FINAL REPORT

Summary of the Financial Impact of the Proposed ETC Texas Pipeline, LTD Gas Processing Plant on the Ganado ISD Under a Requested Chapter 313 Property Value Limitation

Prepared By
Douglas L. Karr, Ed.D.
Contracted Services in School Finance

May 26, 2012

Introduction
ETC Texas Pipeline, LTD (ETC) has requested that the Ganado ISD (GISD) grant a property value limitation under Chapter 313 of the Texas Tax Code for the construction and operation of a gas processing plant. An application has been submitted by ETC to GISD and the GISD Board of Trustees approved that application on April 19, 2012. ETC proposes a minimum qualified investment of $10 million in this project with a total estimated qualified investment of $299 million as set forth in the application. This project is consistent with the state's goal for economic development, the expanded intent of House Bill 1200 as passed by the Texas Legislature in 2001, and Chapter 313 of the Texas Tax Code.

Background
In accordance with the application, this project will be fully taxable for both maintenance and operations (M&O) and debt service (I&S) purposes in the first two years (school years 2013-14 and 2014-15) which represent the project's qualifying time period. GISD intends to offer a value limitation for this project of $10 million effective school year 2015-16 through 2022-23. As a result, the project will impact the local tax roll of the school district at that same amount for M&O taxes only. Taxes for debt service, voter approved projects financed by the sale of bonds, will continue at the full taxable value. I&S taxes for any future projects approved by the voters of the district will also be assessed against the full taxable value. Depreciation will reduce the taxable value of the project over time.

While taxes are collected by the district on the current year county appraisal district (CAD) value, the state funding formulas use the comptroller's property tax division (CPTD) value for the purpose of calculating the district's required local shares within the funding tiers of that formula. The CPTD is a reflection of last year's CAD value; therefore, it lags behind the CAD value in all years. As a result, state and local revenues are generated by two different values in any given year.

With the passage of House Bill 1 in the 2006 special legislative session, the school finance system in Texas moved from one that was formula driven with a maximum M&O tax rate of $1.50 to one that was, and continues to be, target revenue driven at a maximum tax rate of generally $1.04, voter approval for a higher tax rate up to $1.17 notwithstanding. This means that most districts now receive additional state aid for tax reduction (ASATR) to offset the loss in state and local funds at the new maximum $1.04 M&O tax cap vs. what was previously generated at the $1.50 maximum M&O tax cap.

With the passage of Senate Bill 1 in the 2011 special legislative session, funding reductions to the school finance system in Texas amounted to $4 billion for the biennium or $2 billion each year of the biennium. To accomplish these reductions, schools' regular program allotments are reduced by 7.61 percent in school year 2011-12 while those same calculated allotments are reduced by 2 percent in school year 2012-13 in addition to the ASATR funding also being reduced by 7.65%. The stated goal is for ASATR revenue to be completely eliminated by school year 2017-18. Currently filed legal challenges and future legislative sessions will determine the course of school finance beginning in school year 2013-14 and beyond.

Assumptions

As required of chapter 313 projects, 15 years of data must be assimilated in order to produce revenue projections for that same number of years. The revenue projections for the GISD that accompany this project, therefore, adhere the following general assumptions:

1. The current school funding system and formulas as set forth in Senate Bill 1 were used to project state aid; although, no guarantee exists that this system or these formulas will remain in effect after the 2012-13 school year.
2. This system and its formulas are driven by student data, property values, and tax collections. As a result, certain assumptions were made concerning each of these details.
3. The student counts were held constant across the 15 years.
4. The preliminary CAD taxable value for school year 2012-13 as released on or about April 30, 2012 was used as the base value to which the estimated project values for each year as set forth in schedule B of the application were added. These projected CAD values were then used for the CPTD values in each of the following years based on the lag between these two values as heretofore explained.
5. Tax collections each year were based on the district's 2012-13 projected M&O rate of $1.04, projected I&S rates each year ranging from $0.063 to $0.215, and an assumed collection rate of 100 percent each year.

These assumptions allow for the isolation of the effects of the property value limitation on the district's finances. The detail of these assumptions are summarized and depicted in Table I.

School Finance Impact on the District

In accordance with the proposed agreement and under the assumptions heretofore outlined, two models were prepared for comparison purposes in an effort to determine the projected financial impact, if any, to GISD resulting from this agreement.

The first model projects state and local revenue to the district under the agreement. In it, the taxable value of the project each year is added to the district's baseline taxable value including those years in which the value limitation is applicable.

The second model projects state and local revenue to the district without the provisions of the agreement. In this model, no value limitation is applied to the district's base taxable value; instead, the full taxable value of the project when added to the district's base year taxable value is used in place of the value limitation.

A summary of the differences is depicted in separate spreadsheet entitled "Exhibit B." A loss to the district is noted only in year 3 resulting from the agreement due to the value lag between the CPTD and CAD values during the first year of the value limitation and due to recapture. Gains are noted in years 4-11. The larger gain noted in year 11 is due primarily to another value lag between the CPTD and CAD values, the inverse of that observed in year 3. ASATR funding is not a factor for GISD as the district's revenue is completely formula driven in school year 2012-13 and beyond. It should be noted, however, that this source of funding will come under future legislative review as early as the 2013 legislative session. **NOTE:** Because ASATR funding has the effect of offsetting school district revenue losses arising from limitations on the value of a qualified investment, any reduction of ASATR funding after the 2012-13 school year, if applicable, may result in significant increases in the amount of estimated revenue protection payable by the applicant to the district pursuant to the tax limitation agreement.

Impact on the Taxpayer (ETC)

As heretofore mentioned, the property resulting from this project is fully taxable in the first two years under this agreement. In year three, the tax value limitation applies, but only to the M&O taxes collected at the assumed M&O tax rate of $1.04 per $100 of taxable value.

Under the assumptions used herein, the potential tax savings resulting from the value limitation total $25,178,437. In addition, ETC is eligible for a tax credit on taxes paid on value in excess of the value limitation in each of the first two years. The cumulative tax credits are projected to be approximately $6,069,449; although, the Texas Education Agency (TEA) issues the reminder that these estimates will be recalculated based on current data prior to any issuance of the tax credits. The school district is to be reimbursed by the state for tax credit payments.

A separate spreadsheet entitled "Ganado ISD & ETC Texas Pipeline (Comptroller's Beta Spreadsheet)" illustrates both the projected tax savings and tax credits.

Facilities Funding Impact

The ETC project remains fully taxable for I&S taxes. This stipulation applies not only to the district's current debt, but also to any future debt the district's voters may choose to incur.

GISD is currently eligible for facilities assistance from the state in the form of existing debt allotment (EDA) and instructional facilities allotment (IFA). Increasing CPTD values resulting from taxable value added by the project will obliterate future EDA and IFA state share payments beginning in school year 2014-15 and thereafter until GISD final year of debt service in 2026-27. As modeled, however, the increase in taxable value net of depreciation resulting from the project and the fact that the full value of this project remains fully taxable will more than offset, any loss of state facilities assistance at a projected tax rate of approximately $0.063 beginning in year 2 ranging up to $0.101 in 2026-27. By comparison, the projected I&S tax rate for school year 2012-13 is $0.215.

Summary

While some uncertainty exists with regard to the future of the state's public school finance system, the following points appear to currently apply to the ETC project and the GISD:

1. It meets the intent of the economic development initiative for the State of Texas.
2. It increases the district's I&S tax base without creating substantial financial loss for the district with regard to M&O earnings over the term of the project.
3. It produces substantial tax incentives and savings for ETC.