are qualifying jobs? NA Yes No

THE FOLLOWING QUESTIONS APPLY ONLY TO APPROVED APPLICANTS WITH AGREEMENTS THAT REQUIRE THE APPROVED APPLICANT TO PROVIDE A SPECIFIED NUMBER OF JOBS AT A SPECIFIED WAGE.

How many qualifying jobs did the approved applicant commit to create in the year covered by the report?

At what annual wage?

How many qualifying jobs were created at the specified wage?

ENTITIES ARE NOT REQUIRED TO ANSWER THE FOLLOWING FIVE QUESTIONS IF THE YEAR COVERED BY THE REPORT IS AFTER THE QUALIFYING TIME PERIOD OF THEIR AGREEMENT.

What is the qualified investment expended by this entity from the beginning of the qualifying time period through the end of the year covered by this report?

Was any of the land classified as qualified investment? Yes No

Was any of the qualified Investment leased under a capitalized lease? Yes No

Was any of the qualified Investment leased under and operating lease? Yes No

Was any property not owned by the applicant part of the qualified investment? Yes No

THE FOLLOWING QUESTIONS MUST BE ANSWERED BY ENTITIES HAVING A PARTIAL INTEREST IN AN AGREEMENT.

What was your limitation amount (or portion of original limitation amount) during the year covered by this report?

Please describe your interest in the agreement and identify all the documents creating that interest.

Empty rectangular box for describing interest in the agreement and identifying documents.



NOTE: For job definitions see TAC §9.1051(14) and Tax Code, §313.021(3). If the agreement includes a definition of "new job" other than TAC §9.1051(14)(C), then please provide the definition "new job" as used in the agreement.

Notwithstanding any waiver by the district of the requirement for the creation of a minimum number of new jobs, or any other job commitment in the agreement, Tax Code 313.024(d) requires that 80 percent of all new jobs be qualifying jobs.

APPROVAL.

"I am the authorized representative for the Company submitting this Annual Eligibility Report. I understand that this Report is a government record as defined in Chapter 37 of the Texas Penal Code. The information I am providing on this Report is true and correct to the best of my knowledge and belief."

Signature

Printed Name of Authorized Company Representative

Title

Date

CONTACT INFORMATION FOR AUTHORIZED REPRESENTATIVE

Address

Phone

Email

Biennial Progress Report for Texas Economic Development Act



Biennial Progress Report for Texas Economic Development Act

Form 50-773

(Revised July 2013)

Instructions:

- This form must be filled out by each applicant that is party to a limitation agreement.
- If the original application was made by a group of two or more companies, each company must complete this form.
- If the original applicant split into two or more applicants after the original agreement, all current agreement holders must complete this form.
- Applicants should only complete the information for their years as an agreement holder, noting what year they were formed after the original agreement was approved.
- Each agreement holder should respond as a current applicant on Line 9 below.
- Applicants should report their proportionate share of required employment and investment information.
- If the original applicant is still the only agreement holder, please do not complete Lines 31 and 32 below.

In addition to the Biennial Progress Report required from each applicant that is a party to an agreement, a separate Biennial Progress Report summarizing the combined applicant's data for the entire agreement must be completed.

- If one of the applicants cannot provide this information, a summarization report must be completed by the school district.

- Projects spanning more than one school district must complete forms for each school district.
- Please return signed hard copy forms and electronic spreadsheets to the school district before May 15 of each even-numbered year.

Note:

- The school district that is a party to the Chapter 313 agreement is collecting the data required by Chapter 313.008 on this form for the Comptroller of Public Accounts (CPA).
- The CPA requests companies complete the electronic spreadsheet version of the form. Please submit both an *unsigned electronic version* and a *signed hard copy version* of the spreadsheet (with any attachments) to the district. Please contact CPA if you have questions about the form. The spreadsheet version of this form can be downloaded at: www.texasahead.org/tax_programs/chapter313/.
- After ensuring that all forms are complete, the school district will forward that data to the CPA for inclusion in a statutorily required report to the Texas Legislature.

| |
|--|
| 1. Name of school district: |
| 2. Name of CAD appraising the qualified property in this school district: |
| 3. Name of project on original application (or short description of facility): |
| 4. Name of applicant on original application: |
| 5. Date original application filed with school district: |
| 6. Name of company entering into original agreement with district: |
| 7. Date original limitation agreement approved by school district: |
| 8. Date of final signing of agreement (if different from board approval date): |
| 9. Name of current agreement holder(s): |
| 10. Complete mailing address of current agreement holder: |
| 11. Name of company contact person for agreement holder: |
| 12. Title of company contact person: |
| 13. Phone number of company contact person: |
| 14. E-mail address of company contact person: |
| 15. Texas franchise tax ID number of current agreement holder: |

For more information, visit our website: www.texasahead.org/tax_programs/chapter313/

50-773 • 07-13/3



| |
|--|
| 16. If the current agreement holder does not report under the franchise tax law, please include name and tax ID of reporting entity. |
| 17. NAICS Code of current agreement holder (6 Digit): |
| 18. Name of authorized company representative (if different from above): |
| 19. Title of authorized company representative (if different from above): |
| 20. Phone of authorized company representative (if different from above): |
| 21. E-mail of authorized company representative (if different from above): |
| 22. Complete mailing address of authorized company representative (if different from above): |
| 23. First (complete) year of Qualifying Time Period – after the date the application is approved. See Tax Code §313.021[4]: |
| 24. First year of property value limitation (generally the third complete year of the agreement): |
| 25. Original Limitation Amount (for entire agreement): |
| 26. Amount of qualified investment during the qualifying time period the recipient committed to spend or allocate for this project on application (Not Total Investment): |
| 27. Date of construction commencement (estimate if in the future): |
| 28. Date construction completed (actual or estimate if in the future): |
| 29. Has the description of the qualified property changed from that in the application? If so, please describe on an attachment how the actual qualified property — for which you are providing actual and estimated market values on subsequent pages — differs from that property described in the agreement. Include only property located in this school district. |
| 30. What was the number of permanent existing jobs at this facility prior to application? |
| 31. If you are one of two or more companies originally applying for a limitation, list all other applicants here and describe their relationships. (Use attachments if necessary.) |
| 32. If you are a current agreement holder who was not an original applicant, please list all other current agreement holders. Please describe the chain of ownership from the original applicant to the new entities. (Use attachments if necessary.) |
| 33. If the agreement includes a definition of "new job" other than TAC §9.1051(14)(C), please provide the definition of "new job" as used in the agreement. (Use attachments if needed.) |

District Name _____ Project Name _____

Company Name _____ 1st Yr. of Qualifying Time Period _____

Note: Excel spreadsheet version is available for download at URL listed below.

| | Pre-Qualifying Time Period | Qualifying Time Period | | |
|--|---|--|----------------------------------|--------|
| | | From application approval date to Jan. 1 of next tax year ¹ | Year 1 (First Complete Tax Year) | Year 2 |
| | Please enter tax years (YYYY) here (starting in "Year 1"). → | | | |
| 34. Number of qualifying jobs ² applicant committed to create on application (cumulative)** | / / / / / | / / / / / | | |
| 35. Number of qualifying jobs ² applicant actually created (cumulative)** | / / / / / | / / / / / | | |
| 36. Number of new jobs ² created (cumulative)** | / / / / / | / / / / / | | |
| 37. Number of new jobs ² created that provide health benefits for employees (cumulative)** | / / / / / | / / / / / | | |
| 38. Median annual wage of new jobs each applicant created** | / / / / / | / / / / / | | |
| 39. Average annual wage of new jobs each applicant created** | / / / / / | / / / / / | | |
| 40. Total investment for this project (per year or time period, not cumulative)** | / / / / / | / / / / / | | |
| 41. Amount of qualified investment applicant actually spent or allocated for this project ³ (per year or time period, not cumulative)** (See also Note #1.) | / / / / / | / / / / / | | |
| 42. Market value of qualified property on January 1 before any exemptions ⁵ ** | | | | |
| 43. Market value of qualified property (amount shown in #42) less any exemptions, but before the limitation on value authorized by Tax Code 313** | | | | |
| 44. Limitation amount in each of years 1-10. ⁷ ** | / / / / / | / / / / / | | |
| 45. Taxable value of qualified property certified by the county appraisal district for the purpose of school M&O taxes** | | | | |
| 46. School District M&O tax rate (per hundred dollars of value)* | | | | |
| 47. School district I&S tax rate (per hundred dollars of value)* | | | | |
| 48. Total school district ad valorem tax levy (M&O and I&S) on qualified property* | | | | |

*Actual data only. **Actual and projected data. Use actual data for prior years. Estimates are required for current and future years.

Notes:

1. Only projects with agreements executed after June 19, 2009 may have any qualified investment between the time of application approval and Jan. 1 of subsequent tax year.
2. Jobs meeting all of the requirements of Tax Code §313.021(3). Each qualifying job is a new job that meets the wage standard for that school district, and is covered by a group health benefits plan for which the employer offers to pay at least 80 percent of the employee-only premium. Do not include construction jobs in counts of qualifying jobs.
3. For new job definition see TAC §9.1051(14).
4. Total Investment is all investment at original cost, including land acquired after filing of application. Investments made in one year should be reflected in the subsequent year's market value.
5. The investment made during the qualifying time period meeting the requirements of Tax Code §313.021(1). Fill in amounts for the time between the application approval and Jan. 1 of first tax year, Year 1 and Year 2 only. (See also Note #1)
6. For all values, use those from CAD as available. For future years, use market value that the entity estimates will approximate the market value for ad valorem tax purposes in that year.
7. This amount may vary annually for agreements with multiple agreement-holders. Subentities should enter their share of original limitation amount. Limitation amounts of all subentities should sum to that of the original limitation amount originally approved by the school district.

(continued on next page)



Form 50-773 Biennial Progress Report for Texas Economic Development Act

| | Limitation Period | | | | | | | |
|--|-------------------|--------|--------|--------|--------|--------|--------|---------|
| | Year 3 | Year 4 | Year 5 | Year 6 | Year 7 | Year 8 | Year 9 | Year 10 |
| Please enter tax years (YYYY) here. → | | | | | | | | |
| 34. Number of qualifying jobs ² applicant committed to create on application (cumulative)** | | | | | | | | |
| 35. Number of qualifying jobs ² applicant actually created (cumulative)** | | | | | | | | |
| 36. Number of new jobs ² created (cumulative)** | | | | | | | | |
| 37. Number of new jobs ² created that provide health benefits for employees (cumulative)** | | | | | | | | |
| 38. Median annual wage of new jobs each applicant created** | | | | | | | | |
| 39. Average annual wage of new jobs each applicant created** | | | | | | | | |
| 40. Total investment for this project (per year or time period, not cumulative)** | | | | | | | | |
| 41. Amount of qualified investment applicant actually spent or allocated for this project ³ (per year or time period, not cumulative)** (See also Note #1.) | | | | | | | | |
| 42. Market value of qualified property on January 1 before any exemptions ⁵ ** | | | | | | | | |
| 43. Market value of qualified property (amount shown in #42) less any exemptions, but before the limitation on value authorized by Tax Code 313** | | | | | | | | |
| 44. Limitation amount in each of years 1-10.7** | | | | | | | | |
| 45. Taxable value of qualified property certified by the county appraisal district for the purpose of school M&O taxes** | | | | | | | | |
| 46. School District M&O tax rate (per hundred dollars of value)* | | | | | | | | |
| 47. School district I&S tax rate (per hundred dollars of value)* | | | | | | | | |
| 48. Total school district ad valorem tax levy (M&O and I&S) on qualified property* | | | | | | | | |

*Actual data only. **Actual and projected data. Use actual data for prior years. Estimates are required for current and future years.

Notes:

- Only projects with agreements executed after June 19, 2009 may have any qualified investment between the time of application approval and Jan. 1 of subsequent tax year.
- Jobs meeting all of the requirements of Tax Code §313.021(3). Each qualifying job is a new job that meets the wage standard for that school district, and is covered by a group health benefits plan for which the employer offers to pay at least 80 percent of the employee-only premium. Do not include construction jobs in counts of qualifying jobs.
- For new job definition see TAC §9.1051(14).
- Total Investment is all investment at original cost, including land acquired after filing of application. Investments made in one year should be reflected in the subsequent year's market value.
- The investment made during the qualifying time period meeting the requirements of Tax Code §313.021(1). Fill in amounts for the time between the application approval and Jan. 1 of first tax year, Year 1 and Year 2 only. (See also Note #1)
- For all values, use those from CAD as available. For future years, use market value that the entity estimates will approximate the market value for ad valorem tax purposes in that year.
- This amount may vary annually for agreements with multiple agreement-holders. Subentities should enter their share of original limitation amount. Limitation amounts of all subentities should sum to that of the original limitation amount originally approved by the school district.

| | | |
|--|---|-------------------------------------|
| <p>The CPA requests companies complete the electronic spreadsheet version of the form. Please submit both an unsigned electronic version and a signed hard copy version of the spreadsheet (with any attachments) to the district.</p> | <p>By signing below, I, _____, certify that I am the authorized representative of _____, a current agreement holder of a limitation on appraised value, and the contents of this form and the attached documentation are true and correct to the best of my knowledge and belief.</p> | |
| | <p>sign here →</p> | <p>Authorized Official</p> |
| | <p>Print Name/Title</p> | <p>Date</p> |
| | | <p>Phone (area code and number)</p> |

Copies of this report have been distributed to the following:

Legislative Audit Committee

The Honorable David Dewhurst, Lieutenant Governor, Joint Chair
The Honorable Joe Straus III, Speaker of the House, Joint Chair
The Honorable Jane Nelson, Senate Finance Committee
The Honorable Robert Nichols, Member, Texas Senate
The Honorable Jim Pitts, House Appropriations Committee
The Honorable Harvey Hilderbran, House Ways and Means Committee

Office of the Governor

The Honorable Rick Perry, Governor

Office of the Comptroller of Public Accounts

The Honorable Susan Combs, Comptroller of Public Accounts

Texas Education Agency

Members of the State Board of Education

Ms. Barbara Cargill, Chair
Mr. Thomas Ratliffe, Vice Chair
Ms. Mavis B. Knight, Secretary
Mr. Lawrence A. Allen, Jr.
Ms. Donna Bahorich
Mr. David Bradley
Mr. Ruben Cortez, Jr.
Ms. Martha M. Dominguez
Ms. Patricia Hardy
Mr. Tom Maynard
Ms. Sue Melton-Malone
Mr. Ken Mercer
Ms. Geraldine Miller
Ms. Marisa B. Perez
Mr. Marty Rowley
Mr. Michael L. Williams, Commissioner

Austin Independent School District

Members of the Board of Trustees

Mr. Vincent M. Torres, President
Ms. Gina Hinojosa, Vice President
Mr. Jayme Mathias, Secretary
Ms. Tamala Barksdale
Ms. Cheryl Bradley
Ms. Amber Elenz
Ms. Lori Moya
Mr. Robert Schneider
Ms. Ann Teich
Dr. Paul Cruz, Interim Superintendent

Fort Stockton Independent School District

Members of the School Board

Ms. Glenda Pasqua, President

Mr. Billy Espino, Vice President

Ms. Sandra Marquez, Secretary

Mr. Freddie Martinez, Assistant Secretary

Mr. Tom Ezell

Mr. Oscar Gonzalez

Mr. Jacob Vasquez

Mr. Ralph Traynham, Superintendent

Palacios Independent School District

Members of the Board of Trustees

Mr. Rick Cink, President

Ms. Patty Frankson, Vice President

Mr. Steve Stuhrenberg, Secretary

Ms. Donna Brune

Mr. Greg Hunter

Mr. Fabian Marroquin

Mr. Peter Zamarripa

Ms. Vicki Adams, Superintendent

Sterling City Independent School District

Members of the School Board

Mr. Jason Cox, President

Mr. Scot Long, Vice President

Mr. Randy Parrish, Secretary

Mr. Josh Gaines

Mr. Wesley Glass

Mr. Heath Hughes

Ms. Omega Pena

Mr. Bob Rauch, Superintendent



This document is not copyrighted. Readers may make additional copies of this report as needed. In addition, most State Auditor's Office reports may be downloaded from our Web site: www.sao.state.tx.us.

In compliance with the Americans with Disabilities Act, this document may also be requested in alternative formats. To do so, contact our report request line at (512) 936-9500 (Voice), (512) 936-9400 (FAX), 1-800-RELAY-TX (TDD), or visit the Robert E. Johnson Building, 1501 North Congress Avenue, Suite 4.224, Austin, Texas 78701.

The State Auditor's Office is an equal opportunity employer and does not discriminate on the basis of race, color, religion, sex, national origin, age, or disability in employment or in the provision of services, programs, or activities.

To report waste, fraud, or abuse in state government call the SAO Hotline: 1-800-TX-AUDIT.