HOUSE COMMITTEE ON URBAN AFFAIRS
TEXAS HOUSE OF REPRESENTATIVES
INTERIM REPORT 2004

A REPORT TO THE
HOUSE OF REPRESENTATIVES
79TH TEXAS LEGISLATURE

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Committee On
Urban Affairs

December 29, 2004

Robert Talton
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P.O. Box 2910
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The Honorable Tom Craddick
Speaker, Texas House of Representatives
Members of the Texas House of Representatives
Texas State Capitol, Rm. 2W.13
Austin, Texas 78701

Dear Mr. Speaker and Fellow Members:

The Committee on Urban Affairs of the Seventy-Eighth Legislature hereby submits its interim report including recommendations for consideration by the Seventy-ninth Legislature.

Respectfully submitted,

Robert Talton, Chairman

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Bob Hunter

Jose Menendez

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INTRODUCTION

At the beginning of the 78th Texas Legislative Session, the Honorable Tom Craddick, Speaker of the House of Representatives, appointed seven members to the Committee on Urban Affairs. The Committee membership was as follows: Representative Robert Talton, Chairman; Representative Corbin Van Arsdale, Vice-Chairman; and Representatives: Kevin Bailey, Al Edwards, Bob Hunter, Jose Menendez, and Martha Wong.

The Committee requested and was charged with studying and reporting on five matters to the 79th Legislature by Speaker Craddick. These charges were (1) Review the roles of special purpose districts; including justification, powers and responsibilities, as well as relationships with local elected governing bodies. Specifically, include an analysis of the use, benefits and drawbacks of tax increment reinvestment zones; (2) Actively monitor the implementation of SB 264, 78th Legislature, sunset legislation for the Texas Department of Housing and Community Affairs. Include an analysis of whether further reforms are needed through a review of best-practices in other states; (3) Evaluate the effectiveness of current programs in meeting the state's housing needs and examine new alternatives such as urban land banks, homestead preservation districts and programs to provide gap financing; (4) Evaluate the effectiveness of Uniform State Regions in allocation of Home Investment Partnership Program (HOME) funds and low-income tax credits to develop housing and examine alternatives to meet the needs of the state's rural areas; and (5) Monitor the agencies and programs under the committee's jurisdiction.

On March 24, 2004 the Committee held a joint committee session with the Senate Committee on Intergovernmental Relations and held three regular public hearings on May 13, 2004, May 20, 2004, and July 16, 2004.

The Committee wishes to express its appreciation to the citizens, organizations and agencies that testified before the Committee.

HOUSE COMMITTEE ON URBAN AFFAIRS

INTERIM STUDY CHARGES

CHARGE Review the roles of special purpose districts; including justification, powers and responsibilities, as well as relationships with local elected governing bodies. Specifically, include an analysis of the use, benefits and drawbacks of tax increment reinvestment zones.

CHARGE Actively monitor the implementation of SB 264, 78th Legislature, sunset legislation for the Texas Department of Housing and Community Affairs. Include an analysis of whether further reforms are needed through a review of best-practices in other states.

CHARGE Evaluate the effectiveness of current programs in meeting the state's housing needs and examine new alternatives such as urban land banks, homestead preservation districts and programs to provide gap financing.

CHARGE Evaluate the effectiveness of Uniform State Regions in allocation of Home Investment Partnership Program (HOME) funds and low-income tax credits to develop housing and examine alternatives to meet the needs of the state's rural areas.

CHARGE ONE

Review the roles of special purpose districts; including justification, powers and responsibilities, as well as relationships with local elected governing bodies. Specifically, include an analysis of the use, benefits and drawbacks of tax increment reinvestment zones.

BACKGROUND AND OVERVIEW

Special districts are political subdivisions of the State that are authorized to provide public services to specific populations or areas. While they are governmental bodies and are subject to the same laws that govern and regulate counties and municipalities, including open meetings and open records laws, they are always limited to the specific powers granted to them by the Texas Constitution and applicable statutes.

The initial authorization for creation of special districts in the Texas Constitution was added in 1904, followed by a second amendment in 1917. The Texas Constitution thus allowed special taxing districts to build water, wastewater, drainage, and road improvements, and to issue debt to finance these projects. In 1987, the Texas Constitution was amended to authorize loans and grants of public money to be used for economic development purposes. Special districts in Texas today are formed for a variety of purposes, including to build libraries, to fight mosquitoes, and to provide potable water and central wastewater systems throughout the State.

After having received a large volume of bills during the 78th regular session establishing and modifying municipal management districts (MMDs), the Committee chose to educate itself on the numerous powers and responsibilities of these special districts. In addition to this study, the Committee also chose to focus its attention on the use of tax increment reinvestment zones (TIRZs), a municipal tool often used in conjunction with MMDs.

Testimony was received from numerous MMDs operating in Houston, and from consultants from the legal and urban planning communities who work with the boards and managers of the MMDs. In addition, the Report of the Senate Intergovernmental Relations Committee on special districts completed in October, 2002, was studied, and that Committee's staff was consulted.

The Committee found a need for slight changes to the laws associated with MMDs, which will be the primary focus of this report, but it also became convinced of the usefulness of these districts to urban areas whose populations have become increasingly demanding even as municipal and county resources have become more strained and limited. It is important for readers of this report to recognize that the intent of the Committee is to propose changes that continue to encourage the establishment and development of MMDs and TIRZs in those communities where local leaders believe these financial tools to be useful, feasible and necessary.

Municipal Management Districts

MMDs are governed by Chapter 375, Local Government Code. The law allows MMDs to engage in enhancing security and public safety; alleviating traffic congestion and providing greater mobility; beautification programs, including graffiti abatement; street cleaning and garbage pickup; maintaining unique landscaping, street signs and public art; enhancing parks, greenbelts, and other recreational facilities; and launching economic development programs to recruit and retain business in the district.

A MMD is typically authorized to impose ad valorem property taxes or assessments, as well as impact fees, and to issue bonds. A MMD also may annex land, authorized by Chapter 54, Water Code.

The issuance of any bonds by a MMD must be approved by the Texas Attorney General. In addition, a MMD must obtain approval of the improvement project by the governing body of the municipality in which the district is located.

MMDs are generally authorized to serve as an auxiliary source of public funding to a specific portion of a municipality, or a neighborhood. First created in Texas in 1987, there are now a number of such districts throughout the State. MMDs can provide incentives for economic development and tourism, as well as promote economic growth in underdeveloped areas. MMDs supplement basic government services and can address with pinpoint specificity the exact needs of a particular community.

As the Committee learned from its public hearing on the subject, MMDs may be created within the corporate limits of municipalities, upon the request of real property owners who are experiencing a need for more governmental services than the municipality in which the property lies can provide. Such property owners establish an MMD for the purpose of taxing or assessing themselves in order to supplement municipal and county services. Such property owners recognize that MMDs are a valuable and important tool for them to cooperatively implement solutions for collective neighborhood problems.

Since MMDs exist within the corporate boundaries of municipalities, the municipal governments demand accountability from them before allowing implementation of public works projects. A municipality must approve projects that are to be constructed in public rights of way or on city property, or that involve water, wastewater, drainage, or streets and roads. In addition, when the projects involve water, wastewater or drainage, the Texas Commission on Environmental Quality (TCEQ) oversees the plans and construction.

This accountability also extends to the power of a municipality to consent to the creation of a MMD. The city also has the authority to approve or disapprove any requests for annexation of territory into an existing MMD. The appointment of the Board of Directors of a MMD is initially performed by the legislature, or the TCEQ. If a MMD Board of Directors believes it is feasible and necessary to issue public debt to finance a public project, it must obtain consent from the municipality and, in certain cases, from the TCEQ. In certain unique circumstances, a MMD can be created outside the corporate limits of a municipality, in which case many of the city functions are performed by the county.

Key city department heads typically are ex-officio members of a MMD Board of Directors, and will receive agendas, minutes and board packets, as well as the opportunity to attend board meetings and be involved in public discussions about community problems and any plans and projects intended to address such problems. MMDs are subject to all municipal ordinances, and the city personnel often assist the MMD in charting a course through a maze of overlapping and occasionally conflicting regulations in order to enable a MMD-sponsored project to be successful. MMDs also are subject to all "open government" provisions found in state law, as stated above, including open meetings and

open records laws, public funds investment and competitive bidding.

Ultimately, a municipality may dissolve a MMD, under certain circumstances, and subject to the payment of debt.

The TCEQ has oversight over MMD governance, including authority to require annual financial audits, compliance with reporting of information similar to water districts, and, as stated above, approval of certain proposed bond issuances.

Tax Increment Reinvestment Zones

Municipalities are authorized to engage in tax increment financing pursuant to Chapter 311, Tax Code. Forty-eight of the fifty states are engaged in tax increment financing. Tax increment financing is a method that a municipality can utilize to reinvest its tax revenues on a specific portion of its incorporated area to foster and encourage economic development.

Numerous municipalities in Texas engage in tax increment financing, and have created or established TIRZs to denote the area in which such municipal investment will occur. Typically, a municipality elects to devote special investment to the central city or downtown area, and typically a city focuses on aspects of the downtown area that attract tourists and other visitors.

The Committee heard testimony about the partnerships that are formed in some municipalities, MMDs, TIRZs, and the city governments. Public projects agreed upon by all three entities can be accomplished rapidly and efficiently, to the benefit of the citizens and the property owners in the area. Development of unutilized or underutilized areas, and redevelopment of blighted or deteriorated areas is the most common use of tax increment financing.

In the past, confusion has arisen over the working relationships between MMDs, TIRZs, and municipalities. Some have questioned the need for multiple entities addressing the same or similar problems. Testimony was given explaining necessary complexity due to the separate legal interests of the entities. As TIRZs function as financial extensions of cities, the current structure although somewhat cumbersome protects municipal interests while permitting MMDs to better accomplish their localized purposes. Collapsing these interests and pursuits into a single entity would be legally inappropriate and would defeat the purposes for using MMDs in the first place.

The only method for creation and establishment of a TIRZ is a municipal resolution or ordinance adopted at a public city meeting, notice of which was published according to state law. Both the City government and the community have ample opportunity to participate in the organization and formation of a TIRZ. The governing body of a TIRZ is appointed by municipal government, and city representatives typically attend each meeting of the governing body. All projects of a TIRZ are approved, if not conceived of, by the municipality. Since a TIRZ is legally a part of the municipality, and ample municipal oversight is provided, the Committee found that there is no need for Legislative involvement with current law relating to TIRZs at this time. The Committee finds that:

- There is ample municipal oversight of TIRZ's;
- TIRZ's are accountable to the creating municipality and the other participating taxing units;
- A TIRZ cannot issue bonds or other obligations, impose fees, exercise the power of eminent domain, or levy taxes;
- A TIRZ can only exercise the powers granted to it by the municipality;
- A TIRZ must implement the project plan and reinvestment zone financing approved by the municipality;
- The municipality may terminate a TIRZ at any time;
- The use of TIRZ's throughout the state has been tremendously successful;

RECOMMENDATIONS

Municipal Management Districts

The Committee's main purpose in exploring this subject was to educate itself on the purposes of Municipal Management Districts and Tax Increment Reinvestment Zones and the tools these entities use to execute its responsibilities. During this process, the Committee found that virtually all existing MMDs in Texas were created through special legislation, most of which passed through this Committee on their way to final passage. Chapter 375, Local Government Code, was enacted in 1987 to allow creation of MMDs through the agency now known as TCEQ, but to date, not a single MMD in Texas has been created under the provisions of this Chapter.

The Committee discovered, through public testimony and private interviews, that there are numerous issues serving as a barrier to the creation of MMDs through the TCEQ. Among the barriers were the following factors:

- MMDs can be created only over areas inside corporate boundaries, not in extraterritorial jurisdictions;
- Only in cities with populations greater than 25,000;
- In Houston, cannot be created by the TCEQ in areas within a 3.5 mile radius of the Harris County Courthouse; and
- Chapter 375, Local Government Code, has not been revised and updated in many years. As a result, creation of a district by special act of the legislature ensures that

modern statutory language will govern the MMD. Many provisions that have become the standard in special acts are not found at all in Chapter 375.

The Committee firmly believes that for a variety of public policy reasons, the barriers to creation of these districts through administrative petition are both necessary and proper. Despite the success of most MMD's, there have been a few which have not acted in good faith or as originally intended. Therefore, the committee feels it necessary to continue to allow the legislature's natural oversight function to play a part in the creation of MMD's.

Nevertheless, the Committee does believe it is necessary to further explore updating Chapter 375, Local Government Code to include provisions that have been used successfully in special districts established since 1987 during the next legislative session. This "modernizing" of this chapter would act as a model for the future creation of Municipal Management Districts, whether their creation be through special legislation or administrative petition. Any deviation from this model could act as indicator for an in depth review of the proposed special district.

In addition, the Committee expects that it should consider modifying Chapter 375, Local Government Code to remove existing barriers to the expansion or contraction of any special district boundaries or powers through TCEQ's administrative petition process. Like the creation of special districts, the majority of modifications to special districts have been made by special act of the legislature. If a special district has shown that it has benefited the city, its residents, and its property owners it should have the option of moving easily through the administrative petition process in addition to the legislative process.

Finally, any reference to the Texas Natural Resource Conservation Commission (TNRCC) in Chapter 375, Local Government Code should be changed to the Texas Commission on Environmental Quality (TCEQ).

Tax Increment Reinvestment Zones

The Committee recommends no legislative changes regarding TIRZ's. In fact, the use of TIRZ's as a municipal tool to promote the economic development of the state deserves full legislative support. The Legislature should be mindful to not inadvertently damage this vital engine of redevelopment.

CHARGE TWO

Actively monitor the implementation of SB 264, 78th Legislature, sunset legislation for the Texas Department of Housing and Community Affairs. Include an analysis of whether further reforms are needed through a review of best-practices in other states.

SUMMARY

The TDHCA Sunset bill of the 78th Texas Legislature, S.B. 264 by Texas State Senator Eddie Lucio, sought to strengthen the effective ability of the Texas Department of Housing and Community Affairs (TDHCA) to place needed affordable housing in all areas of the state and bring balance and good judgment back to the policies and regulations that govern affordable housing. The Legislature felt that changes made in the name of reform during the 77th Legislature in 2001 had actually weakened the department's ability to do its job and set out to reverse these changes. However, the House Committee on Urban Affairs finds through testimony heard during interim hearings that the department has systematically failed to correctly implement the most recently passed legislative directives in S.B. 264.

BACKGROUND

Senate Bill 264 attempted to bring balance back to the state's affordable housing primarily through modification of the most important public/private partnership program – the Low Income Housing Tax Credit Program. The bill sought to ensure that the private-market players (both for- and non-profit) that are vital to the success of this program are not forced into entering financially unfeasible developments at the behest of the state, as well as to ensure that community input would be bolstered where affordable housing is proposed to be built.

The changes made in S.B. 264 were guided by four overriding principles: reverse the trend of warehousing low-income tax credit developments, encourage community participation in selecting viable low-income housing sites, locate tax credit developments in areas with the most need, and finally make affordable housing available to all persons below 60% of Area Median Family Income (AMFI). The agency was granted three new tools in addressing these principles:

- Prevent the allocation of low-income tax credits for a development within 1-mile of any low-income developments that have received tax credit allocations during the previous tax credit allocation round.
- Increase community participation in the process by requiring elected state officials, local community groups, and elected local officials to be notified of any tax credit applications. Then, granting points to any applicants who have received support among these community groups and/or elected state officials.
- Establishment of the "exurban" definition in an attempt to spread the placement of tax credit developments throughout existing urban regions.

Every year, TDHCA must write and have approved by the Texas Governor a Qualified Allocation Plan (QAP) which governs the details of the actual tax credit application. S.B. 264, for the first time, established statutory scoring priorities which were to be required in any subsequent QAP.

Finally, S.B. 264 also directed the agency to establish an Alternative Dispute Resolution Policy (ADR) to encourage an impartial third party to help the state make reasonable determinations about industry standards in order to help solve issues of appeal that are viewed as overly subjective for such a competitive allocation program.

In large part, Senate Bill 264 attempted to restore the balance in Texas housing policy. At the most basic levels, the state simply cannot afford the cost of pursuing the current housing policy and equilibrium must be restored to allow the state to partner with the private housing industry so that all people and communities that need affordable housing can realize the fulfillment that a stable housing environment can bring.

FINDINGS OVERVIEW

On December 1, 2003 Governor Rick Perry signed the first TDHCA Qualified Allocation Plan (QAP) after the passage of S.B. 264, which would govern the rules of the application process for the 2004 round of the Low-Income Housing Tax Credit Program (LIHTC). On January 7, 2004, at the request of the Urban Affairs Committee, Chairman Robert Talton requested an Attorney Generals opinion on the consistency of this new QAP with Section 2306 of the Texas Government Code, which governs much of the LIHTC.

Having not received a response to the inquiry, the Committee on Urban Affairs met on March 24, 2004 to question the Executive Director of TDHCA, Edwina Carrington, the TDHCA Board Chair, Elizabeth Anderson, several staff members of TDHCA as well as representatives of both the for-profit and non-profit housing community on the implementation of the 2004 QAP.

On June 23, 2004, Attorney General Greg Abbott published Opinion No. GA-0208 in reply to the request. The Attorney General determined that the Department had not in fact complied with many of the changes made in S.B. 264. Though the Department did seek to correct the 2004 QAP with a supplemental QAP, the committee still finds, based on the testimony received and this AG opinion, that the TDHCA staff and board has methodically failed to correctly implement many of the important provisions of S.B. 264. Additionally, the department has unwisely used its discretion to mitigate the effects of the bill by loosely construing stricter statutory directives while at the same time making overly technical interpretations of other provisions of the law. TDHCA's ill judgment has worked to undermine the lawful oversight efforts of the legislature to restore fiscal integrity to the tax credit program while at the same time diminishing the value of local community input about the program.

Finding 2.1- The 1-mile/1-year rule has had a positive effect on reversing the trend of warehousing low-income housing tax credit developments. In addition, two sections in S.B. 264 are potentially contradictory and could work to question the validity of future low-income housing tax credit development locations.

Section 2306.6711(f) of the Government Code was added by S.B. 264 to prevent the continued warehousing of low-income housing tax credit developments.

"Section 23. Section 2306.6711, Government Code, is amended by amending Subsection (b) and adding Subsection (f) to read as follows:

(f) The board may allocate housing tax credits to more than one development in a single community, as defined by department rule, in the same calendar year only if the developments are or will be located more than one linear mile apart. This subsection applies only to communities contained within counties with populations exceeding one million.

After taking testimony on this new provision, the Committee has determined that this is an extremely useful tool, that the positive results from this provision has yet to fully transpire, and that the Department should continue to rigorously enforce this statute. The Committee encourages any future legislature to retain this provision.

Still, the committee is concerned that there is some question as to whether this section is in conflict with Section 2306.6703(a)(3)(B) of the Government Code. The Committee believes that this possible conflict should be examined and alleviated if need be during the next legislative session.

Finding 2.2 - The Exurban distinction first used in the 2004 QAP was an important tool in spreading out low-income housing tax credit developments within the several regions, but the Department has not completely utilized the benefit of this new definition.

The power of an exurban distinction in statute was created to allow proposed developments located on the outskirts of urban areas to be able to compete against proposed developments located in traditional central urban areas. The Committee saw that there is as much or maybe even more need for affordable housing in these areas outside of the traditional urban areas and sought to allow these two areas to compete with the benefit of an exurban distinction.

Though the Department did award 10 points in the 2004 QAP to exurban developments, the majority of those exurban developments that received low-income housing tax credits were granted additional points through special set-asides for at-risk and elderly developments. These exurban developments would not have received tax credits without being placed in the special set-aside designations and department rules are what are blocking the exurban developments from receiving tax credit allocations.

The Committee does find that there has been confusion caused by the omission of a working exurban definition in statute. The Committee believes that there is a need for exurban to be defined in statute, but was unable to create one during the interim period. If the legislature continues to use this tool during the next session as this interim committee recommends, there should be a definition in statute.

Finding 2.3 - Through its overly-technical implementation of community support provisions in SB 264, as well as adding additional hurdles to providing community support in its own QAP, the department has severely undermined the faith that input of local communities is valued by the state in placing low-income housing developments.

Of all of the failings of TDHCA in implementing the legislative intent of SB 264, the failure to properly take into account public input is the most egregious and damaging to the furthering of its mission of providing for affordable housing in Texas. Considering the laxity with which it approached the scoring language in SB 264, TDHCA's decision to take a hard-line approach to scoring of Quantifiable Community Participation letters (QCP, or "support letters") is conspicuously shameful and rife with subjectivity.

Rather than rising in opposition to the placement of affordable housing in their communities during the 2004 tax credit round, the overwhelming number of community organizations (neighborhood associations, city councils, county judges, community development officials, citizen organizations, etc) who provided input to the Department instead expressed great levels of support for the proposed developments. Of the over 240 letters received among the multiple developments, only a handful voiced opposition. However, only 14 letters received full scoring credit and most were rejected out of hand because they either did not comply with the Department's draconian requirements in some cases or were ruled to fail the department's rigid reading of SB 264.[1]

The legislature's purpose in requiring scoring for community support letters was to encourage developers to build community support before any tax credits were allocated. It is clear from the results of the 2004 round that the local communities and development industry rose to the challenge posed by "quantifiable community participation," and that TDHCA, in large part, shirked its duty to the people of Texas by not fully crediting all of the support letters.

During the 2004 allocation round, partial confusion can be attributed to the lack of a working definition for community organizations in S.B. 264. Despite its best efforts, the definition created by the Department staff and approved by the Board of Directors in the 2004 QAP was unable to alleviate any confusion. As a result, many of the organizations who did try to include themselves in the process were locked out.

Even more of these same organizations were locked out of the process by the rules promulgated by the Department for a neighborhood organization actually showing it's support. Such provisions requiring a neighborhood organization to list the names of its members or requiring transcripts of meetings indicating how an organization chose to support a proposed low-income housing development became roadblocks to the legislature's intent to include local residents in the process. The hurdle to community participation is so high that this committee is suspicious that the

Department may have sought to completely subvert its legislative intent with regards to community participation letters.

The Committee does find that rules promulgated by the department for requiring community organizations to indicate its support by a standard date work well in protecting against bad acting developers. The Committee encourages the Board and The Department to strictly enforce these provisions.

Additionally, the Department erred in creating a positive and negative scoring method for Quantifiable Community Participation letters. This was not mandated by SB 264 as clearly indicated by the language in the bill.

"SECTION 22. Section 2306.6710, Government Code, is amended by amending Subsections (b)...to read as follows:

> B) quantifiable community participation with respect to the development, evaluated on the basis of written statements from any neighborhood organizations on record with the state or county in which the development is to be located and whose boundaries contain the proposed development site [~~the rent levels of the units~~];

S.B. 264 did specifically require that letters from state-officials be scored negatively for a negative letter, positively for a support letter, and an application should receive no points for a state-official failing to submit a letter or for submitting a letter with no position on the proposed development. The Committee believes that if the legislature intended to give negative points to negative quantifiable community participation letters, it would have indicated just that as it had done in regards to scoring letters from state-elected officials.

Finding 2.4 - The Department erred in granting points for letters from local elected officials.

Though the Department has since removed any scoring for local elected officials in the current QAP, the Department did originally grant points for letters from local elected officials. It is the Committee's opinion that the language in S.B. 264 was very clear in granting points to only **state** elected officials.

> 2) Language amending Sect. 2306.6710(b)(1)(F):
> "(F) the level of community support for the application, evaluated on the basis of written statements from state elected officials…"

Though this mistake was subsequently corrected in the 2004 QAP, the Committee believes this point illustrates a simple example of the willingness of the Department and the Board to completely ignore the will of the legislature.

Finding 2.5 - TDHCA misinterpreted the plain language of SB 264 with regard to scoring of the tax credit program and, as a result, caused undue harm and unwarranted expense to the state tax credit program, applicants of the program, and those communities most affected by the program.

> "The 2004 qualified allocation plan contradicts section 2306.6710(b)'s plain language and exceeds the Department's authority to the extent it is inconsistent with section 2306.6710(b)(1)."
>
> -- excerpt from Texas AG opinion No. GA-0208

The full text of the applicable sections amended in S.B. 264, as well as Texas Attorney General Opinion No. GA-0208 issued on June 23, 2004, can be found in the Appendix. Following is an excerpted portion of the bill, SECTION 22 of SB 264, that pertains directly to scoring components of the tax credit program:

"SECTION 22. Section 2306.6710, Government Code, is amended by amending Subsections (b), (d), and (e) and adding Subsections (f) and (g) to read as follows:

(b) If an application satisfies the threshold criteria, the department shall score and rank the application using a point system that:

(1) prioritizes in descending order criteria [~~based on criteria that are adapted to regional market conditions and adopted by the department, including criteria:~~

[~~(1)~~] regarding:

(A) financial feasibility of [~~the income levels of tenants of~~] the development based on the supporting financial data required in the application that will include a project underwriting pro forma from the permanent or construction lender;

(B) quantifiable community participation with respect to the development, evaluated on the basis of written statements from any neighborhood organizations on record with the state or county in which the development is to be located and whose boundaries contain the proposed development site [~~the rent levels of the units~~];

(C) the income levels of tenants of the development [~~period of guaranteed affordability for low income tenants~~];

(D) the size and quality of the units [~~cost by square foot of the development~~];

(E) the commitment of development funding by local political subdivisions [~~size, quality, and amenities of the units~~];

(F) the level of community support for the application, evaluated on the basis of written statements from state elected officials [~~the services to be provided to tenants of the development~~];

(G) the rent levels of the units [~~commitment of development funding by local political subdivisions that enables additional units for individuals and families of very low income~~];[~~and~~]

(H) the cost of the development by square foot [~~level of community support for the application, evaluated on the basis of written statements of support from local and state elected officials representing constituents in areas that include the location of the development~~]; and

(I) the services to be provided to tenants of the

development; and…"

The selection criteria are the heart of the Qualified Allocation Plan (the rules for the tax credit program, the QAP). The initial 2004 QAP (draft version, as well as the first approved QAP) did not comply with the scoring criteria mandated by Chapter 2306 of the Texas Government Code, especially the revisions contained in Section 22 of Senate Bill 264. Although the scoring component must also comply with the various provisions of Chapter 2306 of the Texas Government Code that requires scoring preferences, priorities or incentives to various specific activities as mentioned above, based on the language of 2306.6710(b), as amended by Section 22 of SB 264, the scoring feature of the selection plan should have ranked, in descending order of priority, the nine items mentioned with any other scoring preferences or priorities mentioned in Chapter 2306 having points no higher than the lower items in the designated scoring priorities of 2306.6710(b).

Although the staff and board were made aware through public input that the 2004 draft QAP did not comply with SB 264 as early as October 2003, TDHCA appeared to willfully choose to erroneously interpret this plain language, which clearly shows the intent of the Legislature to change the scoring priorities of the tax credit program, in order to issue a QAP that served to render the scoring for financial feasibility meaningless. The Attorney General's Opinion forced the Department to subsequently amend its scoring, however, the Department chose instead to mitigate as much as possible the ruling in order to preserve the scoring system that it preferred.

Due to its actions, TDHCA needlessly caused unwarranted harm to the integrity of the program, its applicants, and local communities, by forcing the program to readjust scoring midway through the process and by recklessly questioning the legitimacy of the oversight of the legislature.

Finding 2.6 - TDHCA has failed to develop and implement a policy to encourage the use of appropriate Alternative Dispute Resolution (ADR) procedures with regard to the tax credit program. All appeals should automatically be referred to an impartial third-party for a swift resolution that can reasonably be expected to take place during a tax credit round.

Chapter 10, §1.17(e)(3) of the Texas Administrative Code (TAC), delineates how the ADR process must be implemented by an applicant for any of the department programs:

> (3) ADR Proposal. If at any time an applicant for Department programs or other interested person would like to engage in an ADR procedure with the Department, the person may submit by letter a written ADR proposal to the Department's Dispute Resolution Coordinator stating the nature of the dispute, the parties involved, any pertinent deadlines, whether all parties agree to refer the dispute to ADR, proposed times and locations, the preferred type of ADR procedure, and, if known, one or more potential impartial third parties.

Even though putting all of the impetus to initiate and sustain ADR upon the applicant during a fast-paced tax credit round seems discouraging enough, the most dissuading aspect of the Department's ADR process is that there is little indication that an applicant may need ADR until the Department rules adversely, and then it is too late for ADR to have any effect under the rules promulgated by the Department.

Due to the fact that Chapter 10 §1.17(b)(1-2) (see below) states that the Governmental Dispute

Resolution Act does not grant TDHCA authority to engage in binding arbitration, and that the mediation process cannot overturn a decision by the Department, this renders the ADR process, as promulgated by the department, meaningless and therefore extremely discouraging to applicants who must pay an application fee of upwards of $5,000 in order to receive unsuitable treatment from the Department.

> Chapter 10 TAC §1.17(b)(1-2):
> (1) "Alternative Dispute Resolution" or "ADR"--a procedure or combination of procedures that uses an impartial third party to assist individuals in voluntarily resolving disputes, including procedures described in Sections 154.023-154.027, Civil Practice and Remedies Code. (§2009.003(1), Governmental Dispute Resolution Act). The Governmental Dispute Resolution Act does not grant the Department authority to engage in binding arbitration. (§2009.005(c)).
> (2) "Mediation"--a dispute resolution procedure in which an impartial person, the mediator, facilitates communication between the parties to promote resolution of the dispute. The mediator may not impose his or her own judgment on the issues for that of the parties. (§154.023(a) and (b), Civil Practice and Remedies Code).

Finally, due to the ex parte restrictions, TDHCA is unable to participate in ADR in good faith as is required. Due to the rules promulgated by the Department, all parties to ADR must have the authority to enter into an agreement to resolve the dispute. At the same time, ex parte prohibits those officials with that authority from participating.

Chapter 10 TAC §1.17(g):
(g) Good faith; Voluntary Agreement; Public Information. All parties participating in an ADR procedure are expected to do so in a good faith effort to reach agreement. All parties participating must have the authority to enter into an agreement to resolve the dispute. The decision to reach agreement is voluntary. If the parties reach a resolution and execute a written agreement, the agreement is enforceable in the same manner as any other written agreement of the same nature with the State. A written agreement to which the Department is a signatory resulting from an ADR procedure must be approved by the appropriate authority and is subject to the Public Information Act, Chapter 552, Texas Government Code.

RECOMMENDATIONS

On September 9, 2004, the Texas Department of Housing and Community Affairs held a public meeting to discuss several items. During this meeting, Vice-Chairman of the Board Kent Conine made a statement that the Committee on Urban Affairs finds is indicative of the overall conflict between the right and duty of the legislature to write the laws and the failure of the Department and Board to implement those laws associated with running the Department.

> "With all due respect, sometimes good ideas do emanate from this board as opposed to the state legislature or the United States Congress. And that being said, we don't necessarily have to do just what we're instructed to do by other folks."
>
> *transcripted quotation from TDHCA Board Member Kent Conine during the September 9, 2004, TDHCA Board Meeting. Although Mr. Conine was discussing the laudable goal of using 5 percent of the HOME Program funds for the Texas Home of Your Own Program (instead of using 100 percent of the non-participating jurisdictions' HOME funds in those areas), his comment is indicative of the challenge facing the 79th Texas Legislature.*

The Committee does agree with Mr. Conine, that some good ideas do emanate from the Board of Directors as well as from the Department staff. It does not agree with him that they "don't necessarily have to do just what we're instructed to do by other folks." Without subjecting the reader of this report to a civics lesson, the Committee believes that just the opposite is true.

The House Committee on Urban Affairs finds that the Department and Board of Directors of the Texas Department of Housing and Community Affairs has either deliberately ignored the will of the legislature or is completely unable to implement the changes in Senate Bill 264. The Committee worked hard during the 78th Legislature to write a bill that was clear and concise and believes that it should explore other options in finding a way to properly administer the Low-Income Housing Tax Credit Program in the future.

The Committee was asked to include an analysis of best-practices in other states in this report, but was forced to spend its time sifting through and understanding the failures of the Department to properly implement S.B. 264. Therefore, the Committee recommends that the 79th Legislature explore in detail the subject of best-practices.

In addition, the Committee would like to make the following recommendations based on the specific findings on the implementation of Senate Bill 264:

- Strictly enforce the 1-mile/1year rule and reexamine the usefulness of this tool in ending the practice of warehousing low-income housing tax credit program developments. Also, clarify the two potentially contradictory sections which were passed in S.B. 264.
- Clearly define an Exurban city/town in statute and make certain this tool will be used to direct low-income housing tax credit developments to those areas with the most need and reverse the practice of warehousing these developments while making certain the

definition does not divert money from rural areas.

- Create legislation that will allow local communities to easily and simply involve itself in the proper placement of low-income housing developments. The language should not allow the Department to undermine this important component through complicated departmental rules.
- Make clear the legislature's policy decision to give points in the Qualified Allocation Plan to only state elected officials, rather than local elected officials.
- Rewrite any language that allows permissive and arbitrary interpretation of scoring in future Qualified Allocation Plans.
- Pass legislation that encourages the use of Alternative Dispute Resolution (ADR), allows either party (agency or applicants) to request ADR, is not a binding arbitration process and does not block access to the courts if necessary, and finally allows ADR to be effective for the same tax credit year.

CHARGE THREE

Evaluate the effectiveness current programs in meeting the state's housing needs and examine new alternatives such as urban land banks, homestead preservations districts and programs to provide gap financing.

SUMMARY

On May 20, 2004 the House Committee on Urban Affairs met to discuss interim charge #3. The Committee heard testimony from several representatives of the housing community about new alternatives to meet the state's housing needs. Testimony centered on how urban land banks, homestead preservations districts and various programs to provide gap financing help meet these needs.

The Committee saw this interim charge as an opportunity to educate itself on these alternatives and will therefore make no recommendations to the 79th Legislature on these subjects. This report will focus on the details of these alternatives.

FINDINGS

Urban Land Banks

Created by HB 2801 of the 78th Regular Session, the Urban Land Bank Demonstration Program allows the City of Dallas to acquire unproductive and vacant, but developable lots to be "banked" for future affordable housing development. Lots are acquired by foreclosing on property with several years of delinquent property taxes. Prior to the passage of HB 2801, property sold pursuant to foreclosure of a tax lien was sold at a public auction. Now, the land bank created by the municipality has the option of obtaining property prior to public purchase. The land bank must then resell the property for the exclusive use of affordable housing to private developers with three years of its purchase. The overall purpose is to stabilize older neighborhoods, reduce the number of vacant or abandoned lots, increase property values, and encourage private investment.

In January of 2004, the Dallas City Council approved the FY 2003-2004 Urban Land Bank annual plan as required by HB 2801 and has since submitted 106 properties for foreclosure. Movement on these properties were delayed because of requirements for inter-local contracts between taxing entities and the City of Dallas and the Dallas Housing Acquisition and Development Corporation (DHADC). 375 properties have been submitted for foreclosure under the FY 2004-2005 annual plan as approved by Dallas City Council in October of 2004. DHADC expects that it should hold title to several properties in the next several months.[2]

Homestead Preservation Districts

HB 3432 by Representative Eddie Rodriguez was filed during the 78th Regular Session. If passed, the bill would have created a Homestead Preservation District Demonstration Program in which three municipalities could participate. The Committee was not able to hear testimony on the bill during the session, but was interested in exploring this concept during the interim. This report will only provide information on the subject and the Committee will not make recommendations.
As written in HB 3432, a Homestead Preservation District combines three economic development tools in concert with each other all for the development of affordable housing. These three tools are described below:

Homeowner Land Bank

Called a Homeowner Land Bank in HB 3432, this is identical to an Urban Land Bank described above. As with an Urban Land Bank, this entity would be created by the municipality, be required to pass an annual plan and would be used to acquire and hold land that has been foreclosed upon for failure to pay property taxes.

Homestead Land Trust

This is a nonprofit entity which purchases land within the Homestead Preservation District, often from the Homeowner Land Bank for the specific purpose of the construction and revitalization of affordable housing. The Land Trust then may confer a long term lease of the land for to a private developer for the construction of either single family or multi-family affordable housing. Since the land continues to be held by the nonprofit, it is not subject to property taxes and the savings is passed on to the residents. It is a unique situation in which the family or developer owns the home, maintains the structure and holds equity in the home, while the underlying land is owned by the nonprofit.

Tax Increment Reinvestment Zone

The final component of a Homestead Preservation District is the use of tax increment financing for the purpose of improving and building affordable housing within the district. Funds created would be dedicated to either city certified community housing development organizations or to the Homestead Land Trust for the purpose of financing needed structural improvements or enhanced infrastructure within the investment zone.

Gap Financing

During interim hearing #3, the issue of gap financing primarily centered on the use of the Housing Trust Fund (HTF) to supplement construction and maintenance in areas with low median family incomes. Low income developments in areas with low median family incomes are very often unviable to both non-profit and for-profit developers because of low rental rates causing low return on investment. The Housing Trust Fund is therefore an important tool in making these developments viable in the areas of the state that most need affordable housing.

Section 2306. 202 of the Government Code requires that the Department of Housing and Community Affairs:

"provide loans, grants, or other comparable forms of assistance to local units of government, public housing authorities, nonprofit organizations, and income-eligible individuals, families, and households to finance, acquire, rehabilitate, and develop decent, safe, and sanitary housing."

Department records show an average of 3 to 1 oversubscription for the Housing Trust Fund from 1999 to 2003 with an average of $10 million being granted to for-profit developers and an average of $9 million for non-profit developers. The 78th Texas Legislature appropriated $9.2 million for the

2004 fiscal year and $3.2 million for the 2005 fiscal year out of the General Fund to the Trust Fund and the Department expects that they will see the same 3 to 1 oversubscription to this fund for 2004 and 2005.

Due to recent shortfalls in the State Budget, housing advocates and developers alike have sought to find a way to permanently fund the HTF through a source other than the state's general revenue. Testimony was given setting out six policy considerations when examining a permanent revenue source for the HTF. The committee feels these considerations are an appropriate way to examine this issue in the future. Those considerations are as follows:

Revenue Potential: *The source of revenue has the potential to generate significant revenue for the fund.*

Nexus to Housing: *The source has a direct connection with affordable housing.*

Collection: *The revenue can be collected easily and with minimal or no additional costs.*

Leveraging: *The source can be used to leverage federal and private resources for affordable housing.*

Security: *The source is permanent and cannot be encroached upon for other uses.*

Efficiency: *The revenue can be used efficiently and effectively for the development affordable housing.*

Considering these guidelines, the committee was presented with two types of permanent revenue options which have been used in other states and given an estimate of how much revenue these could generate.

Thirty-seven states have added a real estate transfer fee on all real estate transactions based on the percentage of total transaction. In Texas, a flat rate of 0.1% on all residential housing could generate as little as $34.2 million which equates to a tax burden of $159 on the average home sold in Texas during 2003. The national average of a 0.44% flat rate could generate $150.5 million and equate to a $703 on the average home sold in Texas during 2003.

2003 Texas Residential Housing Total for 2003: $34,198,650,324	Fee Burden for Average House Price ($159,800)	Fee Burden for Median House Price ($127,900)

0.1% Flat Rate	$34,198,650.32	$159.80	$127.90
0.44% Flat rate (national average)	$150,474,061.43	$703.12	$562.76
0.5% Flat rate (Maryland rate)	$170,993,251.62	$799.00	$639.50
0.7% Flat Rate (Florida rate)	$239,390,552.27	$1,118.60	$895.30

Source: Real Estate Center at Texas A&M Univerisity, http://recenter.tamu.edu/data/hs/hs800a.htm

The State of Arizona has instituted a flat fee of $9 for each real estate transaction and is known as document recording fee. A fee of $9 on each home based on the total number of homes in Texas during 2003 could generate as much as $5.6 million based on statistics gathered from the National Association of Realtors. A $40 fee could generate $25.2 million for the Housing Trust Fund based on those same figures.

Document fee increase amount	2003 MLS Total Home Sales in Texas: 214,006	Average of 2003 MLS and NAR Total Home Sales in Texas: 422,703	2003 NAR Total Home Sales in Texas: 631,400
$9 increase*	$1,926,054	$3,804,327	$5,682,600
$15 increase	$3,210,090	$6,340,545	$9,471,000
$20 increase	$4,280,120	$8,454,060	$12,628,000
$40 increase	$8,560,240	$16,908,120	$25,256,000

based on information gathered from http://www.recorder.maricopa.gov/fees.htm

RECOMMENDATIONS

As mentioned, the committee will not make any recommendations for this particular interim charge, but hopes that this study will act as a starting point for future discussions on these subjects.

CHARGE FOUR

Evaluate the effectiveness of Uniform State Service Regions in allocation of Home Investment Partnership Program (HOME) funds and low-income tax credits to develop housing and examine alternatives to meet the needs of the state's rural areas.

SUMMARY

On July 16, 2004, the House Committee on Urban Affairs met to discuss interim charge #4. The committee heard testimony from the Executive Director of the Texas Department of Housing and Community Affairs, Edwina Carrington, several rural housing advocates, and rural low-income housing developers. Testimony centered on the importance of the Home Investment Partnership Program (HOME) funds to the future of rural development and how to better leverage these funds for future rural development.

This report will focus on how and why the HOME program is the best vehicle for preserving affordable rural multifamily housing, how TDHCA's current allocation of HOME Funds does not sufficiently further the legislative goal of the Cranston-Gonzalez National Affordable Housing Act that created the HOME program, and how it diverts vitally needed rural funding to urban areas. Finally, this report will make recommendations to correct these problems.

BACKGROUND

Created in 1990, the Cranston-Gonzalez National Affordable Housing Act (42 U.S.C. Section 12701) authorized Congress to allocate funds to the states. The Texas Legislature subsequently created legislation to administer these funds through what is now the Texas Department of Housing and Community Affairs.

As with most federal legislation, the Congress states the specific purposes and goals of this act. The first four stated purposes of this act are as follows:

> **SEC. 12722. Purposes**
>
> The purposes of this title are--
>
> (1) to expand the supply of decent, safe, sanitary, and affordable housing, with primary attention to rental housing, for very low-income and low-income Americans;
>
> (2) to mobilize and strengthen the abilities of States and units of general local government throughout the United States to design and implement strategies for achieving an adequate supply of decent, safe, sanitary, and affordable housing;
>
> (3) to provide participating jurisdictions, on a coordinated basis, with the various forms of Federal housing assistance, including capital investment, mortgage insurance, rental assistance, and other Federal assistance, needed--
>
> (A) to expand the supply of decent, safe, sanitary, and affordable housing;
>
> (B) to make new construction, rehabilitation, substantial rehabilitation, and acquisition of such housing feasible; and
>
> (C) to promote the development of partnerships among the Federal Government, States and units of general local government, private industry, and nonprofit organizations able to utilize effectively all available resources to provide more of such housing;
>
> (4) to make housing more affordable for very low-income and low-income families through the use of tenant-based rental assistance;

During the 2004 and 2005 fiscal years, the TDHCA administered annually in excess of $45 million in HOME funds provided to the State of Texas. At present, the state's HOME funds are used for many deserving programs, such as multifamily preservation, single family programs and tenant based rental assistance among others.

Regional Allocation Formula Background

In 2001, the 77th Legislature passed a provision in S.B. 322 requiring HOME funds to be evenly distributed among the 13 Uniform State Service Regions. The purpose of this legislation is simple: the limited housing funds should be allocated among the service regions based on their need and the availability of other housing resources that are available to the regions.

Section 2306.111(d), Texas Government Code, requires TDHCA to allocate the funds. In pertinent part, it reads:

> "d) The department shall allocate housing funds provided to the state under the Cranston-Gonzalez National Affordable Housing Act (42 U.S.C. Section 12701 et seq.), housing trust funds administered by the department under Sections 2306.201-2306.206, and commitments issued under the federal low income housing tax credit program administered by the department under Subchapter DD to all urban/exurban areas and rural areas of each uniform state service region based on a formula developed by the department that is based on the need for housing assistance and the availability of housing resources in those urban/exurban areas and rural areas, provided that the allocations are consistent with applicable federal and state requirements and limitations."

FINDINGS

<u>Finding 4.1</u>: In determining the availability of other housing funds - done as part of the calculation of the Regional Allocation Formula - TDHCA does not adequately take into account which particular funds are available for each corresponding type of housing.

The committee found that in determining the other available sources of financing for a multifamily production program such as the housing tax credits, all multifamily sources of new multifamily financing should be included while excluding government sources that are not related to production or rehabilitation, such as PHA operating subsidies, Section 8 assistance, or HOME financing that is directed to single family or rental assistance. Thus, the availability of funds portion of the housing tax credit formula should include funds available for multifamily housing production and not resident subsidy or single family housing ownership.

In rural Texas today, the availability of mortgage funds is the greatest obstacle to providing housing. By the nature of being located in small communities, the sizes of the developments are smaller than their urban counterparts. Most mortgage lenders will not provide financing for the smaller developments. The reason is simple and understandable – the paperwork costs for a $10,000,000 loan are the same as a $500,000 loan. Since conventional mortgage financing is generally unavailable for the rural developments, it is vital that rural Texas be allowed to leverage HOME

funds and make rural development feasible.

Further compounding the obstacle to rural development, is the Department's new 2004 formula for allocating funds. Prior to the change, the formula included the value of multifamily tax exempt bonds at 100% of their value. Thus, if there were $100,000,000 of multifamily bond funds available, the bonds would count as $100,000,000 of other available financing. The 2004 formula now counts bond financing at only 20% of its value. Thus, the availability of $100 million in bond financing would be reduced to $20 million when determining the other available financing. This reduction has negatively impacted rural Texas as well as all service regions of the state other than three – regions 3, 6, and 7, regions with large urban areas. Thus the funds that would otherwise be available for rural Texas are diverted to areas where financing is available.

In addition, the current Regional Allocation Formula takes into account types of financing that does not directly relate to the production of housing. For example, Public Housing Authorities receive Operating Funds that are applied to the administrative costs of the PHA, but do not directly relate to the production of housing. Still, the current formula includes receipt of these operating funds in its calculation. Another component of the formula is the inclusion of funding available from the United States Department of Agriculture (USDA) Multifamily program. Although some of these funds should be included in the formula, the peculiar accounting methods of the US Government can overstate this other available financing source. Like operating funds, USDA funds included in the formula should be restricted to new direct funds available for multifamily production or rehabilitation while excluding any sum that represents merely the value of a transfer of an existing development.

Finding 4.2: As currently administered by TDHCA, rental housing is not receiving "primary attention" under the HOME Program as required by law.

As indicated before, according to federal law, rental housing must be the primary activity of the HOME Program. As a matter of overall policy, the current allocation of HOME funds fails to sufficiently further the legislative goal of the Cranston-Gonzalez National Affordable Housing Act that created the HOME program. Since Congress has stated that rental housing should be the primary focus of the HOME program, the Texas HOME program should likewise be directed to rental housing. From a review of the programs funded through HOME funds, rental housing is not receiving "primary attention".

In 2003, TDHCA allocated 11.1% of the HOME funds to Rental Housing Preservation or Development. An additional 9.85 % of HOME funds are allocated for Tenant Based Rental Assistance.[3] It is instructive to compare Texas' allocation of funds with the national totals. Obviously, if the Texas experience is similar to the national utilization of funds, then an argument could be made that Texas' priorities are in line with national expectations. However, the converse is true with the Texas utilization of funds deviating greatly from national figures. As of January 1, 2004, the HOME Program has committed $13,163,004,167, of which only 56.1% has been used for rental housing activities. Of the $7,386,045,325 used for rental housing, only $343,353,272 has been used for Tenant Based Rental Assistance. Thus nationally, of the rental housing funds, 95.4% of the total has been used for new construction, rehabilitation or acquisition of rental developments.

The Committee finds that HOME funds have not been used for its original purpose and should be utilized for this purpose in the future.

Finding 4.3: Non-participating jurisdictions should receive 100 percent of the HOME Funds.

HOME funds have been allocated to TDHCA for use in non-participating jurisdictions, which are basically rural Texas. The reason is simple -- participating jurisdictions individually receive a direct allocation of funds from HUD. The mission of TDHCA, as it relates to the HOME program, is to distribute the HOME to areas that do not receive a direct allocation of HOME funds. However, 5% of the HOME funds have been needlessly diverted to urban areas. The Department transfers these rural funds to urban areas because of Section 2306.111(c) of the Texas Government Code, which states:

> "In administering federal housing funds provided to the state under the Cranston-Gonzalez National Affordable Housing Act (42 U.S.C. Section 12701 et seq.), the department shall expend at least 95 percent of these funds for the benefit of non-participating small cities and rural areas that do not qualify to receive funds under the Cranston-Gonzalez National Affordable Housing Act directly from the United States Department of Housing and Urban Development. All funds not set-aside under this subsection shall be used for the benefit of persons with disabilities who live in areas other than small cities and rural areas."

The statute does not require that only 95% of the funds be allocated to rural areas; it states that at least 95% of the funds be allocated to rural areas and "all funds not set-aside" for rural areas shall be used for urban housing for persons with disabilities.

RECOMMENDATIONS

Recommendation 4.1: In order to address the concern raised about the calculation of Regional Allocation Formula the following amendment is recommended to include a legislative directive regarding the types of financing to be included as "other available sources":

(d) The department shall allocate housing funds provided to the state under the Cranston-Gonzalez National Affordable Housing Act (42 U.S.C. Section 12701 et seq.), housing trust funds administered by the department under Sections 2306.201-2306.206, and commitments issued under the federal low income housing tax credit program administered by the department under Subchapter DD to all urban/exurban areas and rural areas of each uniform state service region based on a formula developed by the department that is based on the need for housing assistance and the availability of housing resources in those urban/exurban areas and rural areas, provided that the allocations are consistent with applicable federal and state requirements and limitations. The department shall use the information contained in its annual state low income housing plan and shall use other appropriate data to develop the formula. In determining the availability of housing resources for its multifamily production programs, the Department shall consider the dollar amount of: (1) multifamily tax exempt bonds, (2) HOME funds utilized for multifamily production or rehabilitation, and (3) financing provided by a governmental entity for multifamily production or rehabilitation, but excluding financing involved in the mere transfer of ownership of an existing development. If the department determines under the formula that an insufficient number of eligible applications for assistance out of funds or credits allocable under this subsection are submitted to the department from a particular uniform state service region, the department shall use the unused funds or credits allocated to that region for all urban/exurban areas and rural areas in other uniform state service regions based on identified need and financial feasibility.

Recommendation 4.2: The Committee recommends that serious consideration be given to allocating HOME funds more in line with the primary statutory purpose of the HOME program. In rural Texas, there is a great need for affordable housing. With other federal sources of financing being extremely limited and the tendency for rural properties to be small and unable to obtain bond financing, HOME funds are the sole source of preserving the hundreds of small rural properties that are in need for both development and modernization. The HOME program has been successfully used to provide rehabilitation financing in conjunction with the modernization of affordable USDA financed properties while maintaining the low interest rate loans and the development based rental subsidy for the residents. By coupling various housing programs, the need of rural Texas for adequate housing at affordable rents may be served. In 2004, TDHCA will have $9 million for rental housing preservation an increase from the normal $2 million in prior years. The Department was able to increase the funding because over $50 million in funds previously awarded for single family housing was unused. It is recommended that the legislature direct that $10 million annually of HOME funds be utilized for multifamily development or preservation.

Recommendation 4.3: It is recommended that the statute be amended to set aside 100% of its funds for non- participating jurisdictions and for the preservation of rural housing that meets the

definition of being located in a rural area. Since the urban areas of the state are participating jurisdictions, they receive an allocation of HOME funds directly from HUD. There does not appear to be a substantial justification for transferring funds from rural Texas to areas that receive a direct allocation of funds from HUD. At the same time, the $2,250,000 that would otherwise be available to urban areas under the disability funding would be available for rural disability housing as a matter of first priority. In the event that sufficient applications for the housing for persons with disability in rural areas were not submitted, then the funding would shift to rental housing preservation. Such a shift in policy would still allow for housing for persons with disabilities in rural areas while preserving the ability of the Department to use such funds for preservation in the event that the demand for rural disability housing is less than anticipated.

As mentioned above, there needs to be an exception from the blanket use of HOME funds for non participating jurisdictions and that is to authorize the use of HOME funds to the preservation of developments that will maintain existing governmental financing and that otherwise meet the definition of a rural development. Specifically, there are developments in Texas that receive the benefit of low interest loans from USDA that frequently have development based rental assistance to offer their residents. When they were originally developments years ago, the location was rural. Now, they are still defined as rural by reason of receiving financing from USDA. However, they are ineligible for HOME funds by their location. While ripe candidates for funding as a "preservation of existing affordable multifamily housing", they are unable to obtain HOME funds since the county in which they are located has decided to use its HOME funds for new construction single family housing. An exception for preserving USDA housing should be made.

A proposed revision to §2306.111(c) would be as follows:

"In administering federal housing funds provided to the state under the Cranston-Gonzalez National Affordable Housing Act (42 U.S.C. Section 12701 et seq.), the department shall expend at least ~~95~~ 100 percent of these funds for the benefit of: (1) non-participating small cities and rural areas that do not qualify to receive funds under the Cranston-Gonzalez National Affordable Housing Act directly from the United States Department of Housing and Urban Development or, (2) the preservation of existing affordable housing that receives financing from the United States Department of Agriculture. By rule, the department shall ~~All funds not~~ set-aside 5% of the funds available under this subsection ~~shall be~~ used for the benefit of persons with disabilities. ~~who live in areas other than small cities and rural areas~~. The department shall annually expend $10 million of the funds available under this subsection for multifamily production or rehabilitation in an application cycle that is open to all eligible applicants under subsection 2306.111 (c - 1) and (c -2). If the department does not receive sufficient feasible applications for housing with persons with disabilities or multifamily production or rehabilitation within the first four months of the application cycle, then the funds shall be available for other authorized purposes. "

APPENDIX A
Texas Attorney General Opinion No. GA-0208
Whether the Texas Department of Housing and Community Affairs' 2004 plan for allocating low-income housing tax credits is consistent with Senate Bill 264 (RQ-0161-GA)

APPENDIX B
Texas Government Code, Chapter 2306
Texas Department of Housing and Community Affairs
Subchapter DD - Low Income Housing Tax Credit Program
Section 2306.6710 - Evaluation and Underwriting of Applications

ENDNOTES

[1] Information available at http://www.tdhca.state.tx.us/pdf/agendas/040628-boardbook-040621.pdf

[2] Information available at http://www.dallascityhall.com/dallas/eng/pdf/housing/LandBankPlanFY2004-05.pdf and http://www.dallascityhall.com/dallas/eng/pdf/housing/UrbanLandBankPlan.pdf

[3]Texas Department of Housing and Community Affairs 2004 State of Texas Low Income Housing Plan and Annual Report.