

Understanding Chapter 313:

School Property Tax Limitations and the Impact on State Finances



TEXAS TAXPAYERS
TTARA
AND RESEARCH ASSOCIATION

400 West 15th Street • Suite 400 • Austin, Texas 78701 • 512.472.8838 • www.ttara.org

Understanding Chapter 313: School Property Tax Limitations and the Impact on State Finances

A Research Report by the Texas Taxpayers and Research Association (TTARA)

400 West 15th, Suite 400

Austin, Texas

www.ttara.org

(512) 472-8838

Executive Summary

There are many reasons to invest in Texas: available land at reasonable cost, strong underlying growth with an ample supply of labor, right-to-work protections, a reasonable regulatory and judicial environment, no personal income tax, stable and affordable energy resources, and a location central to both coasts. But Texas does present some barriers for large investment projects: a challenged infrastructure (transportation and water, which are being addressed) and high taxes—particularly the property tax, which is the largest tax business pays.

To ease the sting of high property taxes and improve the economics of potential investments, Texas law allows cities and counties to offer temporary tax abatements under Chapter 312 of the Tax Code and school districts to offer lesser benefits under Chapter 313. Since school districts often account for the biggest share of the property tax bill, Chapter 313 is the state's single most important incentive in its economic development toolbox.

Chapter 313 allows a school district to offer a temporary, 10-year limit (ranging from \$10 million to \$100 million) on the taxable value of a new investment project in manufacturing, and certain environmentally friendly energy projects. The limitation applies only to school district taxes levied for maintenance and operations (M&O); taxes for debt service are not subject to the limitation, nor do business inventories qualify. Before the school district can approve a limitation, the State Comptroller must issue a certificate of approval that finds the project will generate more tax revenue for the state than the amount of the benefit received by the taxpayer.

Through 2015, the State Comptroller reports that 311 projects have participated in the program, creating 12,321 operations jobs (plus an unreported number of construction and contract jobs), adding \$12.1 billion to school M&O tax rolls and \$31.7 billion to school debt tax rolls. Overall the Comptroller estimates the program has brought over \$80 billion in new investment to the state, creating a total of 50,300 jobs and adding \$2.0 billion in personal income.

Critics of the program contend school districts are “giving away state money” by offering the incentives. In truth, Chapter 313 makes money for the state by attracting new taxpayers to invest here who otherwise would not do so. A project is only eligible for a temporary 313 limitation if it demonstrates that the incentive was a determining factor in its decision to move forward with the investment—no incentive, no project. The only revenue “lost” are tax dollars Texas never would have collected. Critics contend that school districts gain more state aid by offering a 313 limitation, but in fact, the school district sees an immediate *reduction* in its state aid, which saves the state money. Once the limitation expires, the district sees a further and typically much deeper reduction in state aid (or an increase in recapture) as a result of the value the project adds to the tax rolls.

Property tax abatements and limitations are effective economic development tools commonly used across the United States. Chapter 313 incentives, while positive for project economics, tend to be less favorable than comparable programs in other states. Rarely is Texas the lowest tax cost state for projects. The average Chapter 313 agreement, in a year when the limitation is in effect, saves the project only 31.8 percent of its already-high school tax bill. The program is also riddled with substantial paperwork. While making the program one of the most transparent in the nation, it adds a significant administrative cost that diminishes the overall net tax benefit. Still, for all its warts, Chapter 313 has proven to be an effective, though certainly not perfect, economic development tool for Texas.

Understanding Chapter 313

Table of Contents

Investing in Texas: The Good and Not-So-Good	1
The Landscape of Texas Taxes	1
The History of Chapter 313	3
The Projects of 313	5
How Chapter 313 Works	5
Eligible Investments and Limitations	5
Jobs Creation and Wage Requirements	6
Applying for a Limitation	6
State Comptroller Review	7
Project Agreement and Payments to School Districts	7
Reporting Requirements	8
The Limitation and Impact on School Finance	9
Base Case (No Project)	9
Project with Limitation in Effect	10
Project with Limitation Expired	11
The Net Taxpayer Benefit of Chapter 313	12
Fiscal Implications of the Program	13
Chapter 313 and Jobs	14
Renewable Energy and Chapter 313	15
Conclusions	16

Understanding Chapter 313:

School Property Tax Limitation and the Impact on State Finances

With the Texas Miracle stalling, investment incentives are once again under scrutiny. Both the Lieutenant Governor and the Speaker assigned interim charges to committees to study and evaluate Texas' economic competitiveness and incentive programs. The state's single most important program, the Texas Economic Development Act found in Chapter 313 of the Tax Code, is under the policy microscope.

Chapter 313 allows school districts to offer a temporary limitation on the taxable value of certain new investments. The limitation applies only to school M&O taxes, and not taxes for debt service. Given the high level of Texas' property taxes, and, in particular, school property taxes, Chapter 313 is the state's single most important economic development tool. It is also the state's most transparent economic development program—with all substantive documents for each application posted on the Comptroller's website. But in spite of its importance and its transparency, it is also the state's most misunderstood program.

In this research brief, TTARA assesses how Chapter 313 fits in the state's economic toolbox in its competition with other states for economic investment. We explain how the program works and address some of the common criticisms of the program.

Investing in Texas: The Good and Not-So-Good

There are many reasons for businesses to invest and grow in Texas. Texas has:

- available land at generally reasonable cost,
- strong underlying growth with an ample supply of labor,
- right-to-work protections,
- a reasonable regulatory and judicial environment,
- no personal income tax,
- stable and affordable energy resources, and
- a location central to both coasts.

But Texas also has some factors that flash caution. The state's infrastructure is lacking (specifically water and transportation—although recent legislative efforts make this a work in progress) and our taxes are high.

The Landscape of Texas Taxes

Our taxes are high? But wait, Texas is a low tax state, right?

Given the high level of Texas' property taxes, and, in particular, school property taxes, Chapter 313 is the state's single most important economic development tool.

Texas is indeed a low tax state for individuals. The absence of a personal income tax saves the average family about \$3,000 annually. Our 2015 state and local tax burden on individuals was 42 percent below the national average, ranking us fourth lowest among the states. However, Texas' heavy reliance on property and sales taxes makes it a relatively high tax state for businesses, particularly those that are capital-intensive. Relative to economic output, Texas' business tax burden was 4 percent *above* the national average, ranking us 20th highest among the states—not outrageously high, but certainly not among the low tax states.

Nationally, business accounts for 44.1 percent of all state and local taxes. In Texas, business foots 61.5 percent of the total bill.

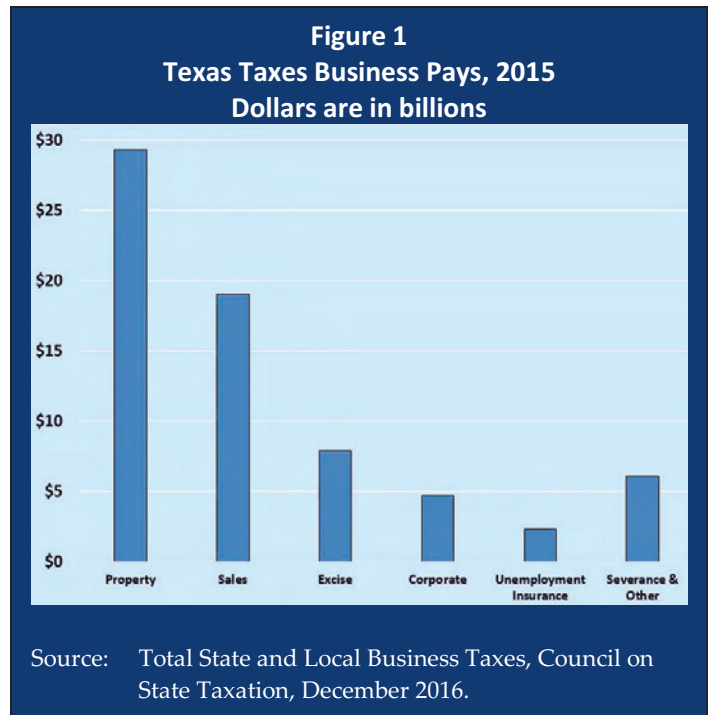
The local property tax poses the single biggest barrier to capital investment (Figure 1). Of the estimated \$69.3 billion in Texas state and local taxes business paid in 2015, almost \$30 billion, over 40 percent, were local property taxes levied by school districts, cities, counties and various special purpose districts. For capital-intensive businesses, the property tax share is much higher.

Texas has relatively high property tax rates that apply to a comparatively high tax base. Texas' property taxes apply to all real estate, land and improvements, but also to any tangible personal property, including inventories, used for the production of income—essentially any *business-owned* personal property. That compares less favorably to other states. Eleven states do not tax business personal property, and 43 states largely exempt business inventories.

The Lincoln Institute of Land Policy, in conjunction with the Minnesota Center for Fiscal Excellence, conducts a periodic review of property taxes across the states. For an industrial project, Texas has the fifth highest property tax rate of the 50 states, and higher than all our surrounding states. Figure 2 shows the total property taxes on a \$1 billion investment over a 25-year facility life absent any tax abatements or incentives. In Texas, the facility would pay \$643 million in property taxes over its lifespan—\$144 million more than the average state and more than in New York, double that of New Mexico, three times more than in Kentucky and almost four times more than in Virginia. Obviously other factors may enter into a project's decision to invest in a state, but a half a billion dollar tax difference between Texas and Virginia is a huge gap for Texas to overcome.

To help compete with locations in other states, local jurisdictions levying a property tax in Texas are able to offer certain incentives:

- under Chapter 312 of the Tax Code, city, county and certain special districts are authorized to offer tax abatements for up to 100 percent of the taxes due for no more than 10 years, and



*The property tax is
Texas' largest tax on
business.*

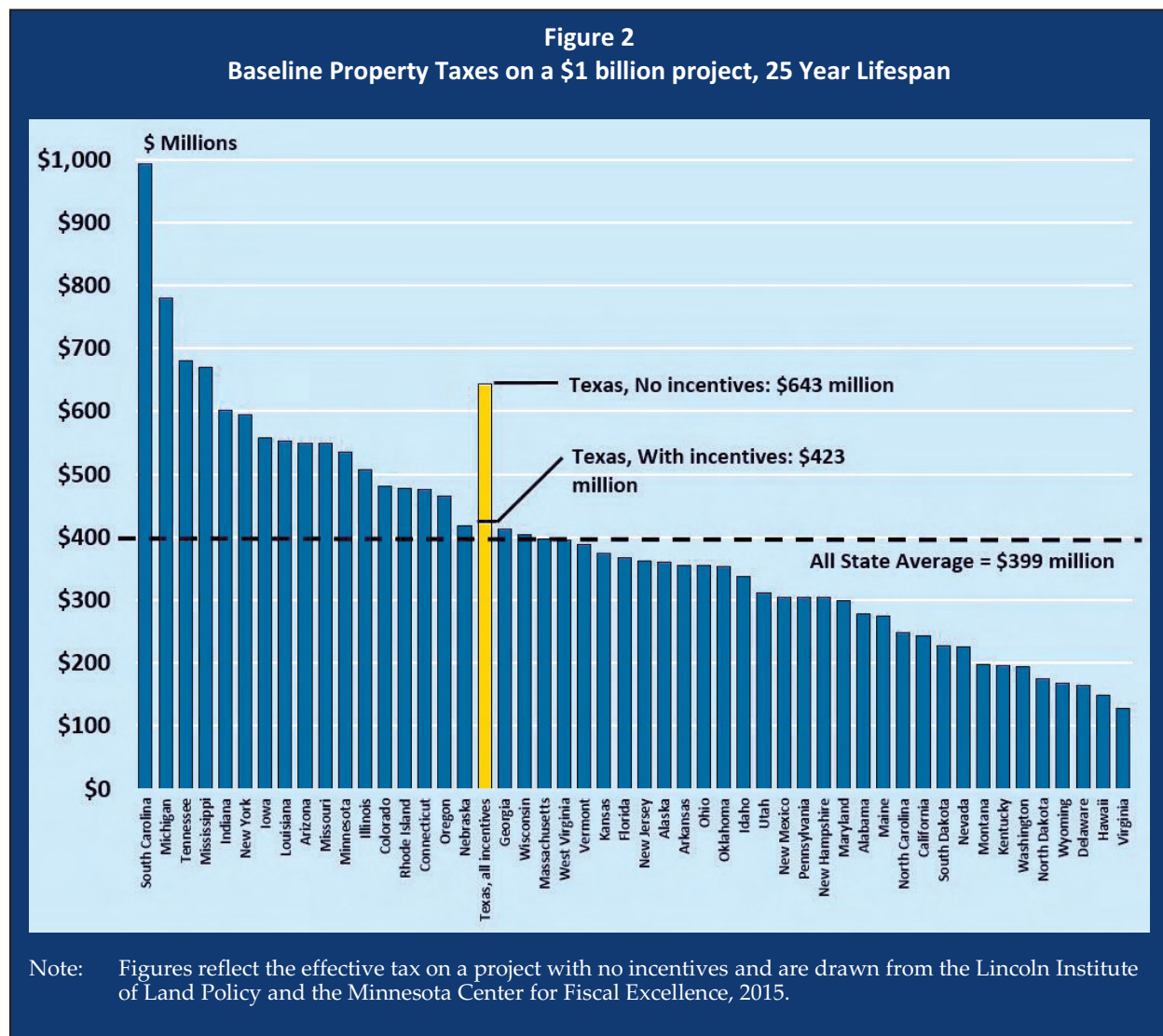
- under Chapter 313 of the Tax Code, school districts may offer a temporary limitation on the taxable value of a project, for M&O taxes only, for no more than 10 years.

In the example illustrated by Figures 2 & 3, if the project availed itself of all property tax incentives offered by local entities, including a Chapter 313 school tax limitation, the project could cut its Texas tax bill to roughly \$423 million, still 5 percent higher than the average state tax load *without* incentives. Unfortunately, the competition is not static; almost all other states offer their own property tax abatement programs, which are not reflected in Figure 2.

The simple truth is that Texas is rarely the lowest cost tax state for new investment. Instead, our incentive programs simply try to keep Texas' tax load "close enough" so the state can win based on other factors.

The History of Chapter 313

Texas has long had a history of being a "business friendly" state, but incentives have always been controversial—particularly those related to public schools. School districts used to have the authority to offer traditional tax



abatements under Chapter 312 of the Tax Code; however, the Legislature changed state law in 1993 so that school districts offering tax abatements would be subject to cuts in state aid. This effectively eliminated the program. What seemed like good, fiscally-conservative politics, though, immediately backfired.

Absent school abatements, Texas, which had been the nation's top location for new industrial projects, started to drift down the rankings—from first to tenth in five years, with the number of new projects dropping more than 70 percent.

One project became the poster child for the perception that Texas was turning its back on economic development. In 1996, anticipating that the state would offer a competitive package of tax abatements, Intel Corporation announced it would build a \$1.3 billion computer chip manufacturing plant near Fort Worth.¹ It was the marquee project of the decade, with 800 permanent jobs. Intel began working with Texas officials on an incentives package, but ultimately the Legislature did not act. Facing a potentially huge property tax bill and frustrated with Texas' inability to offer a tax-competitive package, Intel stopped construction and shifted its investment primarily to Chandler, Arizona. Intel mothballed plans for several additional future plants and jobs at the Fort Worth site.

In 2001, State Rep. Kim Brimer introduced House Bill 1200, known as the Texas Economic Development Act, and recorded as Chapter 313 of the Tax Code. As introduced, the bill would have allowed a school district to offer a temporary limit on the taxable value of any new investment creating over 300 jobs without being subject to a loss of state aid. Rural legislators balked at a program that appeared to offer little for their districts. As the bill wound its way through the legislative process, the jobs requirement was reduced, wage requirements were added, and eligible projects were restricted to either manufacturing, research and development, or renewable energy. Lower thresholds were allowed for projects in rural or economically disadvantaged areas. The bill ultimately garnered four joint authors and 100 co-authors in the House. Ironically, Gov. Rick Perry (who would ultimately become one of the program's biggest proponents) allowed the bill to become law without his signature.² The program took effect Jan. 1, 2002, and was set to expire at the end of 2007 unless renewed by the Legislature.

In 2007, House Bill 1470 by Rep. Rob Eissler extended the program through 2011 while making a number of changes to the program. The program was further extended and modified by House Bill 3676 by Rep. Joe Heflin in 2009 and House Bill 3390 by Rep. Harvey Hilderbran in 2011.

Figure 3
Texas Property Taxes on a \$1 billion Project, 25 Year Lifespan
With and Without Incentives
Dollars are in billions

Taxing District	Taxes W/O Incentives	Value of Incentives	Taxes After Incentives
School District M&O	\$276.0	\$101.9	\$174.1
School District I&S	\$70.9	\$0.0	\$70.9
City	\$103.2	\$41.3	\$61.9
County	\$107.1	\$42.8	\$64.2
Special District	\$85.6	\$34.2	\$51.4
Total Taxes	\$642.8	\$220.2	\$422.5

Source: Texas Taxpayers and Research Association.

Chapter 313 allows school districts to offer a temporary limitation on the taxable value of certain new investment projects.

¹ http://articles.latimes.com/1996-11-14/business/fi-64510_1_texas-plant

² In 2001 Governor Perry vetoed 82 bills, setting an all-time record for bills vetoed in a legislative session.

Hilderbran's HB 3390 tackled two of the program's most controversial aspects, both dealing with the purported "cost" of the program. Hilderbran's bill:

- required projects to demonstrate they would pay more in taxes than the amount of benefit they will receive from the limitation, and
- restricted the program to only those projects that can demonstrate that the limitation is a determining factor in their decision to invest in Texas.

The Projects of 313

Through 2015, the State Comptroller reports that 311 projects have participated in the program, creating 12,321 qualifying operations jobs (construction jobs are not counted), adding \$12.1 billion to school M&O tax rolls (even with the limitation), and \$31.7 billion to school debt tax rolls. Overall, the Comptroller estimates the program has brought over \$80 billion in new investment to the state, creating 50,300 jobs and adding \$2.0 billion in personal income.

Of the 311 projects, renewable energy accounts for just over half—with 144 in wind and 22 in other types of renewable energy. Manufacturing accounts for almost all of the other projects and for 77 percent of the direct investment.

How Chapter 313 Works

Under Chapter 313, certain eligible projects may apply to the school district for a temporary limit on the taxable value of new property it intends to put in place. Property eligible for the limitation includes land, buildings and certain tangible personal property, such as machinery and equipment, but not inventories. If the school district decides to consider the application, it is forwarded to the Comptroller, who evaluates the application and determines whether it meets certain required criteria. If so, the Comptroller issues a certificate of approval and the school district may act on the application. If the school district approves, it enters into an agreement with the owner of the project and elects to temporarily tax only a set amount of the investment for a period of up to 10 years.

The amount of state aid a district receives is largely a function of its taxable property value per student. As the new value of the project, limited or not, is placed on the tax rolls, the district's local property tax collections increase. This triggers a corresponding reduction in its state aid—a small reduction during the period of the limitation and a much larger reduction once the project is on the tax rolls at full value. School districts commonly require supplemental payments in return for the limitation, which are allowed under the law subject to certain limits. These payments reduce the taxpayer's net tax savings and are excluded from consideration in state aid formulas.³

Eligible Investments and Limitations. Chapter 313 is available only to projects making **new investments** in connection with manufacturing, research and development, electricity generation using certain low emission

To be eligible for a 313 limitation a project must demonstrate the limitation is a determining factor in the decision to build in Texas, and it will pay more in taxes than the amount of benefit from the limitation.

³ Under state funding formulas, increases in local revenue generally result in a reduction in state aid.

technologies (including renewable electric generation such as wind), and nuclear energy. Computer centers in connection with any of these activities are also eligible. A provision which took effect in 2014 allows a “Texas priority project”—i.e., any project with a qualified investment in excess of \$1 billion—to qualify as well. Only new property is eligible for the program; existing property is not. **Consequently, Chapter 313 does not remove property from the tax rolls—it simply delays the time that new investments go on to the tax rolls at full value.**

The required amount of investment for a project to qualify differs depending on the property value of a school district. A higher level of investment is required in very large or property-wealthy school districts. Smaller, less wealthy, and rural districts may offer a more advantageous lower value limitation, as shown in Figure 4.

Jobs Creation and Wage Requirements. A project must create at least 25 “qualifying” jobs (or 10 jobs, if the project is to be in a rural or economically disadvantaged school district).⁴ These “qualifying” jobs must be new full-time jobs that pay 110 percent of the area’s average manufacturing wage and come with health coverage in which the employer offers to pay at least 80 percent of the workers’ premiums. A school board can waive the jobs requirement if it makes a finding that the jobs creation requirement exceeds the industry standard for that particular type of facility. Such a waiver has been common for renewable energy projects.

Applying for a Limitation. A project seeking a 313 limitation must make formal application to the school district in which the property is to be located and pay the district an application fee, which typically ranges from \$75,000

Chapter 313 does not remove property from the tax rolls—it simply delays the time that new investments go on to the rolls at full value.

Figure 4
Chapter 313 Value Limitations

School District Value Limitations: Standard Districts			
Category	Total Property Value of School District	Minimum Amount of Qualified Investment	Minimum Amount of Tax Value Limitation
I	\$10 billion or more	\$100 million	\$100 million
II	\$1 billion, but less than \$10 billion	\$80 million	\$80 million
III	\$500 million, but less than \$1 billion	\$60 million	\$60 million
IV	\$100 million but less than \$500 million	\$40 million	\$40 million
V	Less than \$100 million	\$20 million	\$20 million
School District Value Limitations: Rural or Districts in Strategic Investment Areas			
Category	Industrial Value of School District	Minimum Amount of Qualified Investment	Minimum Amount of Tax Value Limitation
I	\$200 million or more	\$30 million	\$30 million
II	>\$90 million, but less than \$200 million	\$20 million	\$25 million
III	>\$1 million, but less than \$90 million	\$10 million	\$20 million
IV	>\$100,000, but less than \$1 million	\$5 million	\$15 million
V	Less than \$100,000	\$1 million	\$10 million

⁴ From 2009 to 2014, a special provision was included in the law which allowed projects creating more than 1,000 qualifying jobs to pay a wage that simply exceeded the county average wage.

to \$150,000. The district uses the fee to defray its consideration costs, including the cost of hiring school finance consultants. The project must use a standard application designed by the Comptroller, which is nine pages long with 84 questions and a minimum of 16 supporting schedules, including project schematics. It is not uncommon for the completed application to exceed 50 pages. The applicant also must demonstrate that it and any affiliates are in good standing with the Comptroller's Office (i.e. no outstanding taxes due).

State Comptroller Review. If it opts to consider the application, the school district forwards the application to the State Comptroller for review. The Comptroller assesses whether the project qualifies under the law's eligibility requirements, but also must determine whether:

- the limitation on appraised value is a determining factor in the applicant's decision to invest capital and construct the project in this state, and
- the project is likely to generate, before the 25th anniversary of the beginning of the limitation period, tax revenue in an amount sufficient to offset the school district M&O ad valorem tax revenue lost as a result of the agreement (includes state tax revenue, school district M&O ad valorem tax revenue attributable to the project, and any other tax revenue attributable to the effect of the project on the economy of the state).

If the above is affirmative, the Comptroller issues a "certificate for a limitation," which is forwarded to the school district. The Comptroller may also issue a certificate if he determines qualitatively that the project would result in a net benefit to the state, though the Comptroller has never used this authority. A school district may not approve a limitation without a certificate.

If the school district approves the application, any information in the custody of the school district or the Comptroller is subject to public disclosure.

Project Agreement and Payments to School Districts. Once the school district receives the certification from the Comptroller, it may opt to negotiate a Chapter 313 limitation with the applicant. The terms are delineated in a standard agreement form prescribed by the Comptroller. State law requires the agreement to provide that the applicant will protect the school district from any loss of state aid resulting from the limitation (so-called "revenue protection payments"). Most agreements also require the project to pay additional amounts termed "supplemental payments" (sometimes called "Payments in Lieu of Taxes" or "PILOTs" or "PILTs"). The total amount of supplemental payments to the school district, or to any entity on behalf of the school district, may not exceed the higher of either:

- \$100 per student, or
- a total of \$50,000 for each year from the first year of the qualifying period through the third year after the limit expires (a total of 15 years).

School districts and their consultants typically target a recovery of 40 percent of the tax savings of the project through supplemental payments.

A chapter 313 agreement involves substantial paperwork and reporting—all of which is publicly available on the Comptroller of Public Accounts' website.

Reporting Requirements. In addition to the application and agreement, a project subject to a 313 agreement must complete a number of very detailed annual and biennial reporting requirements throughout the term of the agreement (Figure 5). School district reports typically are compiled by consultants for a fee, which is passed on to the taxpayer.

All of these completed reporting forms, along with the application and the agreement, are public documents and are available on the Comptroller's website. Given the breadth of material reported, and that it is immediately available online, Chapter 313 is one of the most transparent economic development programs in the nation. However, given the enormous amount of paperwork required, the program is also one of the most bureaucratic and administratively costly of the various states' programs—a significant point that is increasingly becoming a consideration for businesses when evaluating the program in comparison to other states.

Figure 5 Chapter 313 Paperwork			
	Pages	Questions	Schedules
Application Forms			
Form 50-296A Application for Appraised Value Limitation on Qualified Property. To be filled out by an applicant seeking an appraised value limitation and submitted to the school district. The school district submits a completed application to the Comptroller for review and approval.	9	84	16
Form 50-300 Application for Tax Credit on Qualified Property. To be filled out by an agreement holder after paying property tax for the last complete tax year of the qualifying time period and submitted to the school district. Only applies to agreements prior to January 1, 2014.	1	7	3
Agreement Forms			
Form 50-286 Texas Economic Development Act Agreement. To be used by the applicant and school district as a template for a value limitation agreement. The school district submits a draft agreement to the Comptroller for review and approval.	24	n.a.	3
Annual/Biennial Reporting Forms			
Form 50-772A Annual Eligibility Report. To be filled out by agreement holders and submitted by an authorized representative of each company to the school district by May 15th of every year using information from the previous tax (calendar) year. School districts forward the report to the Comptroller's office by June 15th of every year.	4	47	1
Form 50-773A Biennial Progress Report. To be filled out by agreement holders and submitted by an authorized representative of each company to the school district by May 15th of each even-numbered year. School districts forward the report to the Comptroller's office by June 15th of every year.	7	25	4
Form 50-287 Biennial School District Cost Data Request. School districts are also requested to submit the Biennial School District Cost Data Request Form to the Comptroller's office by July 15th of each even-numbered year, indicating—for each project—actual and estimated property values, tax rates, payments in lieu of taxes, extraordinary educational expenses, and revenue protection payments.	1	n.a.	1
Form 50-825 Job Creation Compliance Report. To be filled out by agreement holders and submitted by an authorized representative of each company directly to the Comptroller's office annually.	3	19	1

The Limitation and Impact on School Finance

State aid to school districts is based on a complicated set of formulas that take into account the local property wealth per student of a school district to “equalize” wealth disparities across districts. For example, a property-poor school district receives relatively more state aid than a mid-wealth district, while a very wealthy district may actually have to share a portion of its local tax collections with the state through some form of “recapture.”

Given that a Chapter 313 agreement affects the local tax base, it impacts state formula aid. Critics contend that the state “subsidizes” districts for offering a 313 limitation by sending more money to offset the value lost as a result of the agreement. In fact, the exact opposite happens. A district granting a 313 agreement sees a reduction in its state aid by virtue of the value the project adds to its tax rolls. **Generally, a Chapter 313 agreement results in a modest reduction in state aid during the limitation period, and a much more substantial reduction in state aid once the limitation expires.** At that point, the property is taxed at its full value for M&O purposes.

Figure 6 presents a simplified illustration of how a Chapter 313 agreement relates to school finance—both for purposes of M&O and for debt service, or Interest and Sinking Fund (I&S) revenue. It presents the school finance and local tax impacts of a fictitious school district, “Tejas Independent School District (ISD),” under three circumstances:

1. No project or 313 limitation
2. A project with a limitation in place
3. A project for which the limitation has expired

Base Case (No Project). Tejas ISD has 20,000 students (Line A). State aid formulas guarantee that the district will have \$5,140 in revenue per student (Line B) at a local M&O tax rate of \$1.00 (Line G)—or a total of \$102.8 million (Line C). The district has a tax base of \$4 billion (Line F), and generates a total of \$40 million in property taxes levied for M&O (Line H). In order for the district to receive the guaranteed amount of operating revenue, the state provides aid of \$62.8 million (Line I).

The district also must meet an annual debt service obligation of \$20 million (Line K). The state guarantees that each penny of tax per student will generate \$35 of revenue, so the district’s share of its debt service obligation is \$11.4 million (Line M), raised by a tax rate of \$0.286 (Line N) against its tax base of \$4 billion (Line J). The state sends Tejas ISD a check for \$8.6 million to cover its share (Line L).

In total, the sum of the district’s M&O and I&S revenue is \$122.8 million (Line R), with local taxpayers paying \$51.4 million in property taxes (Line O) and the state paying \$71.4 million (Line P).

The average home in Tejas ISD is appraised at \$200,000 (Line S). Against that, a homeowner receives a state-mandated homestead exemption of \$25,000 (Line T), leaving a taxable value of \$175,000 (Line U). Applying the total tax rate for M&O and debt service of \$1.286 (Line V) results in the average homeowner’s school tax bill of \$2,250 (Line X).

Generally, a 313 agreement results in a modest reduction in state aid during the limitation period, and a more substantial reduction in state aid once the limitation expires.

Figure 6
A Simplified Illustration of How a 313 Agreement Impacts School Finance

Element of School Finance		No Project	Project w/ Limitation in Effect	Diff to No Project	Project w/ Limitation Expired	Difference to No Project
Maintenance and Operations						
A	Number of Students	20,000	20,000	0	20,000	0
B	Basic Allotment	\$5,140.0	\$5,140.0	\$0.0	\$5,140.0	\$0.0
C	Guaranteed Aid (A*B; \$ml)	\$102.8	\$102.8	\$0.0	\$102.8	\$0.0
D	Property Tax Wealth (\$ml)	\$4,000.0	\$4,000.0	\$0.0	\$4,000.0	\$0.0
E	Project Taxable Value (\$ ml)	\$0.0	\$80.0	\$80.0	\$1,000.0	\$1,000.0
F	Total District Property Wealth (D+E; \$ml)	\$4,000.0	\$4,080.0	\$80.0	\$5,000.0	\$1,000.0
G	M&O Tax Rate (per \$100 of value)	\$1.000	\$1.000	\$0.000	\$1.000	\$0.000
H	Local Tax Revenues (F*G; \$ml)	\$40.0	\$40.8	\$0.8	\$50.0	\$10.0
I	State Aid (C-H; \$ml)	\$62.8	\$62.0	(\$0.8)	\$52.8	(\$10.0)
Debt Service						
J	Tax Base for Debt Service (\$ ml)	\$4,000.0	\$5,000.0	\$1,000.0	\$5,000.0	\$1,000.0
K	Debt Service Payments (\$ml)	\$20.0	\$20.0	\$0.0	\$20.0	\$0.0
L	State Share (\$ml)	\$8.6	\$5.7	(\$2.9)	\$5.7	(\$2.9)
M	Local Share (\$ml)	\$11.4	\$14.3	\$2.9	\$14.3	\$2.9
N	Debt Tax Rate (L/F; per \$100 of value)	\$0.286	\$0.286	\$0.000	\$0.286	\$0.000
Total School Finance Impacts						
O	Local Property Taxes (H+M) (\$ ml)	\$51.4	\$55.1	\$3.7	\$64.3	\$12.9
P	State Aid (I+L) (\$ ml)	\$71.4	\$67.7	(\$3.7)	\$58.5	(\$12.9)
Q	Supplemental Payments (A*\$100; \$ml)	\$0.0	\$2.0	\$2.0	see note	see note
R	Total School District Revenue (C+K) (\$ ml)	\$122.8	\$124.8	\$2.0	\$122.8	\$0.0
Taxes on an "Average" Home						
S	Basic Homestead (example)	\$200,000	\$200,000	\$0	\$200,000	\$0
T	Homestead Exemption	\$25,000	\$25,000	\$0	\$25,000	\$0
U	Taxable Value	\$175,000	\$175,000	\$0	\$175,000	\$0
V	Total Tax Rate (G+N)	\$1.286	\$1.286	\$0.000	\$1.286	\$0.000
X	School Taxes on \$200,000 home	\$2,250	\$2,250	\$0	\$2,250	\$0

Note: Technically, school finance formulas use two different measures of student count for maintenance and operations (M&O) and for debt service (I&S), though for simplification this example uses a single measure. Under current state law, state aid for M&O is based on student counts weighted for certain factors while aid for I&S is based on actual unweighted student counts.

Project with Limitation in Effect. The Widget Company—a billion-dollar project—is considering a number of locations in various states, but determines that with a Chapter 313 limitation, Texas is its preferred location. The company negotiates a Chapter 313 agreement with Tejas ISD which provides a temporary cap of \$80 million on the project's taxable value for M&O (Line E). In return, the company agrees to pay the district the maximum allowable supplemental payments of \$100 per student—amounts that will not be considered in current-law school finance formulas.

The number of students and the state revenue guarantee are unaffected by the project—state aid formulas still guarantee that the district will have \$5,140 in revenue per student (Line B) at a local M&O tax rate of \$1.00 (Line G)—or a total of \$102.8 million (Line C). The district, however, now has an additional \$80 million added to its tax base as a result of the project, bringing its total taxable value to \$4.08 billion (Line F), which generates a total of \$40.8 million in property taxes levied for M&O (Line H). Because the district is now “wealthier”—even with only the limited amount of value added to the rolls—it qualifies for a lesser amount of state aid. Under this scenario, the district's \$1.00 M&O tax rate raises an additional \$0.8 million; consequently, the state's aid payment drops by \$0.8 million (Line I). The state saves \$0.8 million in school M&O formula spending as a result of the Widget Company building in Texas.

The state makes money from Chapter 313 because it cuts state aid to districts with active limitations in place.

The state saves even more on debt service because Chapter 313 does **not** allow a limitation to apply against debt service taxes. With the project, the district's total tax base for debt service is \$5 billion (Line J). As a "wealthier" district (compared to the base case), Tejas ISD's share of its \$20 million debt service payment rises by \$2.9 million to \$14.3 million (Line M). The state's obligation drops by the same amount—\$2.9 million (Line L). There is no impact on the local debt service tax rate (Line N).⁵

Overall, under current school finance formulas the tax benefit from the Widget Company locating in the district accrues to the state. Because the district collects \$3.7 million more in property taxes (Line O), state formulas make a corresponding reduction in the amount of state aid the district receives (Line P)—saving the state \$3.7 million. **Critics of Chapter 313 contend that the state subsidizes a school district for granting a 313 limitation, but in fact, the state actually saves money by cutting state aid payments to the district.** The district does gain, however, because the project pays \$2 million in supplemental payments outside of the basic school finance formulas (Line Q). The district is able to use this money without restriction—either for supplemental classroom funding, facilities improvements or any other lawful purpose.

The project and the Chapter 313 limit have no impact on the average homeowner's tax bill. The district's tax rates have not changed, leaving the average homeowner a property tax bill of \$2,250.

Project with Limitation Expired. The limitation is only available for 10 years and may not be renewed. As the limitation expires, the Widget Company facility goes onto the tax rolls at its full value of \$1 billion. The district sees a dramatic increase in its local property value and its local tax collections, causing a corresponding drop in state aid.

The number of students and the state revenue guarantee are unaffected. State aid formulas still guarantee that the district will have \$5,140 in revenue per student (Line B) at a local M&O tax rate of \$1.00 (Line G)—or a total of \$102.8 million (Line C). The district, however, now has an additional \$1 billion on its tax rolls as a result of the project (compared to no project), bringing its total taxable value to \$5 billion (Line F). That local tax base now generates \$50 million in property taxes for M&O (Line H). The district's state aid payment drops by \$10 million (Line I), saving the state budget that amount.

The expiration of the M&O value limit does not impact the district's debt service taxes. Tejas ISD's share of its \$20 million debt service payment remains at \$14.3 million (Line M)—the same as it was when the M&O limit was in effect. The state's obligation remains \$2.9 million lower than it would have been without the project (Line L), and the debt service tax rate remains unchanged (Line N).

In total, the now fully-taxed project allows the district to raise an additional \$12.9 million from its tax base without any change in tax rates (Line O). State

School districts commonly require that projects share a portion of their tax savings through supplemental payments, which are capped at the higher of \$50,000 or \$100 per student and are excluded from state aid calculations.

⁵ In the event Tejas was a "property-wealthy" district subject to recapture, the state would have directly recaptured the excess M&O taxes rather than reducing the amount of state aid to the district. The state does not recapture debt taxes, however, and the district would have used the additional value from the project to reduce its debt tax rate.

aid drops by that amount (Line P), ultimately showing up in the state budget as a \$12.9 million spending cut.

It should be noted that the district may receive supplemental payments from the project for up to three years after the limitation expires, a fact not reflected in the table.

Excluding the supplemental payments, the project ultimately has no direct impact on the school district's total revenues through the school finance formulas. The district's bottom line is determined by state formulas and the tax rates it adopts, not by any changes in its taxable value. The ultimate tax benefit of the project building in Texas accrues to the state (any benefit to the district is from supplemental payments).

Just as when the limitation took effect, the expiration of the limit has no impact on the average homeowner's tax bill. The district's tax rates have not changed, leaving the average homeowner a property tax bill of \$2,250.

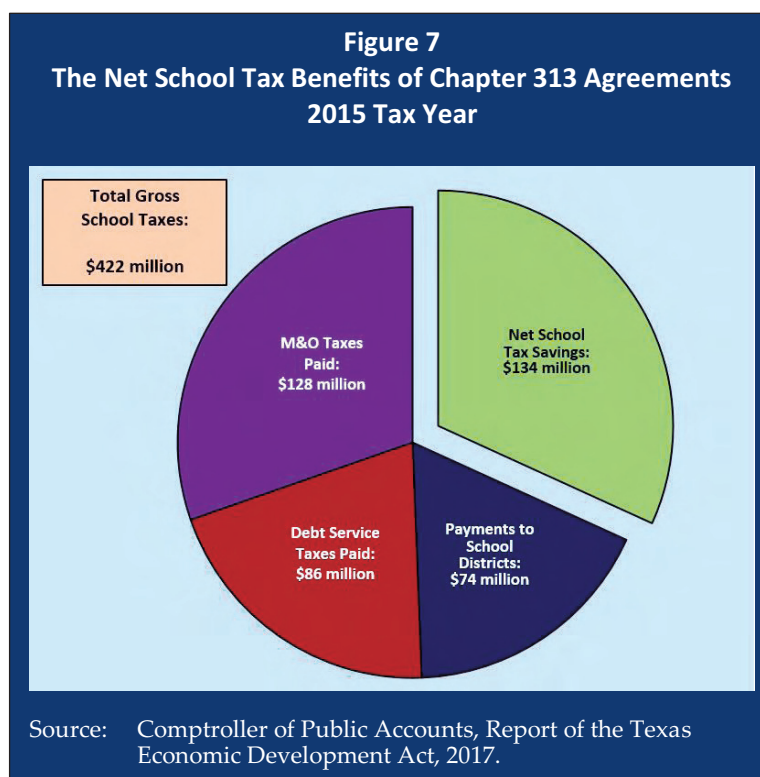
The overall bottom line is that by virtue of a 313 limitation, the Widget Company built in Texas when it would not have done so otherwise. That investment brought \$37 million in new school property taxes to the school district during the temporary 10-year period in which the project was on the tax rolls at its limited value, saving the state \$37 million. Once the limitation expires, the Widget Company pays annual school taxes of \$12.9 million—again, reducing state spending by this amount. In addition, the Widget Company pays millions of additional dollars in other local property taxes, plus state sales, franchise and other taxes. Overall, Chapter 313 was able to attract a project that wouldn't have come to Texas otherwise—a project that pays millions of dollars annually to the net benefit of the state Treasury.

The Net Taxpayer Benefit of Chapter 313

A company choosing to locate in Texas may find the benefits for Chapter 313 are far less than what they might garner in other states. Programs in other states typically offer a temporary 100 percent exemption for a number of years, most commonly 10, but some offer five years. While Chapter 313 benefits in Texas extend 10 years, those benefits are far from 100 percent for a number of reasons.

Chapter 313 applies only to school taxes (which account for 55 percent of the average Texas property tax bill). Abatements may be available on the 45 percent of the property taxes levied by cities, counties and special districts under Chapter 312 of the Tax Code, but this involves a separate and distinct (and much simpler) application process with an additional investment of time and resources. In many states, the state may grant an abatement which applies to ALL local property taxes, essentially providing streamlined, one-stop shopping for incentives.

But even when it comes just to schools, Chapter 313 is also not a comprehensive benefit. **In fact, of the 311 active Chapter 313 projects in 2015, the net school tax reduction equaled only 32 percent of the net amount of school property taxes that would be due without the limitation** (Figure 7). Some minimum amount of the project value—from \$1 million to \$100 million—must be placed on the M&O tax rolls.



In 2015, Chapter 313 projects subject to a limitation actually placed \$12.1 billion of value onto the tax rolls, resulting in an estimated \$128 million dollars of school M&O tax payments.

The Chapter 313 limitation does not apply to taxes levied for debt service—taxes which account for about one-fifth of the total school tax bill. In 2015, active Chapter 313 projects paid an estimated \$86 million in debt service taxes to school districts.

And projects faced more than just tax payments. Supplemental and revenue protection payments to school districts as a condition of their limitation agreements cost projects another \$74 million in 2015.

All totaled, while Chapter 313 projects in 2015 received a net school tax discount of \$134 million, they paid a total of \$288 million in school property taxes and supplemental payments. Chapter 313 projects paid nearly \$86 million in debt service taxes, \$128 million in M&O taxes and \$74 million in supplemental payments to school districts. For every net school tax dollar temporarily saved, projects paid \$2.15 in school property taxes and supplemental payments.

The net property tax benefit from all 2015 Chapter 313 agreements in effect reflected an average of 32 percent in school district property tax savings.

AND that amount excludes the overhead costs associated with the program:

- filing fees that can exceed \$100,000 per application,
- business consultant costs (for the application and on-going reporting), and
- school district consultant costs (typically recovered from fees assessed by school districts on the project).

Overall, Chapter 313 is far less financially advantageous than property tax incentive programs common in other states, which typically offer 100 percent abatements with little overhead or ongoing costs.

Fiscal Implications of the Program

An issue that adds to the controversy of all economic incentive programs is the assessment of their costs and benefits.

For Chapter 313, the Comptroller and the Legislative Budget Board calculate a static fiscal “cost” to the state as being equal to the amount of tax savings received by a project. For example, a project may receive a Chapter 313 benefit that will reduce its school M&O taxes over a 10-year period in an amount equal to \$62 million. The state number crunchers assign a “cost” to the state, or a loss of tax collections, of that \$62 million.

While this seems fairly straightforward, it is incorrect. Simply put, Chapter 313 is not a zero sum game.

Since 2013, in order to be eligible for a Chapter 313 limitation, a project must demonstrate that the incentive is a determining factor—no incentive, no

The average Chapter 313 limitation reduces a project's net school tax bill by only 32 percent—far less advantageous than comparable programs in other states.

limitation. The “loss” to the state is from taxes it would never collect. That is why the Comptroller can approve a Chapter 313 limitation that saves a taxpayer millions of dollars during the state’s budget period without immediately requiring a corresponding reduction to the Comptroller’s projection of state tax revenue collections.

The only way the state loses money is if it grants an incentive to a project that will locate in Texas regardless. The original law was silent on this point, but the statute now requires a project to demonstrate that the limitation was a determining factor in its decision to invest in Texas—a point subject to intense scrutiny by the Comptroller’s Office. The agency has denied a certificate of limitation to several projects the agency believed would locate in Texas without the incentive.

Consequently, Chapter 313 does not “cost” the state money. The only tax dollars Chapter 313 “loses” are those it never would have collected in the first place. In fact, Chapter 313 essentially makes money for the state by bringing new taxpayers and new tax dollars to the state—a dynamic result that is ignored in the state’s fiscal assessment.

State fiscal estimates as to the “cost” of Chapter 313 limitations assume all projects would have come to Texas absent the limitation—something prohibited in current law.

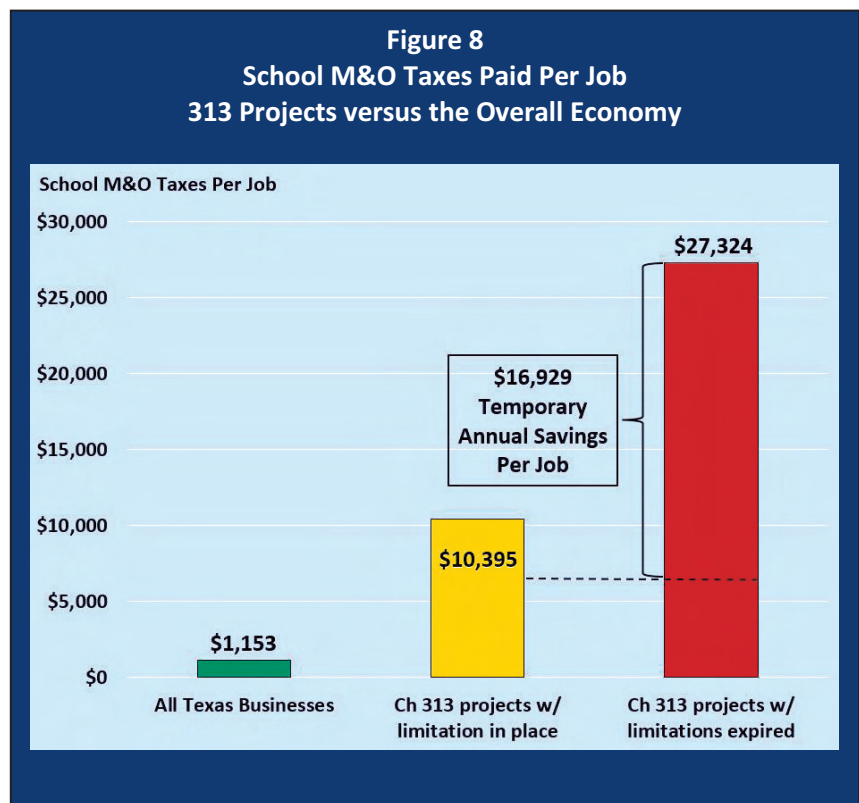
Chapter 313 and Jobs

One of the criticisms of Chapter 313 relates to the high amount of property taxes “lost” relative to the number of jobs the program creates. In 2015, \$19.7 billion of value was exempted from school M&O taxes as a result of Chapter 313 limitation agreements—equating to approximately \$208 million of foregone property taxes. With a reported 12,321 jobs at Chapter 313 projects, that equates to a whopping \$16,929 for every job created. The argument runs that the state is “paying” nearly \$17,000 for each job created.

This is a specious allegation for several reasons.

First, as pointed out previously, Texas statutes require a 313 limitation applicant to demonstrate that it is a determining factor in the decision to invest in Texas—without the limitation, the project would locate elsewhere, and zero taxes would be paid to Texas. Consequently, the state is not “losing” any tax dollars.

Second, the jobs numbers only look at the operations jobs at the project work site. It does not include jobs during the construction phase, nor does it include off-site support jobs. For example, many projects are supported by contract, rather than direct labor. These jobs are excluded from the job count even though they may directly stem from the project. Consequently, the state’s reported numbers undercount the actual number of jobs.



Third, even with the limitation in effect, Chapter 313 projects in 2015 paid an average of \$10,395 in school M&O taxes for each job they created. Economy-wide, the average Texas employer paid \$1,153 in school M&O taxes for every job it created in 2015. **That means the average 313 project paid more than nine times the amount of school M&O taxes per job as the average Texas business—even with the limitation in effect! And once the limitation expires, those projects would pay roughly \$27,000 in school M&O taxes per job—almost 25 times more than the average Texas business pays per job (Figure 8)!**

The high “cost” of creating jobs through Chapter 313 is not a true cost at all; in fact, it is actually a measure of the tremendous barrier Texas’ high property taxes impose on capital-intensive industries.

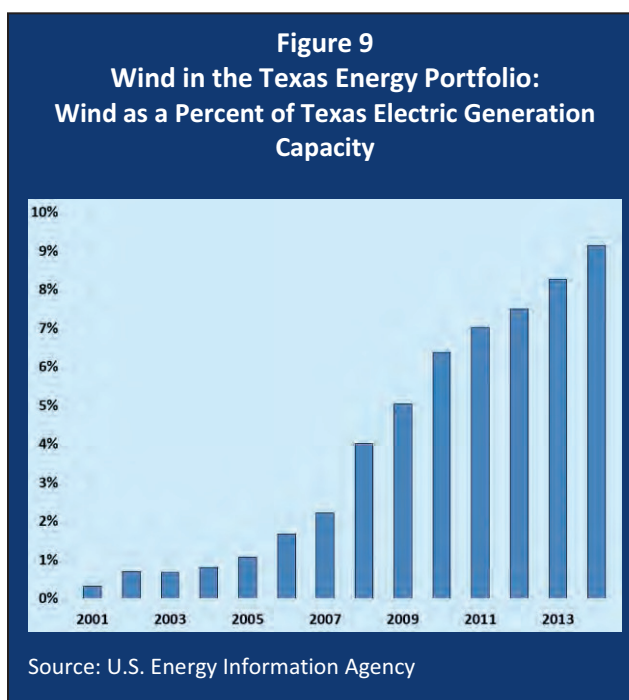
Renewable Energy and Chapter 313

Among the projects eligible for Chapter 313 limitations are those involving renewable energy. Of the 311 projects reported through 2015, 144—almost half—were wind energy projects. Renewable energy projects were included in Chapter 313 through a House floor amendment to the original bill in 2001. At the time, Texas electric utilities were being deregulated, with very aggressive targets set for renewable energy capacity.⁶ Adding renewables to Chapter 313 was viewed as a way to encourage clean energy while easing the cost of complying with the new mandate (renewables tend to be a more costly method than traditional electric power generation). Further, wind energy was considered a method to encourage rural economic development, so its inclusion allowed rural Texas to compete for new investment projects.

What draws attention, however, is that only 10 percent of all the jobs created under Chapter 313 are wind farm operations jobs (1,170 of 12,321). And job creation requirements are commonly waived as a part of the limitation agreement. The Chapter 313 jobs numbers, however, understate the actual totals associated with the turbines. The majority of wind-related jobs are not permanent on-site jobs, which is what Chapter 313 counts. Instead, the bulk of wind jobs are turbine manufacturing, turbine installation and contract maintenance—none of which are reported under Chapter 313. Total wind-related jobs in Texas today are estimated at 24,000, thanks largely to investments made possible by Chapter 313.

Another allegation is that wind projects reap the benefit from the temporary taxable value limitation under Chapter 313, but by the time the limitation expires, the projects have depreciated to zero value and add nothing to the tax rolls. In fact, depreciation is a consideration in valuing business personal property, but appraisers also consider what the equipment would sell for and how much income it generates. A survey of wind projects in Nolan County reveals that the average value decline of a wind project is 3 percent per year, which implies a project will decline in value by 27 percent from its peak value after 10 years, ultimately going onto the tax rolls at 73 percent of its peak value. Of course, individual projects may vary substantially from the average, depending on the hours the turbines operate (i.e. the income they generate).

It is difficult to apply the same measures of industrial economic development projects to renewable energy projects. Industrial projects are about creating economic output, growing tax bases and creating jobs. Energy projects are about expanding infrastructure to service the state’s energy needs. Ultimately, the state’s efforts to



⁶ SB7 by Sibley in 1999.

expand its renewable energy portfolio should be judged a success. Wind energy was not a significant portion of the state's energy portfolio in 2001, when Chapter 313 was enacted. By 2014, almost 10 percent of the state's electrical generation was from wind projects (Figure 9).

Conclusions

Chapter 313 allows certain projects a temporary school property tax incentive in return for investing in Texas. History has shown that absent some type of school tax incentive, Texas will lose substantial new investment to other states and countries.

Given Texas' heavy reliance on local property taxes, particularly to finance public schools, Chapter 313 is the state's most critical economic development tool. While the program has been criticized as costly because of the amount of tax breaks offered, the foregone taxes are revenues the state would never have collected otherwise. In fact, the program generates new revenue for the state by attracting projects that would not otherwise have invested in Texas.

Relative to similar programs in other states, Chapter 313 tax benefits tend to be small and the paperwork immense. However, the incentives are sufficient enough that, when combined with other positive aspects of doing business in Texas they can swing many projects our way.



Texas Taxpayers and Research Association

400 West 15th Street • Suite 400
Austin, Texas 78701
(512) 472-8838
ttara@ttara.org • www.ttara.org

President	Dale Craymer
Senior Analyst	John Kennedy
Counsel	Debbie Cartwright
Senior Analyst	Sheryl Pace
Analyst	George Christian
Director of Communications	Ryan Ash
Director of Marketing	Nancy Shields
Office Manager	Betty Wranischar