

Midland Development Corporation
A Component Unit of the City of Midland Texas

Independent Auditor's Report and Financial Statements

September 30, 2019

Midland Development Corporation
A Component Unit of the City of Midland, Texas
September 30, 2019

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Independent Auditor's Report

Board of Directors
The Midland Development Corporation
Midland, Texas

We have audited the accompanying financial statements of the governmental activities and the major fund of the Midland Development Corporation (MDC), a component unit of the City of Midland, Texas, as of and for the year ended September 30, 2019, and the related notes to the financial statements, which collectively comprise MDC's basic financial statements listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and the major fund of the Midland Development Corporation as of September 30, 2019, and the respective changes in financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison as listed in the table of contents be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

BKD, LLP

Dallas, Texas
March 31, 2020

Midland Development Corporation
A Component Unit of the City of Midland, Texas
Management's Discussion and Analysis (Unaudited)
Year Ended September 30, 2019

As management of the Midland Development Corporation (MDC), we offer readers of the MDC financial statements this narrative overview and analysis of the financial activities of the MDC for the fiscal year ended September 30, 2019.

Financial Highlights

The net position of the MDC was \$56.5 million at September 30, 2019, an increase of \$3.7 million from net position as of September 30, 2018 of \$52.8 million.

At September 30, 2019, amounts restricted for economic development incentives in the general fund increased from \$34.4 million at September 30, 2018 to \$37.6 million at September 30, 2019.

Overview of the Financial Statements

This discussion and analysis are intended to serve as an introduction to the MDC's basic financial statements. The MDC's basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the basic financial statements.

This report also contains required supplementary information in addition to the basic financial statements themselves.

Government-wide Financial Statements

The statement of net position presents information on all of the MDC's assets and liabilities, with the difference between the two reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the MDC is improving or deteriorating.

The statement of activities presents information showing how the government's net position changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows.

Thus, revenues and expenses are reported in this statement for some items that will result in cash flows in future fiscal periods.

Both of the government-wide financial statements display functions of the MDC that are principally supported by sales taxes. The governmental activities of the MDC include general government and economic development only.

Midland Development Corporation
A Component Unit of the City of Midland, Texas
Management's Discussion and Analysis (Unaudited)
Year Ended September 30, 2019

Fund Financial Statements

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The MDC, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The only fund of the MDC is a governmental fund.

Governmental Fund

A governmental fund is used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of a governmental fund is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balance provide a reconciliation to facilitate this comparison between the governmental fund and governmental activities.

The financial statements presented for the MDC are the same at the government-wide and fund levels, with the exception of compensated absences, capital lease obligations and capital assets, because the nature of the assets, liabilities, revenues, and expenses that were reported at the government-wide level were such that they also met the criteria for reporting at the fund level.

Notes to the Basic Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

Required Supplementary Information

In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information concerning the MDC's annual budget. The MDC adopts an annual appropriated budget for its general fund. A budgetary comparison schedule has been provided for the general fund to demonstrate compliance with this budget.

Midland Development Corporation
A Component Unit of the City of Midland, Texas
Management's Discussion and Analysis (Unaudited)
Year Ended September 30, 2019

Government-wide Financial Analysis

As noted earlier, net position may serve over time as a useful indicator of a government's financial position. At September 30, 2019, assets exceeded liabilities by \$56.5 million, an increase of \$3.7 million from the September 30, 2018 amount of \$52.8 million. Additionally, in fiscal year 2019, the MDC had a \$3.9 million increase in total assets.

MDC's Net Position

	Governmental Activities	
	2019	2018
Current and other assets	\$ 38,633,431	\$ 35,232,136
Capital assets	19,114,420	18,642,208
Total assets	<u>57,747,851</u>	<u>53,874,344</u>
Accounts and retainage payable	957,650	708,069
Noncurrent liabilities	289,657	320,982
Total liabilities	<u>1,247,307</u>	<u>1,029,051</u>
Net position		
Net investment in capital assets	18,847,719	18,305,924
Restricted for economic development incentives	<u>37,652,825</u>	<u>34,539,369</u>
Total net position	<u>\$ 56,500,544</u>	<u>\$ 52,845,293</u>

Midland Development Corporation
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Management's Discussion and Analysis (Unaudited)
Year Ended September 30, 2019

MDC's Changes in Net Position

	Governmental Activities	
	2019	2018
Revenues		
Program revenues		
Charges for services	\$ 990,627	\$ -
Operating grants and contributions	161,856	-
Capital grants	549,650	-
General revenues		
Sales taxes	15,078,495	13,353,167
Investment earnings	472,929	365,937
Gain on sale of capital assets	598,239	349,816
Miscellaneous	15,405	42,825
Total revenues	<u>17,867,201</u>	<u>14,111,745</u>
Expenses		
General government	1,620,787	2,366,188
Economic development	12,591,163	4,933,144
Total expenses	<u>14,211,950</u>	<u>7,299,332</u>
Increase (decrease) in net position	3,655,251	6,812,413
Net position – October 1	<u>52,845,293</u>	<u>46,032,880</u>
Net position – September 30	<u>\$ 56,500,544</u>	<u>\$ 52,845,293</u>

The MDC's general revenues for governmental activities provided \$16.2 million in fiscal year 2019 as compared to \$14.1 million in fiscal year 2018. This increase is primarily attributable to an increase in sales taxes resulting from an upturn in the local economy due to increased oil and gas activity. The revenues were used to pay for expenses associated with general government and economic development activities of \$14.2 million in fiscal year 2019, compared to \$7.3 million in fiscal year 2018. Governmental activities are not self-supporting and are paid for through general revenues.

The most significant expense items of the MDC governmental activities are those associated with economic development activities of \$12.6 million, during the year ended September 30, 2019. Economic development activities increased by \$7.7 million due to several specific projects either being completed or released in fiscal year 2019.

Midland Development Corporation
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Management's Discussion and Analysis (Unaudited)
Year Ended September 30, 2019

Financial Analysis of the Governmental Fund

As noted earlier, the MDC uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental Fund

The focus of the MDC's governmental fund is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the MDC's financing requirements. In particular, unassigned fund balance serves as a useful measure of a government's net resources available for spending at the end of the fiscal year.

The general fund is the chief operating fund and the only fund of the MDC. Total fund balance increased \$3.2 million from 2018 to 2019 primarily due to an increase in sales tax revenue and a decrease in capital outlay, which was offset by an increase in economic development activities. As a measure of the General Fund's liquidity, it may be useful to total fund balance to total fund expenditures. Total fund balance represents 218.2% of total general fund revenues. \$37.6 million of the fund balance is restricted for economic development.

General Fund Budgetary Highlights

Actual revenues for fiscal year 2019 exceeded the final budget amount by \$6.2 million. This is primarily due to sales taxes being \$4.1 million higher than budgeted. An upturn in the local economy occurred as a result of increased activity in the oil and gas industry which resulted in higher sales taxes.

Differences between the final budget and actual expenditures resulted in MDC expenditures being \$10.4 million under budget for fiscal year 2019. The major sources of this variance are direct business incentives provided by the MDC, which were under budget by \$10.6 million.

There were no budgetary adjustments during fiscal year 2019.

Midland Development Corporation
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Management’s Discussion and Analysis (Unaudited)
Year Ended September 30, 2019

Capital Assets

MDC’s investment in capital assets for its governmental type activities as of September 30, 2019 amounts to \$19.1 million (net of accumulated depreciation). This investment in capital assets includes land, buildings, improvements other than buildings, machinery and equipment, infrastructure, and construction in progress. Major additions to capital assets in fiscal year 2019 include various improvements and infrastructure.

	Governmental Activities	
	2019	2018
Land	\$ 4,919,828	\$ 5,041,701
Buildings	10,985,057	11,236,268
Improvements other than buildings	455,583	579,555
Machinery and equipment	132,013	100,786
Infrastructure	1,172,526	1,226,102
Construction in progress	1,449,413	457,796
Total capital assets, net	\$ 19,114,420	\$ 18,642,208

Debt

The MDC has a Commercial Hangar Lease Agreement with the City of Midland for economic development purposes and to provide aviation services as permitted within the agreement. This agreement qualifies as a capital lease for accounting purposes. More detailed information about the lease may be found in the notes to the basic financial statements under *Note 7*.

Economic Factors and Next Year’s Budgets and Rates

The budgetary process for fiscal year 2020 focused on the allocation of resources to economic development activities and contractual payments for administration of the MDC. The budget presented for all MDC operations for the 2019–2020 fiscal year totals \$27.8 million.

The fiscal year 2020 operating budget is supported by combined revenues of \$12.3 million. The major source of this revenue is sales taxes of \$12.0 million.

Sales tax receipts are driven by numerous economic conditions. Particularly influenced by oil and gas activity, sales tax increases began to flatten out for fiscal year 2019 due to decreased activity. For 2020, sales taxes were budgeted at \$12.0 million, \$1.0 million higher than budgeted in 2019 and \$3.1 million lower than fiscal year 2019 actual sales tax receipts due to volatility of oil and gas activity.

Midland Development Corporation
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Management's Discussion and Analysis (Unaudited)
Year Ended September 30, 2019

The expenditures budget for the General Fund of the MDC is \$27.8 million. The revenue budget for the 2019–2020 fiscal year is expected to fall short of expenditures by \$15.5 million.

Request for Information

This financial report is designed to provide a general overview of the MDC's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Finance Director, MDC, 300 N. Loraine, Midland, TX 79702-1152.

Midland Development Corporation
A Component Unit of the City of Midland, Texas

Statement of Net Position
September 30, 2019

Assets

Current Assets

Cash and cash equivalents	\$ 29,621,495
Sales tax receivable	2,486,351
Prepayments	107,133
Due from primary government	5,911,873
Notes receivable	506,579
Capital assets (net of accumulated depreciation)	<u>19,114,420</u>
Total assets	<u>\$ 57,747,851</u>

Liabilities and Net Position

Liabilities

Accounts payable	\$ 922,079
Retainage payable	35,571
Noncurrent liabilities	
Due within one year	104,283
Due in more than one year	<u>185,374</u>
Total liabilities	<u>1,247,307</u>

Net Position

Net investment in capital assets	18,847,719
Restricted for economic development	<u>37,652,825</u>
Total net position	<u>\$ 56,500,544</u>

Midland Development Corporation
A Component Unit of the City of Midland, Texas
Statement of Activities
Year Ended September 30, 2019

Functions/Programs	Expenses	Program Revenues		Net (Expense) Revenue and Changes in Net Assets Governmental Activities
		Charges for Services	Operating Grants and Contributions	
Governmental activities				
General government	\$ 1,620,787	\$ -	\$ 161,856	\$ -
Economic development	12,591,163	990,627	-	549,650
Total governmental activities	<u>14,211,950</u>	<u>990,627</u>	<u>161,856</u>	<u>549,650</u>
General revenues				
Sales taxes				15,078,495
Investment earnings				472,929
Gain on sale of capital assets				598,239
Miscellaneous				15,405
Total general revenues				<u>16,165,068</u>
Change in net position				<u>3,655,251</u>
Net position – beginning				<u>52,845,293</u>
Net position – ending				<u>\$ 56,500,544</u>

Midland Development Corporation
A Component Unit of the City of Midland, Texas

Balance Sheet – General Fund
September 30, 2019

Assets

Current Assets

Cash and cash equivalents	\$ 29,621,495
Sales tax receivable	2,486,351
Prepayments	107,133
Due from primary government	5,911,873
Notes receivable	<u>506,579</u>

Total assets \$ 38,633,431

Liabilities and Fund Balance

Liabilities

Accounts payable	\$ 922,079
Retainage payable	<u>35,571</u>

Total liabilities 957,650

Fund balance

Nonspendable	
Prepayments	107,133
Restricted	
Economic development	<u>37,568,648</u>
Total fund balance	<u>37,675,781</u>

Total liabilities and fund balance \$ 38,633,431

Midland Development Corporation
A Component Unit of the City of Midland, Texas
Reconciliation of the Balance Sheet to the Statement of Net Position
September 30, 2019

Reconciliation of Fund Balance of the Governmental Fund to
the Governmental Activities in the Statement of Net Position

Fund balance of governmental fund	\$ 37,675,781
Amounts reported for governmental activities in the statement of net position are different because	
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the fund.	19,114,420
Long-term liabilities, including capital lease obligations and compensated absences, are not due and payable in the current period and, therefore, are not reported in the fund.	<u>(289,657)</u>
Net position of governmental activities	<u>\$ 56,500,544</u>

Midland Development Corporation
A Component Unit of the City of Midland, Texas
Statement of Revenues, Expenditures and Changes in Fund Balances –
General Fund
Year Ended September 30, 2019

Revenues	
Sales taxes	\$ 15,078,495
Interest income	472,929
Rentals	990,627
Intergovernmental	161,856
Other	<u>565,055</u>
Total revenues	<u>17,268,962</u>
Expenditures	
General government	
Administration	1,130,676
Economic development	12,591,163
Capital outlay	1,038,322
Debt service	
Capital lease	63,899
Interest	<u>13,300</u>
Total expenditures	<u>14,837,360</u>
Excess of revenues over expenditures	2,431,602
Other Financing Sources	
Proceeds from sale of land	<u>720,112</u>
Net change in fund balance	3,151,714
Fund Balance, Beginning	<u>34,524,067</u>
Fund Balance, End	<u><u>\$ 37,675,781</u></u>

Midland Development Corporation
A Component Unit of the City of Midland, Texas
Reconciliation of the Statement of Revenues, Expenditures and
Changes in Fund Balance to the Statement of Activities
Year Ended September 30, 2019

Reconciliation of the Governmental Fund Statement of Revenues, Expenditures, and
Changes in Fund Balance to the Governmental Activities in the Statement of Activities

Net change in fund balance – governmental fund	\$ 3,151,714
Amounts reported for <i>governmental activities</i> in the the statement of activities are different because	
Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period.	594,085
Governmental funds do not report disposal of capital assets. However, disposal of capital assets are reported net of proceeds from disposition in the Statement of Activities.	(121,873)
The issuance of long-term debt (e.g. bonds, leases) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net position. This amount is the net effect of these differences in the treatment of long-term debt and related items.	63,899
Compensated absences expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in the governmental fund.	<u>(32,574)</u>
Change in net position of governmental activities	<u>\$ 3,655,251</u>

Midland Development Corporation
A Component Unit of the City of Midland, Texas
Notes to Financial Statements
September 30, 2019

Note 1: Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations and Reporting Entity

The Midland Development Corporation (MDC), a component unit of the City of Midland, Texas (the City), is a legally separate nonprofit corporation organized under the Texas Development Corporation Act of 1979, Article 5190.6 Vernon's Texas Revised Civil Statutes Annotated as amended and governed by Section 4A of the Act. The MDC was incorporated in February 2002. The purpose of the MDC is to:

1. Keep existing jobs in Midland;
2. Keep existing businesses in Midland;
3. Foster the expansion of businesses currently located in Midland;
4. Attract new industry and businesses to Midland;
5. Provide long-term employment opportunities for Midlanders;
6. Promote and develop industrial and manufacturing enterprises in order to eliminate unemployment and underemployment;
7. Promote and encourage employment and the public welfare of, for, and on behalf of the City;
8. Promote areas of the City with a large number of substandard, deteriorated, or deteriorating structures, which impairs the sound growth of the City or constitutes an economic and social liability;
9. Develop areas of the City that should be developed in order to meet the development objectives of the City; and
10. Consider the impact on any local business before providing an incentive to any corporation or entity. The financial reporting entity presented in the accompanying financial statements of the MDC includes the primary corporate entity, the Midland Development Corporation. The MDC has no component units.

The accounting policies of the MDC, as reflected in the accompanying financial statements, conform to U.S. generally accepted accounting principles for local government units as prescribed by the Governmental Accounting Standards Board (GASB), the accepted body for promulgating governmental accounting and reporting principles.

Midland Development Corporation A Component Unit of the City of Midland, Texas

Notes to Financial Statements

September 30, 2019

The entirety of the MDC Board is appointed by the City Council and the City can impose its will upon the MDC. Additionally, the City Council and the MDC Boards are not substantively the same and the MDC does not provide services entirely or almost entirely to the City. Therefore, MDC is a discretely presented component unit of the City. The MDC began operations on February 1, 2002.

Basic Financial Statements

The basic financial statements are presented at two basic levels:

1. The government-wide level, where all statements are prepared using the economic resources measurement focus and the accrual basis of accounting. These statements present all assets, liabilities, revenues, expenses and gains and losses of the MDC as governmental activities.
2. The fund level, where governmental fund statements are prepared using the current financial resources measurement focus and the modified accrual basis of accounting.

Government-wide and Fund Financial Statements

As previously discussed, the basic financial statements of the MDC are presented at two basic levels, the government-wide level and the fund level. These statements focus on the MDC as a whole at the government-wide level and on the major fund at the fund level. Government-wide financial statements (*i.e.*, the statement of net position and the statement of activities) report information on all activities of the MDC. There is no interfund activity in the MDC financial statements. Governmental activities, which are normally supported by taxes, are the only reported activities.

The government-wide statement of net position reports all financial and capital resources of the MDC and is presented in “assets less liabilities equals net position” format. Assets and liabilities are presented in relative order of liquidity with liabilities that have an average maturity of more than one year separated into the amount due within one year and the amount due in more than one year.

The government-wide statement of activities identifies the relative financial burden of each of the MDC’s functions on the taxpayers by identifying direct expenses and the extent of self-support through program revenues. Direct expenses are clearly identifiable expenses that can be specifically associated with a function. Program revenues are revenues derived directly from the function or other sources that reduce the net cost of the function to be financed from general government revenues. Program revenues are 1) charges to customers who purchase, use, or directly benefit from services provided by a function and which are generated by that function, 2) grants and contributions restricted to operating requirements of a function and, 3) grants and contributions restricted to capital requirements of a function. Items such as taxes, investment earnings, and nonspecific grants are not included as program revenues but are reported as general revenues that normally cover the net cost of a function.

Midland Development Corporation A Component Unit of the City of Midland, Texas

Notes to Financial Statements

September 30, 2019

Fund level financial statements are presented for the governmental fund, with a focus on the major fund. A major fund is a fund meeting certain specific asset, liability, revenue, or expenditure criteria relative to all funds of that type. The only major fund used by the MDC is the General Fund which is the only operating fund of the MDC. This fund accounts for the economic development activities of the MDC: collection of sales tax revenues and expenses associated with marketing and promotion of Midland.

Measurement Focus and Basis of Accounting

The government-wide statements are prepared using the economic resources measurement focus and the accrual basis of accounting. Revenues are recognized when earned and expenses are recognized when a liability is incurred, regardless of the timing of related cash flows.

Governmental fund financial statements are reported using a current financial resources measurement focus and modified accrual basis of accounting. Under the modified accrual basis of accounting, revenues are recognized when susceptible to accrual, *i.e.*, both measurable and available. “Measurable” means the amount of the transaction can be determined and “available” means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. In the case of sales taxes, available means due within the current period and collected within the current period or soon enough thereafter to be used to pay liabilities of the current period. Such time thereafter shall not exceed 60 days. Expenditures are generally recorded when a fund liability is incurred. Governmental fund revenues, which have been accrued based upon the susceptible to accrual concept, are sales taxes.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Equity in Cash and Investments

The City pools a portion of the resources of its various funds and component units, including MDC, to facilitate the management of cash and enhance investment earnings. Records are maintained that reflect each fund or component unit’s equity in the pooled investments.

Cash, Cash Equivalents and Investments

Cash and cash equivalents include any cash on hand, demand deposits, and any highly liquid investments that have an original maturity of three months or less from date of purchase. Investments in Texas Local Government Investment Pool (TexPool) and TexStar are considered cash equivalents as the amounts are available on demand. Investments, other than investments in TexPool and TexStar, are recorded at fair value based upon verifiable market prices.

Midland Development Corporation
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Notes to Financial Statements

September 30, 2019

Notes Receivable

MDC provides loans to new and expanding businesses that meet certain qualifications aligned with MDC's purpose. In some instances, the loans are given in the form of forgivable loans and are forgiven if all requirements are met.

Capital Assets

Capital assets are defined as a purchase or other acquisition of land, equipment, facilities, or other similar assets or the cost of construction of such asset the cost of which is in excess of \$5,000 and has a useful life of more than one year. These assets include property, plant, equipment, and all other tangible assets purchased or acquired. Purchased or constructed assets are carried at historical cost. Contributed assets are recorded at acquisition value at the time of donation.

Major outlays for capital assets and improvements are capitalized as capital projects are completed. Depreciable capital assets are depreciated using the straight line method over the following estimated useful lives:

<u>Asset Classification</u>	<u>Years</u>
Buildings	40
Improvements other than buildings	20
Machinery and equipment	6
Infrastructure	50

Compensated Absences

The MDC's employees earn paid time off, which may either be taken or accumulated, subject to a specified maximum, until paid upon retirement or termination. The MDC has accrued paid time off using the regular pay and termination pay rates in effect at the balance sheet date plus an additional amount for compensation-related payments based on the criteria set forth in GASB Statement No. 16. The liability has been accrued in the government-wide statements. A liability for those amounts is recorded in the governmental fund only if the liability has matured as a result of employee resignations or retirements.

Net Position

Net position of the MDC is classified in two components on its statements of net position.

- Net investment in capital assets consists of capital assets net of accumulated depreciation and reduced by the outstanding balances of borrowings used to finance the purchase or construction of those assets.
- Restricted net position is made up of noncapital assets that must be used for a particular purpose, as specified by creditors, grantors or donors external to the MDC.

Midland Development Corporation A Component Unit of the City of Midland, Texas

Notes to Financial Statements

September 30, 2019

Nature and Purpose of Classifications of Fund Balances

Governmental funds fund balances classified as restricted can only be used for specific purposes pursuant to constraints imposed by state law for Type A development corporations. Fund balances classified as nonspendable include amounts that cannot be spent because they are not in a spendable form.

Net Position/Fund Balance Flow Assumption

It is the MDC's policy to consider restricted net position/fund balances to have been depleted before unrestricted net position/fund balances is applied.

Note 2: Deposits, Investments and Investment Income

Custodial MDC deposits, which are combined with the City's deposits, were fully insured or collateralized as of September 30, 2019. The bank balance of the City was covered by sufficient collateral at September 30, 2019, held in the City's name by the Federal Reserve Bank of Minneapolis as agent for the City.

The MDC's investment policies are governed by State statutes. The MDC is governed by the City's investment policies which further limit State statutes such that eligible investments include the following:

Obligations of the United States or its Agencies and Instrumentalities

1. United States of America Treasury securities
2. Farmers Home Administration (FmHA) obligations backed by the full faith and credit of the United States
3. Federal Home Loan Bank (FHLBs) bonds
4. Federal National Mortgage Association (Fannie Mae or FNMA) notes and debentures
5. Farm Credit System Obligations
6. Federal Home Loan Mortgage Corporation (Freddie Mac or FHLMC) obligations, *i.e.*, discount notes or debentures.

Direct Obligations of the State of Texas or its Agencies

Texas State, City, County, or School District General Obligation Bonds with a remaining maturity of 10 years or less having been rated as to investment quality by Moody's or Standard and Poor's (nationally recognized investment rating firms) and having received a rating of no less than "A" or its equivalent.

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Certificates of Deposit Issued by State and National Banks Domiciled in this State

Certificates of deposit issued by state and national banks domiciled in this state that are: (1) guaranteed or insured by the Federal Deposit Insurance Corporation, or its successor; or (2) secured by obligations that are described in V.T.C.A., Local Government Code Sections 105.001 et seq.

Fully Collateralized Repurchase Agreements having a Defined Termination Date

Fully collateralized direct repurchase agreements and reverse repurchase agreements with a defined termination date of no more than 90 days from the date such investment is purchased, secured by obligations of the United States or its agencies and instrumentalities with a market value of not less than the amount of the funds disbursed and held by a custodian for the MDC.

Repurchase agreements must be purchased through a primary government securities dealer, as defined by the Federal Reserve, or a bank domiciled in Texas. Money received under the terms of a reverse repurchase agreement shall be used to acquire additional eligible investments whose maturity does not exceed the expiration date of the reverse repurchase agreement.

Money Market Funds

Money market funds fully authorized by State statute of both public and private sponsorship.

Other Securities or Obligations Approved by the City Council

Other such securities or obligations as authorized by State statute and approved by the City Council.

Deposits and Investments

The MDC invests in two governmental pools: TexPool and TexStar, both of which were created under the Interlocal Cooperation Act, Texas Government Code Ann. Ch. 791 and the Texas Government Code Ann. Ch. 2256.

The Texas Treasury Safekeeping Trust Company is trustee of TexPool and is a limited purpose trust company authorized pursuant to Texas Government Code Ann. Section 404.103 for which the Texas State Comptroller is the sole officer, director, and shareholder. The advisory board of TexPool is composed of members appointed pursuant to the requirements of the Public Funds Investment Act, Texas Government Code Ann. Ch. 2256. TexStar is governed by a five-member Board of Directors comprising three government officials or employees and two other persons with expertise in public finance. Additionally, TexStar has a five-member advisory board. Both TexPool and TexStar are rated AAAM by Standard & Poor's.

Certain external investment pools and pool participants have an option to measure these investment pools at amortized cost rather than fair value if certain criteria are met. TexPool has opted to report at amortized cost, while TexStar measures their investments at net asset value (NAV).

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Investment income earned on pooled cash and investments is allocated to each fund based upon each fund's weighted average daily cash and investment balances.

Investments other than investments in TexPool and TexStar are valued based upon quotes obtained from Interactive Data Pricing and Reference Data (IDC). As of September 30, 2019, MDC had no investments other than TexPool and TexStar.

Interest Rate Risk

As a means of limiting its exposure to fair value losses arising from rising interest rates, the City's investment policy limits final stated maturities to ten years maximum with no more than 30% exceeding seven years and dollar weighted average portfolio maturity not to exceed five years in the investments listed above. The investment pools are presented as an investment with a maturity of less than one year because the average maturity of the pools is less than one year.

Note 3: Receivables

The Receivables as of September 30, 2019, for the MDC include sales tax receivables of \$2,486,351 due from the State of Texas.

MDC provides funds to the primary government and to other entities in which requirements, contained within agreements between the MDC and recipients, are to be met or funds are required to be returned to the MDC. Receivables are recorded until requirements are met. At the time requirements are met, MDC reduces its receivables and recognizes economic development expenses. The MDC also has \$5,911,873 due from the City of Midland, which is part of an economic development agreement for street improvements. Additionally, notes receivable of \$506,579 are economic development agreements with two external entities.

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Note 4: Capital Assets

Capital assets activity for the year ended September 30, 2019:

	Beginning Balance	Additions	Retirements	Transfers/ Adjustments	Ending Balance
Governmental activities					
Capital assets, not being depreciated					
Land	\$ 5,041,701	\$ -	\$ (121,873)	\$ -	\$ 4,919,828
Construction in progress	457,796	991,617	-	-	1,449,413
Total capital assets, not being depreciated	<u>5,499,497</u>	<u>991,617</u>	<u>(121,873)</u>	<u>-</u>	<u>6,369,241</u>
Capital assets, being depreciated					
Buildings	11,972,820	-	-	103,231	12,076,051
Improvements other than buildings	716,709	-	-	(103,231)	613,478
Machinery and equipment	115,875	46,706	-	-	162,581
Infrastructure	1,362,237	-	-	-	1,362,237
Total capital assets, being depreciated	<u>14,167,641</u>	<u>46,706</u>	<u>-</u>	<u>-</u>	<u>14,214,347</u>
Less accumulated depreciation for					
Buildings	(736,552)	(354,442)	-	-	(1,090,994)
Improvements other than buildings	(137,154)	(20,741)	-	-	(157,895)
Machinery and equipment	(15,089)	(15,479)	-	-	(30,568)
Infrastructure	(136,135)	(53,576)	-	-	(189,711)
Total accumulated depreciation	<u>(1,024,930)</u>	<u>(444,238)</u>	<u>-</u>	<u>-</u>	<u>(1,469,168)</u>
Total capital assets, being depreciated, net	<u>13,142,711</u>	<u>(397,532)</u>	<u>-</u>	<u>-</u>	<u>12,745,179</u>
Governmental activities capital assets, net	<u>\$ 18,642,208</u>	<u>\$ 594,085</u>	<u>\$ (121,873)</u>	<u>\$ -</u>	<u>\$ 19,114,420</u>

Note 5: Employee Benefit Plan

The MDC participates in a multiple-employer defined contribution salary deferral plan created in accordance with Internal Revenue Code Section 401(k). The plan is administered by the American Chamber of Commerce Executives Profit Sharing Plan. Active participants must be at least 21 years of age with a minimum of one year of eligibility service. The MDC contributes 9% of each eligible employee's total annual compensation to the plan. Employees may also make elective deferral contributions up to specified limits of their total compensation each year. The MDC will match those contributions up to a maximum of 3% of each participant's total annual compensation. The MDC contributed a total of \$42,099 to the plan during fiscal year 2019.

Employees are immediately vested in their own contributions and earnings on those contributions and become vested in MDC contributions at 25% after one year of eligible service, 50% after two years, 75% after three years and 100% after four years of eligible. Nonvested MDC contributions are forfeited upon termination of employment. Such forfeitures are used to cover a portion of the pension plan's administrative expenses. There were no forfeitures during 2019.

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Notes to Financial Statements
September 30, 2019

Note 6: Long-term Obligations

The following is a summary of long-term obligation transactions for the MDC for the year ended September 30, 2019:

	<u>Beginning Balance</u>	<u>Additions/ Completions</u>	<u>Retirements/ Adjustments</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Governmental activities					
Compensated absences	\$ 25,953	\$ 65,743	\$ (33,169)	\$ 58,527	\$ 40,384
Capital lease	295,029	-	(63,899)	231,130	63,899
Governmental activities long-term liabilities	<u>\$ 320,982</u>	<u>\$ 65,743</u>	<u>\$ (97,068)</u>	<u>\$ 289,657</u>	<u>\$ 104,283</u>

Note 7: Capital Lease Liabilities

The MDC has a Commercial Hangar Lease Agreement with the City of Midland for economic development purposes and to provide aviation services as permitted within the agreement. This agreement qualifies as a capital lease for accounting purposes. A portion of the leased space is subleased under a lease expiring over the next 15 years. Per the terms of sublease agreement, MDC will rebate a portion of the sublessee's rent for the first five years of the lease if they meet certain conditions related to economic development. For the year ended September 30, 2019, \$837,283 was rebated.

A summary of assets acquired through capital lease is as follows:

Buildings	\$ 429,994
Less: Accumulated depreciation	<u>(266,319)</u>
	<u>\$ 163,675</u>

Future minimum lease obligations and the net present value of these payments as of September 30, 2019, were as follows:

<u>Fiscal Year Ending September 30:</u>	
2020	\$ 77,199
2021	77,199
2022	77,199
2023	<u>19,300</u>
Total minimum lease payments	250,897
Less interest at 5.00%	<u>(19,767)</u>
	<u>\$ 231,130</u>

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September 30, 2019

Minimum future rentals receivable under operating subleases at September 30, 2019, were as follows:

<u>Fiscal Year Ending September 30:</u>	
2020	\$ 976,644
2021	976,644
2022	976,644
2023	976,644
2024	976,644
2025-2029	4,883,220
2030-2034	<u>3,092,706</u>
	<u>\$12,859,146</u>

Note 8: Risk Management

The MDC is exposed to various risks of loss related to torts. For the purposes of the Texas Tort Claims Act (Subchapter A, Chapter 101, Texas Civil Practices and Remedies Code), the MDC is a governmental unit and its actions are governmental functions and, therefore, are limited by governmental immunity. As of September 30, 2019, there were no claims outstanding. There has been no significant reduction in coverage from 2018 to 2019; nor have settlement amounts exceeded coverage for each of the past three years.

Note 9: Commitments and Contingencies

Litigation

No legal action arose in the ordinary course of the MDC's business during the fiscal year ended September 30, 2019.

Commitments

At September 30, 2019, the MDC had contracts for economic development commitments of \$38,250,215.

Midland Development Corporation

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Notes to Financial Statements

September 30, 2019

Note 10: Related Party Transactions

A majority of the MDC and the Midland Spaceport Development Corporation (Spaceport) boards are appointed by the City and the City can impose its will upon MDC and Spaceport. Accordingly, both MDC and Spaceport are discretely presented component units of the City.

During 2019, the Spaceport repaid the \$698,107 interest-free loan to MDC. The MDC did not make any contributions to Spaceport during fiscal year 2019. However, the Spaceport made capital contributions to MDC of \$549,650 during fiscal year 2019 for the purpose of constructing capital assets. The capital assets constructed by MDC will be transferred to Spaceport upon completion.

Note 11: Subsequent Events

The current economic decline currently presents difficult circumstances and challenges for the energy industry, which is a key player in the local economy. Future changes caused by the current economic environment and the resulting impact on the MDC's financial statements are uncertain at this time but could be significant.

As a result of the spread of the COVID-19 coronavirus, economic uncertainties have arisen which may negatively affect the financial position, results of operations and cash flows of the MDC. The duration of these uncertainties and the ultimate financial effects cannot be reasonably estimated at this time.

Note 12: Future Change in Accounting Principle

The Governmental Accounting Standards Board issued its Statement No. 84 (GASB 84), *Fiduciary Activities*. The objective of this Statement is to improve guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported. GASB 84 establishes criteria for identifying fiduciary activities of all state and local governments. The focus of the criteria generally is on (1) whether a government is controlling the assets of the fiduciary activity and (2) the beneficiaries with whom a fiduciary relationship exists. Separate criteria are included to identify fiduciary component units and postemployment benefit arrangements that are fiduciary activities. The MDC expects to first apply GASB 84 during the year ending September 30, 2020, using a prospective recognition method. The impact of applying the Statement has not been determined.

The Governmental Accounting Standards Board also issued its Statement No. 87 (GASB 87), *Leases*. This new Statement establishes a single model for lease accounting based on the principle that leases represent the financing of the right to use an underlying asset. GASB 87 includes the accounting guidance for both lessees and lessors. The MDC expects to first apply GASB 87 during the year ending September 30, 2021, using the facts and circumstances in place at the time of adoption, rather than retroactive to the time each lease was begun. The impact of applying the Statement has not been determined.

Required Supplementary Information

Midland Development Corporation
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Schedule of Revenues, Expenditures, and Changes in Fund Balance –
Budget and Actual – General Fund
Year Ended September 30, 2019

	Original / Final Budget	Actual	Variance – Favorable (Unfavorable)
Revenues			
Sales taxes	\$ 11,000,000	\$ 15,078,495	\$ 4,078,495
Interest income	100,000	472,929	372,929
Rentals	-	990,627	990,627
Intergovernmental	-	161,856	161,856
Other	-	565,055	565,055
Total revenues	<u>11,100,000</u>	<u>17,268,962</u>	<u>6,168,962</u>
Expenditures			
Administration	2,001,995	1,130,676	871,319
Economic development	23,142,005	12,591,163	10,550,842
Capital outlay	61,000	1,038,322	(977,322)
Debt Service	72,000	77,199	(5,199)
Total expenditures	<u>25,277,000</u>	<u>14,837,360</u>	<u>10,439,640</u>
Excess of revenues (deficiencies) over (under) expenditures	<u>(14,177,000)</u>	<u>2,431,602</u>	<u>16,608,602</u>
Other financing sources			
Sale of capital assets	-	720,112	720,112
Total other financing sources	<u>-</u>	<u>720,112</u>	<u>720,112</u>
Net change in fund balance	(14,177,000)	3,151,714	17,328,714
Fund Balance, Beginning	<u>34,524,067</u>	<u>34,524,067</u>	<u>-</u>
Fund Balance, Ending	<u>\$ 20,347,067</u>	<u>\$ 37,675,781</u>	<u>\$ 17,328,714</u>

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Notes to Schedule of Revenues, Expenditures, and Changes in Fund Balance –
Budget and Actual – General Fund
Year Ended September 30, 2019

Notes to Schedule:

The annual budget is legally adopted by the MDC Board and approved by the City Council of the City of Midland (City) on a basis consistent with U.S. generally accepted accounting principles.

The MDC Board follows these procedures in establishing the budget reflected for the MDC:

1. At least sixty (60) days prior to October 1 of each year, the MDC Board, with the assistance of the MDC Treasurer, prepares and adopts a proposed budget for the fiscal year beginning on the following October 1. The operating budget includes proposed expenditures and other such budgetary information as required by the City Council for approval and adoption.
2. The proposed budget is then submitted to the City Council for approval and is considered adopted upon formal approval by the City Council.
3. Expenditures may not exceed the appropriation for the adopted annual operating budget.
4. Supplemental appropriations during the year must be approved and adopted by the MDC Board and the City Council through passage of resolution.