

## Who's Afraid of Sunlight? Explaining Opposition to Transparency in Economic Development

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### Abstract:

Why do some firms oppose transparency of government programs? In this paper we explore legal challenges to public records requests for deal-specific, company-specific participation in a state economic development incentive program. By examining applications for participation in a major state economic program, the Texas Enterprise Fund, we find that a company is more likely to challenge a formal public records request if it has renegotiated the terms of the award to reduce its job-creation obligations. We interpret this as companies challenging transparency when they have avoided being penalized for non-compliance by engaging in non-public renegotiations. These results provide evidence regarding those conditions that prompt firms to challenge transparency and illustrate some of the limitations of safeguards such as clawbacks (or incentive-recapture provisions) when such reforms aren't coupled with robust transparency mechanisms.

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## 1. Introduction

Government transparency can improve public policy as well as public trust in government. Revelations enabled by open records laws have prompted numerous calls for domestic and international government reform. (Mizrahi and Vigoda-Gadot. 2009, Kim and Lee 2012). In the United States, the lack of transparency surrounding the economic development activities of states and cities, such as the use of targeted tax incentives to encourage business investment, has been heavily criticized by scholars and activists (LeRoy 2005, Jensen and Malesky 2018). Recent efforts by activist NGOs and governments have led to increased transparency in many economic development programs.<sup>1</sup> Yet little is known regarding the effects of these reforms.

In this project we take a novel approach to this question by examining the transparency behavior of corporate beneficiaries of economic development programs. These economic development programs, or incentives, are financial support for firms in exchange for promises of capital investment or job creation. These financial benefits for firms can come with political or societal costs. For example, great opposition resulted from the announcement of Amazon's second headquarters in New York City due to the almost \$3 billion in incentives offered to the company. Similarly, protest against incentives for Amazon in Virginia and Foxconn in Wisconsin haven't gone unnoticed as well. Additionally, industry trade publications such as *Area Development* included advice to firms on how to avoid unwanted media scrutiny of these deals (Harris 2018).

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<sup>1</sup> For example, the NGO Good Jobs First began "grading" states on deal-specific transparency in 2007. It found then only 23 states with even one program disclosed online. By 2015, it found that all 50 states and the District of Columbia were disclosing online. In 2008, Good Jobs First began aggregating this state data, along with federal and local-government records, in its Subsidy Tracker, an online database.

Given the sensitivity of this policy area, we specifically examine firms' responses to public records requests for information on their economic development incentive deals that they received from a state economic development program. We argue that by understanding firm preferences for or against transparency, we can begin to understand the implications of this transparency revolution for policymaking as well as the types of activities that firms are attempting to shield from public scrutiny.

Specifically, in our paper, we examine firm opposition to public records requests from the State of Texas discretionary economic development program, the Texas Enterprise Fund (TEF). This program selectively awards cash grants to companies relocating or expanding operations in Texas in exchange for job creation. The TEF includes clawback or recapture provisions that allow the state to enforce incentive agreements by delaying payment, canceling contracts or even forcing repayment of past grants with interest. We made public records requests for TEF deals and then documented which firms challenged our requests by attempting to withhold or redact parts of their state files.

Our records request, specifically for company-specific applications and contracts, was submitted to the Texas Office of the Governor. Then, the subject companies were notified and given the opportunity to challenge our request. We reviewed these firm challenges to examine why each respective firm challenged our request and what types of information they were attempting to withhold from us. Firms challenged our public records request in 45 out of the 164 total grant contracts.

Although companies were partially successful in limiting our public records requests, we were still able to acquire two valuable sets of documents from the State of Texas. First, the State of Texas released to us a list of all companies that have amended their Texas Enterprise Fund contracts. These amendment documents are not public and to our knowledge haven't been reported

by the media or announced by the state. Second, the state complied with our public records requests by releasing batches of partially redacted amendment and application documents in waves. In total, we have received applications, agreements and any amendments from 90 of the 164 TEF grants. Some of the documents are partially redacted, but in all cases, we have been able to document how the amendments differ from the original incentive agreement.

What explains a firm's legal challenges to our public records request? We focus on two potential explanations –firms that have been subject to formal clawback penalties for non-compliance, and firms that have privately renegotiated their incentive contracts in order to reduce or delay their job creation commitments to avoid clawbacks.

The State of Texas monitors the performance of the Texas Enterprise Fund, and has imposed public clawbacks, or grant recapture, for many companies that participate in the program. These formal contract provisions enforce the negotiated terms for job creation and wage levels. The State may also rescind awards for defaulting, along with additional financial penalties. Information detailing such penalties is public, posted directly on the government website in an accessible table format.

What isn't public is that a large number of companies have renegotiated their TEF agreements. Renegotiations usually come in the form of committing to fewer jobs created, or changing the hiring schedule, or how headcount should be computed (with some renegotiated deals allowing firms to count employees in subsidiaries that weren't party to original TEF-subsidized project). In many cases, such contract amendments are made right before a company would otherwise be subject to clawback provisions. For example, in one case, an incentive agreement was changed to reduce the number of jobs required just one day before an employment deadline.

Statistical analysis of which companies challenged our public records request suggests that factors such as the size of the incentive or the number of jobs proposed have little predictive power

in explaining the challenges. To our surprise, we found that companies that had been subject to clawbacks or recapture in the past were less likely to challenge our request. Conversely, companies that had negotiated secret amendments to their TEF agreements were much more likely to seek closure for their files.

These results suggest to us that the firms that have already been subject to publicly disclosed clawbacks for failing to fulfill the conditions of their agreements had little incentive to block investigations into their applications and agreements. Rather, companies that had made amendments to their agreements, which to our knowledge had never been made public, challenged our public records request.

In the final section of the paper we examine a sample of these applications and find a clear pattern regarding amendments. First, a large share of these companies amended their applications to lower their job-creation requirements and thus ease compliance with the conditions of the grant. Our analysis doesn't include any verified external data on the companies' actual jobs, but this pattern is consistent with companies renegotiating their incentive contracts, often also agreeing to smaller grant awards, in order to avoid public clawbacks. We also found other kinds of application amendments, such as how jobs are defined, and how much of a penalty a company will be obligated to pay in the event of non-compliance with the contract.

We are careful to note that these amendments, although in some cases particularly egregious, aren't uncommon across states. In two states that make their contract awards public, California and Michigan, we also observe the use of amendments. We suspect that the use of amendments is widespread, but without state by state public records requests, we don't know how representative Texas is relative to other states.

Our results also speak to the academic literature on the implications of transparency for firms. Although our study focuses on a single incentive program, the firms involved in this study are

large, often multinational firms with the ability to locate across the country. Our study suggests that although some firms renegotiated their contracts to limit the costs of the clawback, many of these amendments were targeted to avoid a publicly-disclosed clawback, even if that meant accepting a smaller incentive award. This suggests that the public stigma from being identified as non-complaint with an incentive award is a motivating factor in renegotiation as well as the motivation for challenging the transparency measures. We suspect that these preferences for avoiding public non-compliance with awards is generalizable across states.

Our results are troubling for what has been seen as best practices in economic development. Clawback provisions and transparency are considered fundamental safeguards for assuring that taxpayers are protected and that companies are held to accountable in terms of job creation and wages, although there is considerable variation in the implementation of these standards.<sup>2</sup> As noted by Mattera et al (2012) in their landmark study of clawbacks provisions, many states fail to publicly disclose clawbacks and many states fail to properly enforce facially sound provisions. Our results suggest an additional concern. Companies can not only avoid clawbacks through private renegotiations, they can also use open records appeals to limit the transparency of these programs.

## **2. Economic Development Programs and Firm Preferences on Transparency**

Countries, states and cities around the world use specialized policies to attract investment. This includes the use of investment incentives which can be in the form of tax holidays, tax abatements, cash grants, subsidized loans or infrastructure for a firm. The drivers for the use of these programs are multifaceted. Proponents of these policies argue that individual incentives can lead to positive economic development spillovers that justify their use, although much of the

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<sup>2</sup> See LeRoy (1997) for one the first collection of clawback provisions in the United States.

academic literature is skeptical of this position.<sup>3</sup> Others, such as Li (2006) argue that governments can use these policies to overcome barriers such as the weak rule of law as a means of compensating firms for these other barriers. Rickard (2018) argues that electoral geography shapes these decisions to provide private benefits to individual firms. Jensen (2018) shows that program design can influence the overuse of incentives, even when there is considerable transparency in the program. Jensen and Malesky (2018) argue that the main motivation for the overuse of these programs is for government officials to claim credit for firms that locate in their districts.<sup>4</sup>

Despite the considerable attention on the impact of incentives and the potential for rent seeking, surprisingly little has been written on the role of transparency in economic development. Although the empirical evidence has been mixed, increasing the transparency of the policy process has been heralded as one of the keys to reducing government malfeasance and corruption (Rose-Ackerman 1999)<sup>5</sup>. Studies on corruption have found that increasing transparency can either decrease (Islam 2006) or increase (Escaleras et al 2010, Costa 2013) perceived corruption. Cordis and Warren (2014) argue that transparency can deter corruption by uncovering it, which can have opposing effects on the perception of corruption. Using actual corruption conviction data, Cordis and Warren find that strong Freedom of Information Act (FOIA) laws in the United States increase the likelihood that corruption will be deterred, uncovered, and/or prosecuted.

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<sup>3</sup> See Jensen and Malesky (2018) for a review. See also Austin et al (2018) for a review of place-based policies.

<sup>4</sup> Jensen, Malesky, and Walsh (2015) find that more directly elected politics offer larger incentives and are less likely to provide oversight of these programs. See Fox (2007) on transparency and policy making.

<sup>5</sup> Another literature studies the impact of fiscal transparency rules on government performance. See Alt et al (2002) and Alt et al (2006) for examples. Bac (2001) argues that transparency can decrease corruption through the detection of illegal activities but it can also increase corruption by providing outsiders information on the key decision makers to target for illicit activities.



Evidence shows that the political environment shapes the creation of transparency laws. In one of the most comprehensive studies on the topic, Hollyer, Rosendorff, and Vreeland (2018) find that democratic regimes are more likely to provide transparency in their economic data, which reinforces democratic institutions and facilitates the attraction of more investment. Wehner and de Renzio (2013) find that democratic states are more likely to have strong fiscal transparency infrastructure, and that the effect is greatest in the presence of high levels of partisan competition. In the U.S. context, Berliner (2014) shows that states enact strong FOIA laws where there is political uncertainty over who will control the government in the future. This political competition finding is one of the clearest in the literature (Alcaide Muñoz et al. 2017). These laws provide transparent institutions that seem to be more effective at providing information than informal requests from government agencies.<sup>6</sup>

Bureaucracies may also selectively provide information based on the attributes of the requestor, including partisanship (Porter and Rogowski 2018) and gender (Rodríguez and Rossel 2018). Other studies find that the political context, such as the polarization of politics (Wood and Lewis 2017) or the perceived behavior of other government agencies towards FOIA requests (Ben-Aaron et al 2017) all impact responses.

Many of these studies examine how variation in bureaucracies or requests affect responses. Little is known about how third parties, specifically corporations, respond to these public record acts. Management scholarship has examined voluntary disclosure in areas such as political spending (Goh et al 2019) and financial reporting (Leuz and Wysocki 2016), but it lacks work focusing on firm responses to disclosure laws. Jensen and Malesky (2018) find that numerous industry associations as well as state economic developers formally protested new rules to improve the

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<sup>6</sup> See Worthy et al (2017) for experimental evidence from England.

transparency of tax incentives. In this study, we explore the different firms' responses to these requests.

Our focus on the preferences of firms on the disclosure of economic development incentives provides a broader window into firm preferences for transparency. Academics have long been critical of these programs, arguing that the majority of economic development incentives provided in the form of cash grants, property tax abatements, or income tax credits are particularly ineffective (Busse 2001). A recent meta-analysis of 34 studies by Bartik (2018) finds that the majority of incentives are offered to firms that already have plans to relocate or expand in a given location. The studies' findings range from only 2% to 25% of incentives tipping investment decisions to a given location, with the remaining 98% to 75% of firms maintaining preexisting plans.

Nationally, economic development incentive programs have come under fire across a number of states, including Texas. The specific program that we are exploring, the Texas Enterprise Fund, has been the subject of numerous controversies<sup>7</sup>, sparking a heated debate in a recent legislative session over whether to defund the program.<sup>8</sup>

While criticisms of the program can be detrimental to firms, even more important is the information contained in these reports can be individually damaging to a firm's reputation. This can include information on a firm's financials, which are required upon application, as well as awareness of the inability for a firm to fulfill its promises.

In some states, firms have a limited ability to withhold incentive information, such as Michigan which provides full disclosure of firms' contracts. Interestingly, many of these contracts contain amendments, which are often admissions by the company that it cannot fulfill the initial terms of its incentive contract. These contracts are reported in the local press and include negative

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<sup>7</sup> McGaughy (2014).

<sup>8</sup> Walters (2017).

press stories on amendments that are sought after by companies to provide fewer jobs than initially pledged.<sup>9</sup> Yet this transparency isn't complete, as the Snyder administration recently used a non-disclosure agreement with General Motors to avoid disclosure of its total tax incentives.<sup>10</sup>

Thus, Michigan provides us with an example of a state where due to the publicly available incentive contracts, we can observe the large number of amended contracts. In the next section we examine the flagship Texas incentive program, which is the largest “deal closing” fund in the country. Unlike Michigan, these incentive contracts are not publicly available and Texas law allows firms to challenge disclosure. We argue that this is the perfect environment for examining how firms respond to transparency requests.

### **3. Public Information Requests and the Texas Enterprise Fund**

Texas has a number of economic development programs, but none are as high profile as the Texas Enterprise Fund. This “deal closing fund” was created in 2003 to target firms considering either Texas or other out of state investment locations. According the Office of the Governor (2017, 3), “The fund is used only as a final incentive tool where a single Texas community is competing with another viable out-of-state option.” In other words, awards are made on a discretionary basis; they are not “as of right,” or automatic based on a company performing an eligible activity. Texas Enterprise Fund awards can be made only by a unanimous vote of the Governor, Lieutenant Governor, and Speaker of the House of Representatives.

With an original allocation of \$295 million dollars, this fund is the largest deal-closing fund in the United States. As of 2017, just over \$600 million in grants had been awarded to 146 projects

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<sup>9</sup> <https://www.detroitnews.com/story/news/politics/2015/02/05/michigan-tax-credits-car-companies/22908711/>

<sup>10</sup> <https://www.autonews.com/article/20181203/OEM01/181209951/gm-may-keep-cashing-in-michigan-tax-credits-after-cuts-closures>

guaranteeing 83,000 jobs.<sup>11</sup> A wide range of firms have received TEF grants, and in some cases multiple awards. Recipients include Apple (two awards of \$21 and \$25 million), Cabela's (\$400,000), Caterpillar (\$1.1 million and \$8.5 million), Chevron (\$3 million), Citgo (\$5 million), Dow Chemical (\$1 million, \$1.5 million), Facebook (\$1.4 million), Kohl's (\$750,000), LegalZoom (\$1 million), Lockheed Martin (\$4 million), Merck (\$6 million), Samsung (\$10.8 million), Sematech (\$40 million), SpaceX (\$400,000), Texas Instruments (\$50 million), Toyota (two awards of \$40 million each), and Visa (\$7.9 million). These Texas Enterprise Fund awards were often accompanied by local incentives<sup>12</sup> and potentially other state incentives.

The Texas Enterprise Fund hasn't been without controversy. A scathing audit of the program in 2014 uncovered numerous weaknesses, including companies being awarded grants without filling out formal applications, companies having no job creation obligations for awards, as well as poor oversight and monitoring (State Auditor 2014). Numerous news outlets ran stories on the program and high-profile politicians including the then House Speaker Joe Straus, have criticized the program.<sup>13</sup>

In an unrelated case, after this audit, the Supreme Court of Texas issued a ruling that was criticized by transparency experts in the state. In *Boeing vs. Paxton*, the Court ruled that if disclosed records would put governments or companies at a competitive disadvantage, they could legally be withheld. The *Boeing* ruling has been invoked by numerous firms and government agencies, most famously by the city of McAllen, Texas to shield the details of its contract, including the fee, for an Enrique Iglesias concert.<sup>14</sup> In the context of our study, the *Boeing* ruling provides a legal avenue for

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<sup>11</sup> [https://gov.texas.gov/uploads/files/business/TEF\\_Listing\\_10-11-18.pdf](https://gov.texas.gov/uploads/files/business/TEF_Listing_10-11-18.pdf)

<sup>12</sup> Typically the Texas Enterprise Fund matches, and exceeds local incentives offers. In some cases firms withdraw from the local incentives programs and continue in the Texas Enterprise Fund program.

<sup>13</sup> Poppe (2018).

<sup>14</sup> See Collins (2018) for an excellent overview.

firms receiving economic development incentives to challenge public records requests seeking information on their applications or contracts. As a result, affected parties—including government actors, consultants and the firms receiving awards— are given ten days from notification by Office of the Governor to formally challenge the public information request.

#### **4. Research Design and Methods**

Our original research project began as a study of economic development in Texas, issuing public records requests for all application materials as well as contracts for the Texas Enterprise Fund (TEF). Given that our original inquiry was not about transparency, our research here is not experimental, nor did we have clear theoretical expectations prior to data collection. Thus, our research design is observational and exploratory, yielding insights into the workings of this program as well as theory regarding firm behavior around transparency.

Our public records request was submitted on November 28, 2017 which included all applications as well as the formal contracts for every applicant to the program since inception.<sup>15</sup> Application materials include a formal application, two years of financial statements, as well as other materials. Contracts include the formal contract between the state and the company as well as any amendments.

Third parties were given ten days to respond to this request. They presented legal challenges and the Office of the Attorney General issued a letter on March 28, 2018 summarizing their comments. A total of 45 third parties legally challenged our request including 44 companies receiving TEF awards.<sup>16</sup>

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<sup>15</sup> The Office of the Governor generated a cost estimate of \$1,207.60 which was deposited on Dec 19 2017.

<sup>16</sup> One consulting company involved in economic development impact analysis for applications also responded.

Many of these companies cited the *Boeing* ruling in their complaints. In the Office of Attorney General's summary (March 28, 2018, 3): "ADP, Allstate, Apple, BASF, Charles Schwab, Chevron, CITGO, Comerica, Cordish, eBay, E&Y, Fred's, Fritz, GM, GSF, Hulu, Reuters, USAA, and Westlake Chemical each state they have competitors and the release of their information at issue would give their competitors an advantage." Some of these firms, along with others, also used arguments on trade secrets to shield parts of the application, including CED, Corrigan, Cordish, Dow, HMS, Kubota, Lockheed-Martin, Riseever, Toyota and Visa. Many of these same firms, including Apple, Cordish, Fred's, GATX, GGNCS, Payless and Riseever also raised legal exceptions for economic development activities through Section 552.131 of the Texas Government Code. In addition to these challenges, firms included other additional challenges, such as USBC's claim that notes in the margins of the application constitute attorney-client privilege.

We are careful in our interpretation of these challenges given that many of these legal challenges were both broad and initiated by hired legal counsel. For example, Apple's public records challenge, from law firm DLA Piper, was one of the broadest in the group, challenging almost every aspect of the application, including the already public information in the document, using numerous cases as well as exceptions for economic development. It is unclear if this especially aggressive legal challenge was at the direction of the company, the firm, or a particularly ambitious associate at the firm. We simply assume that the challenge, and not the specific details, are done at the request of the company.

As we note below, these legal challenges were partially successful; a number of the application and contract documents that we received through our public records request included redacted sections. Despite these partially successful legal challenges, this public records request yielded three pieces of data that we discuss in more detail. First, the State of Texas provided a complete list of all companies participating in the programs and the companies which have amended

contracts to their agreements. This list doesn't provide details on the content of the amendments, but it allows us to determine which companies made changes to original agreements. Second, the Office of the Governor released redacted application and agreements. We have received a total of 48 out of 56 amended contracts and can document the changes from the original contract. The missing amendments, listed in Appendix B, largely consisted of a number of agreements that never formally submitted applications to the program or didn't have detailed contracts to begin with. This was noted by a 2014 state audit and was the subject of a number of critical media stories about mismanagement of the Texas Enterprise Fund under then Governor Perry (McGaughy 2014). Third, we have the complete list of companies that challenged our public records request. Thus, we have a data set that includes all company participants in the program, we know which companies challenged our public records request, and for 90 of the grant contracts we have the contents of the firm's applications, agreements and any amendments.

For our purposes, we do not focus on the legal arguments made by the third parties in their challenges, although our robust tests and empirical analysis do allow us to exclude certain types of legal challenges. Our main dependent variable for our project is whether a third party challenged our public records requests. Focusing only on the projects that have received funding (not new applicants that have yet to receive a first disbursement), we assigned an independent variable denoting the total awards, and a dependent variable signifying the total legal challenges to our request (See Appendix A).

We examine two main explanatory causes. First, TEF has a formal process of allocating incentives after certain job-related benchmarks are met. Clawbacks (or recapture) provisions allow firms that are found to be non-compliant with the terms of their incentive award to be punished. These clawbacks have become best practice in economic development (Ledebur and Woodward 1990) although there are concerns about the willingness of politicians to enforce these sanctions and

doubts as to whether such measures actually improve the performance of these programs (Weber 2002, Mattera et al 2012, Jensen 2017).

Since clawback events are publicly disclosed on the TEF program website, we code firms that paid a clawback or a similar repayment with a 1, and 0 for those with no repayments. A total of 61 firms in our data set paid clawbacks in the period of 2003 to 2017. We code *Clawback Dummy* as 1 for any firms that had paid a formal clawback at the time of our public records request (November 2017).

Our second explanation pertains to what we believe is the first discovery of amended contracts in TEF data. Numerous project agreements were amended after the initial award, in many cases lowering the number of jobs necessary to fulfill the TEF obligations, changing the definition of a job (sometimes even allowing project headcount to include subsidiaries that weren't included in the original application), or changing the job-creation schedule in its entirety. In most cases, these changes led to both fewer jobs and smaller TEF grants. To our knowledge, these amended agreements have heretofore not been public documents.

Our study codes amendments in two ways. First, we requested a list of all companies that received amendments as a follow up to our public records request.<sup>17</sup> We proceeded to Code *Amended Contract* as 1 for all such companies.

After receiving this list from the Governor's office, we checked this list against a sample of contracts and did notice a small number of discrepancies between the Governor's office list and our own documented amendments. We realized that some contracts may have been amended before

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<sup>17</sup> The office of the Governor has been releasing batches of contracts to us through this public record process. After receiving numerous amended contracts we submitted a follow-up request for a list of all amended contracts. The Office of the Governor provided us with this list. Thus we have the full list of amended contracts, but as of writing this paper, we do not have the content of all of the amended contracts.



their projects began, such as a contract with SpaceX, and thus were not listed as having been amended on the Governor's list. Thus, as a second coding, we simply coded all firms that had undisbursed funds at the time of our public records request with a 1. The correlation between these two measures is 0.82.

Following the advice of Lenz and Sahn (2018), we utilized probit models with no control variables denoting the firm's legal challenge as the dependent variable. We present four probit models in Table 1; the coefficient estimates are marginal effects at the mean (MEMs). Our first model includes only our *Clawback Dummy* and dummy for an *Amended Contract*. Across all four models we find a consistent sign and size of the coefficient on clawbacks, although the variable becomes statistically insignificant when we include a control variable for the size of the investment.

To our surprise, we find that firms that have been subjected to clawbacks were 12-15% less likely to have challenged our public records request. One interpretation of this result is that these companies have already been revealed publicly for not complying with the agreement and faced a financial penalty, leaving less incentive to shield their contracts from public records request.

Our main finding is that amended contracts, regardless of the amendment process, have a significant impact on whether firms challenged our public records requests. Firms that have amended their contracts are between 15% and 24% more likely to have challenged our public records request. Our results are consistent to additional robustness test including dummy variables in Models 5 and 6.

**TABLE 1: Modeling Public Record Challenges**

	<i>Dependent variable:</i>					
	Legal Challenge					
	(1)	(2)	(3)	(4)	(5)	(6)
Clawbacks Dummy	-0.152** (0.08)	-0.156** (0.08)	-0.121 (0.08)	-0.135* (0.08)	-0.143* (0.08)	-0.148* (0.08)
Amended Contract	0.178** (0.09)		0.158* (0.09)		0.225** (0.10)	
Amendment Proxy		.244*** (0.08)		0.224*** (0.08)		0.264*** (0.08)
Award Size (ln)			0.0397 (0.03)	0.0271 (0.02)	0.0226 (0.03)	0.0107 (0.02)
Industry Dummies	No	No	No	No	Yes	Yes
Observations	125	125	125	125	125	125
Pseudo R <sup>2</sup>	0.05	0.10	0.07	0.10	0.13	0.16
$\chi^2$	6.31	10.14	8.64	10.92	17.81	21.14

*Note:* Coefficients represent marginal effects. \*p<0.1; \*\*p<0.05; \*\*\*p<0.01

*Note:* Probit models presented as marginal effects. Firm legal challenges as the dependent variable. Robust standard errors in parentheses. \*\*\* p<0.01, \*\* p<0.05, \* p<0.1

Our results provide suggestive evidence that firms that have amended their incentive contracts are more likely to challenge public records request for information on their projects. Given the small sample size we are careful in our interpretations of these results. Yet, this is consistent with firms blocking records requests to hide details of amended contracts.

Another important limitation of our work is that we do not know what is in all of these amendments, and whether there is a causal relationship between potentially embarrassing information and a firm's legal challenges. We turn to this question in the next section.

## 5. Case Studies: Company Amended Contracts

The results of our regression analysis indicate, firms that amended their original grant contracts were more likely to challenge our public records request, and firms that paid clawbacks were less likely to challenge. One possible explanation for this result is that firm challenges are not driven simply by whether the firm underperformed/overpromised, but instead by whether its underperformance was public information.<sup>18</sup> It could be that amending firms are pulling a bait-and-switch by publicly committing to create a number of jobs, and then privately walking back their commitments afterwards by amending their contracts. Amending firms would then have an incentive to keep their amendments private via challenging our records request, as a public release could hurt the firms' reputations. Unlike amendments, which are private, grant repayment via clawbacks is a public signal that a firm has dialed back (or fully withdrawn from) its job-creation commitment. Firms who paid clawbacks have less incentive to block our records request since a public record of their grant nonperformance already exists.

To explore the plausibility of this explanation, in this section we analyze the content of the 48 amended contracts that we were able to access via our public records request. While we do have the complete list of TEF firms who have amended their grant contracts, we do not have the complete set of all 56 amendment documents themselves; some firms were successful in blocking our document requests via legal challenge, while other missing documents may not have been included due to human error or lack of records.<sup>19</sup> However, we do have over 85% of the amendment documents, and the broad variation in the industry and size of the firms whose documents we have received provides reassurance that our sample is representative of all amendments.

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<sup>18</sup> To be clear, this analysis is exploratory and not confirmatory.

<sup>19</sup> Because they were not available at the time of our original public records request, we restrict our analysis to the 56 amendments signed prior to 2018. Information on the amendments that we did not receive can be found in Appendix B.

**Figure 1: TEF agreement amendments by type, challenger status, and clawback payment status**

Amendment Type	Challenged Records Request?	
	No	Yes
Technical	Hanger, Cerealto Seguin <b>HelioVolt Corp.</b> , Grifols, <b>Rockwell Collins</b> , LiveOps <b>Flexsteel</b> , Tenaris	Dow Chemical (2012), Dow Chemical (2013)
Job Target	<b>Ferris Mfg.</b> , <b>KLN Steel Products</b> <b>Grifols</b> , <b>GE Transportation</b> , <b>Huntsman</b> , <b>Fidelity</b> , Rackspace, <b>Rockwell Collins</b> , Tenaris	<b>Lockheed Martin</b> , <b>SpaceX</b> ,
Job Schedule	Continental, <b>Martifer-Hirschfield</b> <b>athenahealth</b> , <b>Authentix</b> , <b>Forum Production</b> , <b>KLN Steel</b> <b>Huntsman</b> , <b>Fidelity</b> , Oracle Rackspace, <b>Santana Textiles</b> , Tenaris, Motiva	Zah Group
Expand Position Def.	Hanger, <b>CGI Technologies</b> , Forcepoint, <b>Flexsteel</b> , <b>GE Transportation</b> , <b>Fidelity</b> <b>Caterpillar</b> , Motiva	Comerica, Zah Group, <b>Consolidated Electrical Distributors</b> , Health Management Systems, Charles Schwab & Co., <b>Allstate Insurance</b> , <b>Golden Living</b>

Note: Bold text indicates that the firm repaid part or all of the grant award via clawbacks.

To reiterate, the “bait-and-switch” explanation requires that firms are using amendments to make changes to their original contracts that they want to keep hidden from the public. We argue that the content of the amendment documents supports this interpretation; the majority of the amendments serve to reduce or delay the job creation requirements that firms committed to under the terms of their original grant contracts. We identify four non-mutually exclusive categories of amendment, and discuss each in turn.

The four primary types of amendment are: (1) technical changes, which cover issues unrelated to contract performance (change in firm name, etc); (2) changes in job-creation schedule, meaning an extension to the deadline upon which a firm is required to have fulfilled its job target; (3) changes to a job target, meaning a reduction in the total number of jobs the firm is required to create; and (4) broadening of the contractual definition of a “created position,” which typically

means that the firm becomes able to include jobs created at non-project subsidiaries and affiliates towards its job obligations.

Figure 1 presents three pieces of information about each of the amendments to which we have access. First, each row represents one of the four amendment categories identified earlier.<sup>20</sup> The amendments are evenly spread between the four categories, though technical amendments were least common and job definition expansion amendments were most common. Second, each column indicates whether or not the firm challenged our records request. Note that the proportion of challengers is highest for the job definition expansion category, and lowest for the job schedule and job target amendments. Third, bolded text indicates that the firm publicly repaid its grant contract in part or in full through the clawback mechanism. Note that, among amending firms, the proportion of non-challengers who paid clawbacks is greater than the proportion of challengers who paid clawbacks. We discuss the significance of this fact in greater detail later on.

Of the four primary amendment types, technical change amendments result in the least substantive alternation to the original contract. For example, in 2016 food manufacturer Cerealto amended its 2014 agreement contract to reflect its name change from Siro Group USA to Cerealto Group USA. This simply changes the name on the contracts but doesn't result in any other substantive changes. Since the majority of these amendments do not reduce the amending firm's job creation commitments, it is unsurprising that we see few challenges from firms in this category; while still private, these amendments do not contain information that would damage the firm's reputation if made public.

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<sup>20</sup> Some firms combine multiple amendment types into one amendment document; for example, Zah Group amended its 2010 agreement to both delay its job schedule by one year and to allow positions created with its affiliate (Klein Tools) to count towards its job target. For this reason, some firms appear in the table multiple times.

Dow Chemical is the exception, as it has made technical amendments on two separate contracts and challenged our records request. However, unlike the other technical amendments, Dow's amendments lowered its job "threshold" (the number of pre-agreement employment positions that the firm maintains in Texas) to reflect the firm's decision to transfer a number of its employees to a non-Dow company. Changing the job threshold does not change the job target, job schedule, or definition of a created employment position. However, the amendment documents reveal that Dow is actually transferring a larger number of jobs out of the company than the number of new jobs that it has promised to create under the grant agreement; this is information that Dow would likely prefer to keep hidden from the citizens whose taxes funded the grant. Dow's amendments, which allowed the firm to privately move jobs out of Texas while its commitment to create new jobs remained public, are consistent with the bait-and-switch explanation.

The second TEF amendment category involves reductions of the job target, the total number of jobs that the firm has committed to create. These amendments arguably result in the largest changes to the original agreement, as they directly reduce the size of the primary deliverable that the firm is required to produce in return for its grant funding. However, the changes are not one-sided; amendments to the total job creation requirement are paired with amendments to the size of the TEF grant. For example, in 2008 Lockheed Martin amended its 2007 agreement to reduce its job target from 800 to 550 new employment positions, a reduction of 31%. The amendment also reduced the size of the grant from \$5.48M to \$4M, a reduction of nearly equal scope (~30%).

The third major amendment type involves changes to the job schedule. This allows firms to alter their yearly job creation targets, or to push back their final deadline. For example, Martifer-Hirschfield Energy's 2009 amendment to its 2008 agreement pushed back its job target of 10 new jobs to April 2009. The Martifer-Hirschfield amendment is notable because it was signed on January 31<sup>st</sup>, 2009, the same day that its first annual compliance verification (a report on the number and

type of newly created positions) was due. Continental Automotive's 2013 amendment to its 2012 agreement left the original annual job targets unchanged, but shifted each of them two years into the future, changing the job creation deadline from December 2016 to December 2018. Job schedule amendments thus allow firms to fine-tune their plans for job creation (as in the case of Martifer-Hirschfield) or make larger changes to the project completion date (as in the case of Continental).

As Figure 1 shows, only two of the eleven firms that amended their job target also challenged our records request, and only one out of the thirteen firms that amended their job schedule challenged our request. At first, this may seem to be inconsistent with the bait-and-switch explanation – shouldn't the firms who most directly reduced or delayed their job creation commitments have the greatest incentive to keep this information private? It is important to note that amendments and clawbacks are not mutually exclusive. Many companies, most likely struggling to comply with the agreement, first renegotiate their contracts. Some of these companies, such as SpaceX, fail to deliver promised jobs even after the amendment and are subject to a clawback.

Our case studies reveal that firms who directly reduced or delayed their job creation requirements were also the most likely to repay part of their grant award; nine out of the eleven firms who amended their job target paid clawbacks, and eight of the thirteen firms who amended their job schedule paid clawbacks. Recall that clawbacks, unlike amendments, are made public on the Office of the Governor's website. Since the majority of firms in the job target/job schedule amendment categories have already had their grant reduction made public, they have less incentive to keep the details of the grant reduction private by challenging our records request.

Among the 48 amendment documents to which we have access, the most common amendment type is the expansion of the contractual definition of a created job. These amendments allow firms to utilize their subsidiaries and affiliates towards their total job target, effectively treating indirect job creation (for example, new positions created by an affiliated transportation company as a

result of increased output from the new production facility) as equivalent to direct job creation (workers hired for the specific purpose of operating the facility for which the firm received the TEF grant) for their development project.

As an example, in 2007 Comerica received a \$3.5 Million TEF grant to relocate their corporate headquarters to Dallas in order to create 200 jobs. In 2012, Comerica negotiated an amendment to its original agreement that expanded the range of jobs that could be counted towards its original job creation target. First, the amendment allowed jobs created with subsidiaries, Comerica Bank and Comerica Management Company, to count towards its job target. Second, the amendment allowed Comerica to count fifteen of its executive officers (including the CEO) as newly created jobs provided that they relocated to Dallas or Houston. As an added benefit, executive officers would clearly have an impact on the average wages of the new employees, making it easier to meet wage requirements.

Amendments that expand the definition of a created job alter the agreement more substantively than technical agreements, but they do so less directly than reductions to the job target or delays of the job creation deadline. This may explain the fact that, as Figure 1 shows, firms with amendments in this category were most likely to challenge our request. Allowing jobs created with non-project affiliates and subsidiaries not only makes the job target easier to meet, but also changes the composition of the created jobs from what was originally promised; unlike technical amendments, firms certainly want to keep these amendments private. However, unlike direct reductions to the target or changes to the deadline, firms making these amendments were less likely to need to repay part of their grant through the clawback mechanism. Note that of the seven firms in this amendment category who challenged our request, only three paid clawbacks. This finding is well-explained by the bait-and-switch logic. Firms who expanded the definition of a created job privately rolled back their original commitments; unlike the other amendment types, many of these



amendments were not publicized via the payment of clawbacks; a relatively large proportion of these firms challenged our records request.

In summary, these amendments suggest that firms have been able to renegotiate their TEF agreements in ways that are consistent with the “bait-and-switch” logic. Amending firms publicly commit to create a certain number of jobs in a certain time frame, and then privately dial back these commitments via amendment; amending firms who paid clawbacks were less likely to challenge our records request, as clawback payment already serves as a public signal that the firm’s original bargain has changed.

As we noted previously, Texas isn’t the only state to technically allow for amendments in their contracts. Major incentive programs in California and Michigan both list amendments to their incentive offers. The Michigan Economic Development Corporation (2018) provides a summary of its amendments for fiscal year 2017 in its annual report. These amendments look similar to Texas with a large number of companies making amendments to their contracts.<sup>21</sup> This includes changing the definition of a job (Hanson Solutions LLC, OPS Solutions LLC, ), delaying their job creation deadlines (Cosworth LLC, Pro Services, Suvina LLC) and in some cases fully reducing the number of jobs required (Flow-Rite, Micro Industries). Many firms included more than one change in their amendments (Bowers Manufacturing Company, Carhartt Inc). Thus, we contend that this process of amendments occurs in other states and our research design provides a generalizable finding on the firm preferences on the disclosure of this information.

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<sup>21</sup> The state lists a total of 39 amendments in fiscal year 2017. During this same period, 107 new incentive approvals were made. Unlike Texas, some of these firms include amendments to their local incentive requirement in the state amendments.

## 6. Conclusion

In this project we harness firm legal challenges to public records requests as data. Our project examines firm performance in conjunction with receiving incentives from the flagship Texas economic development fund, the Texas Enterprise Fund (TEF). The program provides cash grants to firms in exchange for meeting job creation targets that include both the quantity of jobs and the average wages of these jobs.

In our request for the original applications and the formal agreements, firms used an economic development exception in Texas public records laws to formally challenge our request in 45 out of the 164 total contracts. In our statistical analysis we show that the firms that were most likely to challenge our requests were firms that amended their contracts in methods that are consistent with lowering standards to avoid formal non-compliance with the program.

Our select case studies illustrate the various types of amendments, but the most common amendment lessens the burdens for job creation through changing the number of jobs required, allowing firms to include employees not originally part of the agreement, or lengthening the amount of time companies have to create promised jobs.

We believe this paper has two important implications for economic development. First, numerous amended contracts suggest the ineffectiveness of formal clawback mechanisms if they are not coupled with strong transparency provisions. Allowing companies to renegotiate contracts outside of the public eye violates the very spirit of adding performance requirements and performance provisions. Second, we provide evidence consistent with firms using exceptions to public records requests to hide non-compliance with economic development agreements. In short, the firms that are hiding their contracts seem to be doing so for serious reasons.

What remains unexplained is the ability of some firms to completely avoid public clawbacks while others firms pay penalties, often the complete Texas Enterprise Fund award plus interest. Our

own analysis of the amended contracts finds considerable variation in the renegotiated terms across firms, suggesting a variation in bargaining power between the firms and the state. Our conjecture is that traditional bargaining models of firm government relations (Kobrin 1987) explains the state's willingness to renegotiate contracts with an investor. This could range from employment in important areas of the state, the promise of additional investment in the future, or the political connections of the firm receiving incentives.

It is important to note that political factors could also shape the willingness of the Governor's office to provide more favorable terms to some investors. This could be due to strong relationships with firms through direct or indirect campaign contributions. Equally important, these investments are often touted as major "successes" at ribbon cutting ceremonies and are announced through formal press releases from the Governor's office. Some of these investments may be particularly high profile, and thus the perceived success is important to elected politicians. In future research we hope to further explore this amendment bargaining process.

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#### **Appendix A: Third Party Challenges**

According to the Attorney General of Texas letter OR2018-07128 the following third parties challenge the request:

ADP LLC  
Allstate Insurance Company  
Apple  
Arconic Inc f/k/a Aloca Inc  
BASF Corporation  
Charles Schwab and Co. Inc  
Chevron USA Inc  
CITGO Petroleum Corporation  
Comerica Incorporated and Comerica Bank  
Consolidated Electric Distributors Inc  
Cordish Companies and Arlington Live LLC  
Corrigan OSB LLC  
The Dow Chemical Company  
Ebay Inc and Subsidiaries  
Ernest and Young LLC  
Fred's Inc  
Fritz Industries  
GATX Corporation  
General Motors LLC  
GGNSC Holdings LLC  
Golden State Foods Corp  
Health Management System Inc  
Hefei Risever Machine Co. LTD  
Hulu LLC  
Impact Data Source LLC  
Jacob's Engineering Group, Inc  
JSW Steel Inc  
Klein Tools Inc and ZAH Group Inc  
Kubota Tractor Corporation  
Kuraray Americas Inc  
Lockheed Martin  
Louis Vuitton US Manufacturing  
Okidata Americas Inc  
OmniTracs LLC  
Pacific Dental Services LLC  
Payless ShoeSource Inc  
PepsiCo Inc  
Ruiz Food Products Inc  
Space Exploration Technologies Corp  
Thompson Reuters Inc  
Toyota Motor North America Inc  
United Services Automobile Association  
United States Bowling Congress  
Westlake Chemical  
Visa



**Appendix B: Existing pre-2018 amendment documents that we did not receive via records request, by challenge status.**

Challenged Records Request?	
Yes	No
ADP, Natgasoline, Triumph Aerostructures (x2)	Texas Energy Center(x2), Texas A&M U. System (w/Lexicon), Heliovolt (2nd amendment)