



INTERIM REPORT

TO THE 88TH TEXAS LEGISLATURE

HOUSE COMMITTEE ON
URBAN AFFAIRS
NOVEMBER 2022

**HOUSE COMMITTEE ON URBAN AFFAIRS
TEXAS HOUSE OF REPRESENTATIVES
INTERIM REPORT 2022**

**A REPORT TO THE
HOUSE OF REPRESENTATIVES
88TH TEXAS LEGISLATURE**

**PHILIP CORTEZ, PH.D.
CHAIRMAN**

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Committee On
Urban Affairs

November 28, 2022

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Chairman

P.O. Box 2910
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The Honorable Dade Phelan
Speaker, Texas House of Representatives
Members of the Texas House of Representatives
Texas State Capitol, Rm. 2W.13
Austin, Texas 78701

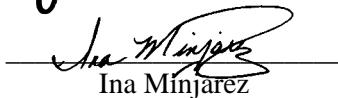
Dear Mr. Speaker and Fellow Members:

The Committee on Urban Affairs of the Eighty-seventh Legislature hereby submits its interim report including recommendations and drafted legislation for consideration by the Eighty-eighth Legislature.

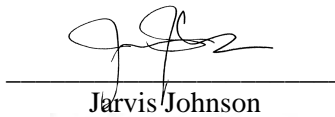
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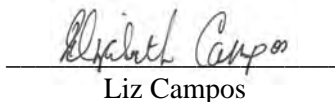

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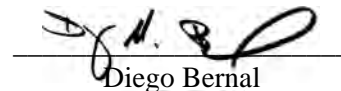

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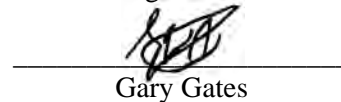

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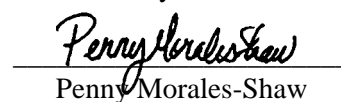

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INTERIM STUDY CHARGES

- CHARGE I:
Oversight** Monitor the agencies and programs under the Committee's jurisdiction and oversee the implementation of relevant legislation passed by the 87th Legislature. Conduct active oversight of all associated rulemaking and other governmental actions taken to ensure the intended legislative outcome of all legislation.
- CHARGE II:
Workforce Housing** Evaluate the availability of workforce housing to support the dynamic economic growth of the state. Study the use of public-private partnerships and other tools to incentivize the development of housing that meets Texas' expanding workforce demands. Develop and include measures to ensure accountability and transparency associated with these tools.
- CHARGE III:
MMD** Review the Municipal Management District Legislative Template with respect to representation and accountability. Make recommendations for improving the template.
- CHARGE IV:
Municipal water &
Wastewater
infrastructure** Study the effects of local governance, planning, and administration on the current state of municipal water and wastewater infrastructure. Examine the measures municipally owned utilities have taken and the costs required to maintain and improve that infrastructure. Make recommendations for cost-effective solutions to ensure reliable infrastructure and uninterrupted municipal utility services, especially during a severe weather event.
- CHARGE V:
Municipal fees** Study municipal fees with respect to the function of the fee and the relationship of the fee to the cost of providing an associated municipal service. Make recommendations to address municipal fees that are disproportionate or unrelated to the cost of providing the associated service.

CHARGE I: OVERSIGHT

Monitor the agencies and programs under the Committee's jurisdiction and oversee the implementation of relevant legislation passed by the 87th Legislature. Conduct active oversight of all associated rulemaking and other governmental actions taken to ensure the intended legislative outcome of all legislation.

BACKGROUND

Texas Department of Housing and Community Affairs

The rules of the Texas House of Representatives grant the Committee on Urban Affairs jurisdiction over matters pertaining to the Texas Department of Housing and Community Affairs (TDHCA). Most of the programs operated by the department are funded almost exclusively with federal funds, and the department has been operating most programs for many years. As with most federally-funded programs, the department must remain within the rules and guidelines laid out by the federal government, and the department continues to run these programs effectively and efficiently.

The most significant addition to TDHCA's programs is the addition of the Rent Relief Program and the Homeowners Assistance Program. With the onset of the COVID-19 pandemic, millions of Americans found themselves unable to continue working as businesses were ordered to close to contain the spread of the virus. Fearing widespread evictions and increased homelessness that would only exacerbate the spread of the disease, federal authorities barred evictions.

First, the federal government enacted the Coronavirus Aid, Relief, and Economic Security (CARES) Act, which placed a moratorium on many evictions through August 24, 2020. The law supplemented temporary eviction moratoria and rent freezes implemented by many state and local jurisdictions using emergency powers. As the CARES Act moratorium expired, the Centers for Disease Control issued a temporary national moratorium on most evictions through December 31, 2020. Further federal action then extended the moratorium through July. Then the CDC issued a limited eviction moratorium on August 3, 2021. On August 26, 2021, the United States Supreme Court ended the moratorium.

In addition to imposing moratoria, the federal government provided a total of \$46.55 billion in Emergency Rental Assistance (ERA). On December 27, 2020, the Consolidated Appropriations Act provided \$25 billion to states and some local jurisdictions to help Americans pay for rent and utilities. Then on March 11, 2021, the American Rescue Plan Act provided another \$21.55 billion for rental assistance.

Prior to federal action, some Texas cities had developed their own rent relief programs using local funds. These cities usually turned to local charitable and religious organizations for help with outreach and qualifying eligible families.

Under the program, each state would receive an allocation of funds, and units of local government with populations that exceed 200,000 would also receive allocations. In the first round of funding through the CARES Act, all eligible Texas units of government were granted a total of \$1.95 billion, with local governments receiving approximately \$638 million dollars, and the state receiving \$1.308 billion. (A complete listing of the ERA1 allocation can be found in Appendix A.)

Under the American Rescue Plan Act, the state received an additional \$1.014 billion, while local jurisdictions received a total of \$526.5 million. (A listing of allocations under ERA2 can also be found in Appendix A.)

After receiving its allocation, the State of Texas opened the Texas Rent Relief Program operated by the TDHCA. The total allocation to the state was almost eight times more than the annual budget of TDHCA. With about 313 full-time equivalent employees, all dedicated to existing programs, the agency could not operate the program on its own, so it turned to private contractors to provide a "turn key" program for intake, qualification, and payments to renters.

While TDHCA made Texas the first state receiving more than \$1 billion to start receiving application for rent relief, the operation was any but smooth sailing. The staff of the House Committee on Urban Affairs prepared a report to the members of the committee detailing the issues the program faced and the delays that had been incurred.¹

The report's highlights include:

- Winter Storm Uri struck as the program went online.
 - The number of vendor-provided phone operators was only about one-third of what was planned.
- Software did not perform correctly and the software needed to be replaced and the website reprogrammed.
 - A second update required thousands of people to reapply or update their applications to continue being processed.
- By March 3rd, less than three weeks since the start of the program, more than 52,000 requests, totaling \$180.2 million had been received, but none had been paid.
- By March 19th, a month after opening, the program had only made three payments.
- By March 23rd, almost 170,000 people had applied, but only 134 had been approved.

-
- The backlog of cases would take months to resolve.
 - The online application process was cumbersome and few could complete it in one pass.
 - Loading documents using mobile phones, often the only computer access many applicants had was very hard.
 - Hold times at call centers were extremely long
 - Applicants often had to make multiple calls for assistance in applying online.
 - The vendor ultimately had to increase the number of people working on the program from the 400 originally planned to more than 1,600 people.

Over time, the total amount of assistance requested exceeded the amount of money available. The application was stopped, but it still took months for applications to be processed and paid. Near the end, the program was advising approved applicants not to expect payment for 21 days after approval. Originally, the department believed it would make payments within 3 days of an application being approved.

TDHCA did prioritize cases facing imminent eviction. The agency contracted with lawyers to find eviction cases and get those cases paid as quickly as possible. Such action undoubtedly saved many people from eviction.

Texas was not alone in facing difficulties administering the rent relief programs. No state had the technical skills to implement such a massive program or the number of spare employees necessary to run it. The private sector vendor chosen to run the program accounted for most of the program's difficulties. While the vendor worked to correct issues, the applications were mounting up much faster than they could resolve issues.

Sadly, Texans who were already under duress due to loss of employment and the threat of COVID-19, suffered more stress as the program failed to perform as expected. Only the stopping of new applications provided the opportunity to begin to clear the backlog.

While activity is way down from the peak, Texas is anticipating getting more money for the program as the federal government reallocates unused money from other states. How much additional money will come and how many more families will receive assistance remains to be seen.

To date, more than 313,984 families have been helped by the program, and each receives an average of \$6,664 in assistance. In total, the program has paid out \$2,154,057,436.²

A concern that was raised early related to assistance for rural Texas. The federal government

structured the program so that local governments with 200,000 people received an allocation, and the state received an allocation. However, they could not neglect applicants from local governments that received money. So, a person in the local jurisdiction that received money could apply and receive benefits from either that local jurisdiction or the state. Because of outreach difficulties and less reliable Internet access, some were concerned that rural Texas might be neglected.

To test the concern, the committee staff enlisted the help of the Research Division at the Texas Legislative Council. We classified the local jurisdictions that received an allocation as "urban," and those that did not as "rural." While some may disagree with the classification, it did fit neatly with the program.

Committee staff wanted to determine whether rural Texas had received rent relief in proportion to its share of the total Texas population. The comparison revealed that rural Texas accounts for about 23.9 percent of the Texas population, but rural Texas only received 8 percent of rent relief dollars. (While the program is still ongoing, the numbers could change slightly. Given the relatively small amount of relief that is yet to be paid, one should not expect the change to be statistically significant.)³

A wide variety of reasons may be responsible for the difference. As explained, urban areas were given their own allocation, plus those residents could also apply to the state. It is possible that rural Texans rent and have lower incidence rates than urban Texans. Outreach in urban areas was often conducted by charities, churches, and other neighborhood groups, which may not have occurred to the same degree in rural areas. News reporting in urban areas may have been much greater than in rural areas. Much further analysis and data gathering would be required to answer the question of whether rural Texas receives proportional relief compared to urban Texas.

The Texas Homeowner Assistance Program

The American Rescue Plan Act provided up to \$9.961 billion nationwide to help homeowners who had fallen behind on their mortgages due to the economic effects of COVID-19. Texas' share of the money totaled \$842,214,006. Unlike the Rent Relief Program, no local government entities were allocated funds.

The money can be used to pay delinquent and some future mortgage payments, property taxes, homeowner association fees, utility bills, and insurance premiums.

The program's rollout was much slower than the rent relief program. Completed plans or notice of intent to submit a completed plan from the states was not due to the U.S. Treasury Department

until late August of 2021, about six months after the Act was passed.

The Texas Department of Housing and Community Affairs was designated the state agency to operate the program. After receiving approval from Treasury for its plan in late January of 2022, TDHCA announced the opening of the program on March 2, 2022.

The demand for the program has not been as great as the demand for the Rent Relief Program. About sixty days after opening the program, about \$19.2 million had been awarded to 2,800 families.⁴ About two months later, the total had risen to \$50 million in assistance, helping more than 7,000 families.

By late October of 2022, TDHCA has paid about \$200 million helping almost 21,000 families, for an average of \$9,751 in relief.⁵ Assistance to each homeownership household is more than \$3,000 higher than each renting household helped through the rent relief program. About 400 families have collected more than \$45,000 each, and another one thousand have collected between \$35,000 and \$45,000 each. The maximum any one household may receive under the program is \$65,000.

To help with outreach, TDHCA has contracted with 26 sub-recipients across Texas to provide help in the application process and provide housing and legal counseling.

Why the program seems to have lower demand is probably related to many factors. These may include lower homeownership rates than the national average, homeowners may have been less affected by economic losses due to COVID-19, and negotiating equitable terms with lenders prior to the program starting.

RECOMMENDATIONS

The Texas Department of Housing and Community Affairs should be directed to conduct a thorough analysis of the program's problems. It is conceivable that the federal government may implement a similar program in the future should another pandemic, major recession, or other event occur. The department should memorialize the difficulties it faced and the ultimate outcomes so that the lessons learned are not lost to future administrators and legislators.

The Texas Legislature should continue to monitor the progress if and the demand for the Texas Homeowners Assistance Program. The House Committee on Urban Affairs should request routine updates from the Texas Department of Housing and Community Development throughout the 88th Legislative Session.

CHARGE II: WORKFORCE HOUSING

Evaluate the availability of workforce housing to support the dynamic economic growth of the state. Study the use of public-private partnerships and other tools to incentivize the development of housing that meets Texas' expanding workforce demands. Develop and include measures to ensure accountability and transparency associated with these tools.

BACKGROUND

For decades, wages for U.S. workers have been fairly stagnant. Lower wage workers have been priced out of the housing market, especially for purchasing housing. The situation has begun to concern businesses and policymakers as workers have been harder to find, especially after the COVID 19 pandemic.

In many area across the country a familiar scenario has been playing out. Moderate-income workers needed in central cities are forced to live far away from their jobs to find housing that is affordable. Part of the issue is the cost of much of the housing being built. Builders have concentered on higher-end and luxury homes because the return on investment is greater than housing for average workers. Another part of the issue is where homes are being built.

Where affordable housing does exist..., it usually is located far from where most people work. In rapidly growing cities throughout the United States, most new affordable housing is being created in the outer exurbs, so this is where moderate-income families are being forced to live. This outward movement of population brings with it all the undesirable aspects of sprawl: grinding traffic congestion, school overcrowding, air pollution, and a loss of open space. Yet, most major institutions - governments, hospitals, and the like - are located near the central city and cannot move out to follow the workforce. This dynamic makes it harder to recruit moderate-income employees such as teachers, fire fighters, nurses, and so forth. Private businesses, on the other hand, are more mobile. Many are moving to the outer fringes to be closer to their workforce. While this might appear to solve the jobs/housing imbalance, it actually further compounds the cycle of sprawl by driving up land costs and forcing affordable housing further out.⁶

Resort communities were among the first in the nation to experience the problem. Wealthy

buyers from the country's major metropolitan areas would buy vacation or retirement homes in beach, ski, golf, and entertainment resorts. They often paid top dollar for existing housing or land on which to build luxury homes, usually close to the amenities that attracted them to the location. In doing so, they drove up the price of the housing needed by the moderate-wage employees necessary to operate the resort venues.

In some locations, geography limited the capacity to sprawl, and resort communities were forced to find methods to ensure that essential employees could live nearby even though they had been priced out of the market to buy or rent homes. The communities used various tools from deed restrictions, to low interest loans, creative financing, and even capping rates on profits on the resale of workforce housing.

By the early 2010s, homeownership has become unattainable for many "community workers." One study compared more than sixty occupations in more than two hundred metropolitan areas and found that most workers could not afford to buy a home.⁷

Simply put, middle-income workers like police officers, firefighters, teachers, health care workers, retail clerks, and others could not afford to buy or rent housing in the high-priced metropolitan regions in which they worked. This was due, in part, to the failure of their wages to keep up with the rising cost of living in these various regions. This situation was also spurred by the stagnation in the supply of houses affordable to these workers.⁸

As is typical, workers moved to the fringes of metropolitan areas, committing to longer commutes. Families suffered as parents spent more time commuting and less time with children. Employers found it was harder to keep workers that relocated to the outskirts.

To address these issues, cities and some states have begun to develop workforce housing initiatives to keep workers, especially "essential employees," in affordable housing near vitally important jobs. These initiatives are limited by funding, and in some cases legal constraints. From a practical standpoint, however, cities need to decide who should qualify for any workforce housing they develop.

It should be made clear that for the purposes of this report that while workforce housing needs to be affordable, it is not the same as affordable housing programs funded by the federal and state governments. There is, however, some overlap.

Traditional affordable housing programs target families earning eighty percent or less than the

average media income (AMI) for the community the family lives in. The target is for qualifying families not to spend more than thirty percent of their gross income on housing costs, including utilities. Even with government assistance, usually tax credits, for constructing apartments, many extremely and very low income families are priced out of the rental market.

The three income brackets are defined as follows:

- Extremely low income - 30% or less of AMI;
- Very low income - 50% or less of AMI, but more than 30% of AMI; and
- Low income - 80% or less of AMI, but more than 50% of AMI.

The State Low Income Housing Plan showed that in 2021, there were about two million Texas families considered extremely, very, or low income. These families would live in dwellings that include: substandard physical conditions, such as no kitchen or running water; cost more than thirty percent of the families income; or are overcrowded. Through the low income housing tax credit program, builders can construct housing affordable to those earning fifty to sixty percent of AMI.⁹

Builders report that the cost of building is just too great to charge a rent amount equal or less than thirty percent of the income of a family making thirty percent or less of AMI without taking a financial loss. Most housing authorities say that their greatest backlog of housing need is for the extremely low and low income populations.

The National Low Income Housing Coalition's 2022 Gap Report shows that in Texas there are only 29 affordable units for every 100 families at or below thirty percent of AMI. Texas has 51 affordable units for every 100 families earning fifty percent or less of AMI. In Houston, a city with a population of about 2.3 million people, there are only 87 rental homes affordable to a family of four at fifty percent of AMI. In San Antonio, there are only 20 rental homes for a family of four at fifty percent of AMI.

Texas Housers testified that Houston's population of service worker professionals will increase by almost 105,000 over the next six years, and they will earn 30 to 40 percent of AMI. For San Antonio, more than 50,000 people will become retail salespeople and earn 30 to 40 percent of AMI for that city.

The situation may be most drastic in Austin, which has seen incredible growth. The average rent in Texas increased twenty-two percent last year, while the rest of the country saw a fifteen percent increase. For Austin, however, rent increased 46 percent.¹⁰ The fastest growing

occupations in Austin are customer service representatives, office clerks, retail salespeople, fast food and counter workers, and waitstaff. These jobs will pay between 24 and 41 percent of AMI. At those income levels they will be able to pay between \$492 and \$920 per month in rent.¹¹ In October of 2022, the average rent for a one-bedroom apartment in Austin was \$1,650.¹²

Tax credit programs are an excellent example of public/private partnership attempting to resolve a public policy issue. Government provides tax credits, and private businesses sell the tax credits to raise financing for units they will build and own. The businesses then rent units to eligible families.

While low income housing is a substantial problem that needs greater resource to resolve, many workers and working families fall within the traditional income qualifications of affordable housing programs. Workforce housing needs encompass these families and many others.

The term "workforce housing" is somewhat fluid, and there is no national standard for determining who needs or should qualify for such housing. Some argue "workforce housing" is "housing that fits the budget of the median-income household in a community." Others might describe it as "housing that is affordable to working families and individuals who do not qualify for housing subsidies."¹³

Most researcher seem to agree that families should not pay more than thirty percent of their gross income on housing, including utilities. They believe that standard is a good measure of affordability. The Urban Land Institute, which has done considerable research into workforce housing, defines workforce housing as affordable to households earning between 60 and 120 percent of AMI.¹⁴ Local programs may narrow or widen the range, or add other qualifying conditions, depending the local need.

While technically affordable housing programs can promote renting or buying, in reality most of the financial resources for the programs goes to renting. While there are programs to help low income people purchase homes, the numbers are relatively limited. The Texas Department of Housing and Community Affairs' Texas Homebuyer program helped about 9,300 families with mortgages or mortgage credit certificate products. Considering that over the next few years Texas will add hundreds of thousands of lower income workers, and assuming most would rather purchase than rent, helping fewer than ten thousand per year is a modest number. The program is not inefficient or ineffective, it is just underfunded given the demand.

Testimony revealed that the median home price in the Houston metropolitan area in 2022 was \$282,000, which would require an annual income of about \$80,000 to buy under normal

conditions. But, the median household income in the area is \$53,600,¹⁵ which is about \$27,000 less than the income traditional lenders would require. So, the income required to buy the average house in Houston is 150 percent of the average family's income.

For Texas's metropolitan areas, there is a considerable gap between what the average working family can afford and what the average house costs. Workforce housing initiatives will have to determine whether the goal will be to help working families find affordable rent, or help the purchase an average home. There will undoubtedly a substantial cost difference between the two goals.

In general, almost half of Texans spend more than thirty percent of their income on housing costs. This includes about a quarter of families that own homes. So, whether they are renting or own, Texans are paying larger portions of their income to housing than they have in previous decades.

The reasons housing costs have outstripped many workers wages are myriad. The current market has been volatile because of the pandemic and interest rate increases. During the pandemic builders were not able to construct as many homes as they had previously because of worker illnesses and social distancing restrictions. Additionally, customers were unable to view homes and met to develop financing and finalize mortgages.

Many people with existing mortgages could not make payments, and due to eviction moratoria, mortgage lenders could only hold on to the nonperforming loans. So, even though interest rates were very low due to attempts to stimulate the economy, homebuying was a slow and difficult process.

Though the pandemic limited opportunities to buy, the growth in demand for housing continued to grow, and became pent up. Once the pandemic's restrictions were lifted, potential homebuyers rushed into the market and drove prices up quickly, contributing to inflation. Prices for homes and other goods grew so rapidly that inflation became a concern throughout the economy as producers could not ramp up production fast enough to meet demand. To cool the economy, the Federal Reserve has substantially and steadily increased interest rates, thus limiting the number of buyers for most products, including homes.

The pandemic and the resulting effects accounts for the recent volatility in the housing market, but home prices have been outstripping wage growth for decades. Population changes are a big part of the increased demand. Texas had reputation as an affordable state to live in. Texas has been slightly more affordable than the national average, but as more people move into the state,

prices continue to climb. The state's metropolitan areas are feeling the impact hardest.

Until the pandemic, the Texas economy was expanding at a rapid rate, with job creation running about 2.5 percent, well ahead of the national average. The job creation, in turn, attracted more people to move into the state, averaging about 1,100 per day for several years before the pandemic hit. Obviously, this in migration, combined with Texas' natural population growth rate, increased the demand for homes. The vast majority located in Texas' metropolitan areas or the surrounding suburbs.

As people flooded into certain areas of Texas, land costs increased substantially. Developers always seek the best locations, nearest to jobs, good schools, and roads. Sellers knew demand was increasing, and developers were willing to pay more for land on which to build homes.

As demand has increased so has building costs. After the Great Recession of 2008, which was caused substantially by problems in the sub-prime housing market, economic activity shrank. Builders laid off tens of thousands of construction workers, and many never returned to building. The shortage of construction workers increased competition among builders and forced wages upward. Those higher wages added to the cost of construction.

Government has also played a part in increasing home costs. Zoning ordinances, which control how land can be used, and construction standards can remove desirable tracts of land from development potential, and drive up prices for the remaining land. Some testimony complained that in some areas zoning ordinances were enacted to limit development rather than improve safety. Periodic upgrading of construction standards have also increased the cost of construction.

Increased costs have made the construction of entry-level single families homes less profitable for builders. Consequently, builders generally construct larger, more expensive homes with more luxurious amenities, which are more profitable but also out of the reach for most Texas families.¹⁶

Texas's heavy reliance on property taxes has also contributed to workforce housing issues, even though the Legislature has periodically brought down property tax rates. School district ad valorem taxes make up the largest component of a tax bill, accounting for about sixty percent of the total bill.

In addition to budgeting more of state revenues into school finance formulas and mandating the lowering of school tax rates, the Legislature has also increased the homestead exemption. The homestead exemption eliminates part of homes value from taxation. Today, the homestead

exemption for school tax purposes is \$40,000, with an additional \$10,000 exemption available for homeowners age 65 or older, or disabled. So, for a home at the median price of \$325,000, only \$285,000 of the house's value is taxable. So, the home receives a 12.3% tax reduction because it is a homestead.

Texas also caps the amount the taxable value the homestead can increase to ten percent per year. This further reduces the taxes collected from some of the state's most valuable properties. It does however, protect some homeowners from rapidly increasing tax bills.

Economists generally believe that such schemes shift the tax burden within a jurisdiction. When a taxing entity loses revenue through exemptions and caps, revenue may need to be made up by increasing the tax burden on the remaining taxpayers, in this case renters and commercial property owners.

About thirty-eight percent of Texans rent their homes. Each year, their landlords are taxed for the full value of the property and there is no cap on the amount the appraised value can increase. While landlords are responsible for paying the tax, they generally include the tax in the price of the rent. While both an apartment or rental house serves the same purpose as a homestead, the two are taxed at very different levels.

To further exacerbate the difference, homeowners can also deduct their property tax payments from their income taxes. Renters cannot deduct the portion of their rent that goes to paying property taxes from their income taxes. The disparate tax treatment almost certainly increases the cost of renting a home or apartment, making it more difficult for low and moderate income workers to find affordable housing near their work.

For about twenty years, state legislators have been perplexed by the difference in the treatment of homeowners and renters in tax policy. If Texas were to extend an exemption equal to the homestead exemption to rental properties, there is no simple option for ensuring the tax relief would "trickle down" from landlords to renters, especially in competitive markets with rising rental rates. While many legislators would like to find a way for the nearly forty percent of families who are renters to get taxation relief, no solutions have yet presented themselves.

While the pandemic has contributed mightily the current workforce housing shortage, the increasing separation between what the average Texas family can afford and price of homes has been growing for decades. While increasing costs of housing construction inputs and government regulation and taxation have added to the increase cost of housing in Texas, the demand for housing created by in migration, immigration, and increasing urbanization, probably account for

most of the increase in cost. Regardless of the reasons, nearly half of Texas families spend more than thirty percent of their income on housing and associated costs, making these families "cost-burdened" by most standards.

Some local communities have begun to respond to their workforce housing issues, but in limited ways. Some have assessed their lot size requirements to increase housing density, or rezoned areas designated for single-family homes to permit multi-family buildings. The success of changes often hinges on area residents' willingness to accept changes.

Other cities have experimented with other options. Some have added loans or other funding to leverage the state-administered federal tax credit programs. These are generally expansion to assist with affordable housing, rather than workforce housing. Due to increased homelessness many Texas cities have prioritized assisting their poorest residents find housing. Pairing local dollars with federal tax credits enables the creation of more units, but only for those with affordable housing program eligibility.

Still other cities have examined seeking certain special tax increment financing options currently open to commercial enterprises. Others would like to state to develop a public/private partnership program similar to the 4% Tax Credit Affordable Housing Program, but expand the eligibility criteria. Such an expansion would have to be financed exclusively with state dollars because the expanded eligibility would not qualify for federal funding.

Some businesses have considered the workforce housing problem significant enough to try to develop their own solutions. In Cactus, Texas, meat processing plant owner JBS USA Holding, Inc. designed a program to develop housing near its plant. The company already operates apartment complexes for employees in the area, and has a waiting list of employees seeking apartments. JBS paid a builder to cover development costs, and gets paid back when the property is sold to an employee. JBS also covers closing costs for the employee. The employee must commit to staying with JBS for two years.¹⁷ Land costs in the rural community, may have been considerably lower than in an urban or suburban areas.

Large employers may have the capacity to help build apartments or houses for employees, and consider such costs a benefit to attract and maintain workers. Small businesses with smaller margins would find such benefits very difficult to offer. It is difficult to imagine that restaurants or small retailer, who may be employees just as badly, finding the resources to develop such programs.

The gap between wages and home prices has been expanding for decades. The pent up demand

for housing increased prices rapidly as the economy reopened after vaccines increased immunity or decreased the severity of COVID 19 cases. While the federal government and the Federal Reserve have taken actions to slow the economy, the ultimate impact of those actions on housing prices is still evolving. Regardless of how well these temporary measures may work, it is inconceivable that they will reverse the trend that has been building for years.

The problem is already impacting economic activity as employers continue to have difficulty finding employees. Housing isn't the only reason for the worker shortage, but it is a consideration workers evaluate when determining where they will work.

RECOMMENDATIONS

The Texas housing market and home prices are influenced by a very complicated mixture of population trends, economic factors, and federal, state, and local government policy. Texas is facing a workforce housing problem that many consider a crisis. The current post pandemic economic volatility only increases the uncertainty in the housing market.

Because of the complexity of the influencing factors, the housing industry's importance to the Texas economy, and the employment issues the lack of housing will create for some vital industries, the Legislature should appoint a broad commission of state and local government lawmakers, state and local housing officials and workforce development officials, and leaders of various industries, especially the home building and service industries, to comprehensively assess the regulatory and tax environment that contribute to the increasing gap between housing prices and average wages.

Texas' appropriations for affordable housing are insufficient to address the problems of families with incomes below eighty percent of the average median income in their area. The Legislature should consider appropriating additional money to assist families who earn between 60 and 120 percent of AMI, find housing, including utilities, that does not require more than 30 percent of their income. One option the Legislature should consider is establishing a \$50 million revolving fund for the construction and rehabilitation of workforce housing, especially if construction worker training can be included.

CHARGE III: MMD

Review the Municipal Management District Legislative Template with respect to representation and accountability. Make recommendations for improving the template.

BACKGROUND

Review the Municipal Management District Legislative Template with respect to representation and accountability. Make recommendations for improving the template.

Municipal management districts are created to help property owners develop land for numerous industrial, commercial, and residential uses. A district is given the power to levy assessments on property, and with that authority, the district borrows money by floating bonds to pay for the construction of infrastructure and other improvements. Because the payment of assessments is mandatory, the district can secure more favorable financing terms from lenders than property owners would if the district did not exist. Essentially, future assessment payments back the bonds rather than just the value of the land or any improvements.

The creation of a district enables development to occur with much less upfront capital on the landowners' part, yet provide additional security for bondholders lending money to the district. Municipal management districts (MMD) provide an efficient method for financing economic development projects. While the Houston area has seen the most concentrated use of MMDs, recently the use of such districts has expanded to other parts of the state, multiplying and diversifying economic growth.

While there is an administrative method for creating districts using Chapter 375, Local Government Code, most landowners and developers have chosen to have districts created legislatively. The method is simpler, and legislation creating districts can be better tailored to the needs of the area much better than administrative codes. Landowners and developers feel they can better shape the financing, use of property, infrastructure development, and other amenities through designing legislation rather than dealing with administrative codes.

The drawback is that there may be some delay in starting a district because the Texas Legislature meets only every other year, and bills creating new MMDs can only be passed while the Legislature is in session. However, the administrative process can be lengthy, too, so most landowners and developers seem to be willing to wait until a legislative session to get the exact authority they want.

As the number of bills requesting the creation of MMDs began to rise, the House Committee on Special Purpose Districts looked at trying to create more uniformity in the construction of such bills. The committee recommended House committees with jurisdiction over the creation of MMDs consider using a template format for drafting and considering passage of MMD bills.

The Special Purpose Districts Committee made clear that the template was to help committee members evaluate the structure and authority of bills creating districts, but that each member introducing a bill would be free to deviate from the template as needed. Different landowners and developers may need different authority depending on the local economic environment. The committee recognized that a "one size fits all" approach would unnecessarily restrict some districts' authority, while grant other districts more authority than the owners wanted or needed.

Since the Special Purpose Districts Committee made its recommendation, most bill authors have drafted bills using the template, but deviating where they thought necessary. The template has given the committees considering new MMDs the ability to determine when a bill was requesting greater authority than is traditionally given to MMDs. Authors have generally been able to justify the requests for additional authority based on meeting some unique local need.

The governing structure of MMDs is generally that the owner or owners of a majority of the assessed property within the district nominate a slate of board members and submit the slate to the city with jurisdiction over district. Once the city approves, the board members serve staggered, four year terms. As terms end, the board submits to the city candidates to replace board members whose terms are ending. Board members can be renominated. Board members generally serve without compensation.

As the district constructs infrastructure, existing landowners may wish to sell parcels of land. The new purchasers must be made aware of the obligation to pay any assessments that district imposes. With such information any prospective buyer should be aware of the governance structure, and he or she can determine whether they wish to continue with the purchase.

Recently, some interested parties have raised concerns about the continuation of MMDs after the original purposes for which the districts were created have been met. They argue that boards sometimes find additional tasks in order to continue the assessments and thereby the existence of the board, even though many, perhaps even a majority of property owners, may not want those tasks performed. It is possible, for example, that a board will expand spending by the MMD to include new infrastructure projects or services, like police presence, as bonds are paid off.

As long as the tasks are within the purview of the board, then question of whether the board

should take on the task is a question for the board and legislative intervention is probably not warranted. However, for districts created by legislation, that legislation may be amended as the Legislature sees fit. Owners dissatisfied with a board's action can ask the Legislature to intervene. The Legislature should consider such legislation as it does bills that create districts.

When a district is created, it is often impossible to determine each bit of authority that may be required over the existence of the district, which can be for decades just to pay off any bonds. It is not uncommon for districts created by legislation to request the Legislature expand of the district's authority. Just as a district or individual owners can ask the legislator representing the area in which the district is located to expand the district's authority, an individual property owner can ask the legislator to carry a bill restricting the district's authority.

Because board members do not stand for election by property owners, some argue that property owners are denied a direct say in who is appointed to the board. Because MMDs are usually created from territory that is raw, unimproved land, initially there may be only one property owner, be that an individual or a company, which makes initial elections unnecessary.

Municipal management districts, by law, are not democratic institutions where any eligible voter can elect a director. Rather MMDs more closely resemble an association of land owners. How much an individual property owner pays is determined by the value of that owner's property. Property owners who buy within the district accept the terms of the district, for better or worse.

They can appeal to the governing body of the city to reject board members who are unacceptable, or ask the Legislature to amend the statute regulating the board to remove offensive provisions.

Another option for disgruntled landowners is to try to abolish the district. If, however, the district has outstanding bonded indebtedness the district continues to exist for the purposes of paying off the debt, regardless of whether all the criteria for dissolution are met. Sec. 375.262, Local Government Code, DISSOLUTION BY PETITION BY OWNERS, states:

Except as limited by Section 375.264, the board shall dissolve the district on written petition filed with the board by the owners of at least two-thirds of the assessed value of the property subject to assessment or taxation by the district based on the most recent certified county property tax rolls.

Some interested parties argue that the two-thirds requirement is too high and should be reduced to something closer to fifty percent. In 2019, the Legislature reduced the threshold from seventy-

five percent to the current threshold of at least two-thirds. Supporters of the current statute argue that the two-thirds standard guarantees stability for the payment of the district's liabilities. They believe that stabilities enables them to access lower interest rates and lower prices because obligations cannot be cancelled easily. Still others argue that a simple majority is sufficient should be enough to determine whether the district should continue to exist, especially since bondholders' interests are safe regardless of whether the board is abolished by a landowner petition.

The law also provides that the city may abolish a board if not less than two-thirds of the governing board votes to abolish the district. The city would assume responsibility for the debts and obligations of the district.

RECOMMENDATIONS

Committees referred legislation creating a new municipal management district should continue to use the existing template to assess legislation and determine when legislation asks for more or less authority than the template lays out. The template and the legislative process currently offer sufficient flexibility and opportunities to influence any statute creating a new municipal management district.

- As the House Committee on Special Districts concluded:
While a template is useful for evaluating requested powers it does not mean that every district must conform to the template. While a common baseline is appropriate, each district is unique and meant to serve the needs and desires of the local citizens. Districts will still have the ability to request powers not granted through the template and template language is not meant to preclude districts from having powers necessary to accomplish their goals. Instead, template language is meant to reduce carte blanche grants of authority and provide a clean and efficient 40 form for districts as they first come before the legislature.

Committees referred legislation modifying a municipal management district created by special law should assess such legislation individually, using the template as a guide but not a requirement.

CHARGE IV: MUNICIPAL WATER & WASTEWATER INFRASTRUCTURE

Study the effects of local governance, planning, and administration on the current state of municipal water and wastewater infrastructure. Examine the measures municipally owned utilities have taken and the costs required to maintain and improve that infrastructure. Make recommendations for cost-effective solutions to ensure reliable infrastructure and uninterrupted municipal utility services, especially during a severe weather event.

BACKGROUND

Water and wastewater service are critical to the health and safety of any community. Most Texans living in urban and suburban areas can generally take the low cost and reliable delivery of clean water and the proper disposal of wastewater for granted. As we have learned during the Coronavirus pandemic, disease can spread rapidly in population centers when each person may interact with dozens or even hundreds of people each day.

Clean water is essential for drinking, bathing, and washing hands to contain the spread of diseases. Equally important is the sanitary disposal of wastewater, which if left untreated, can cause diseases. But the systems necessary for the purification and handling of water and wastewater are extremely complex, but most Texans rarely give those system much thought, unless water doesn't come out of the tap, has to be boiled before use, or toilets cannot flush. It can be argued that without clean, reliable service communities cannot prosper, economically or healthfully.

Disruptions to water supplies are not merely an inconvenience, but can be a threat to a population. Texas water utilities must deal with a variety of circumstances that can interrupt service. Some are weather related, while others may be related to the failure of equipment that is directly and indirectly necessary to the providing of clean water.

Water systems are made up of a complex network of treatment facilities, pumping stations, thousands of miles of pipe for both clean water and wastewater, and meters. Major systems will have hundreds of people working each day to monitor cleanliness and sanitation, the distributions system, and repair breakages when they occur. The systems are extremely intricate and perform very efficiently the vast majority of the time.

Events like hurricanes, tornados, flooding, freezes and droughts can impact a water utilities' ability to provide clean water, even if the event does not directly impact the water system. Winter

Storm Uri was a classic example. The storm did freeze some water infrastructure, but much of the loss of service was caused by the loss of electricity to run pumps and water treatment facilities. When houses, apartment buildings, and commercial buildings lost electricity, the lack of heating caused pipes in many of those buildings to freeze. (Even homes heated with natural gas require electricity to operate fans that move the heated air and vent the byproducts of burning gas.)

As outdoor temperatures warmed, pipes burst resulting in not only flooding structures, but increased demand overall until the water could be shut off at the meter. Many Texans had no idea how to shut off water coming into their homes or even where their meters were. According to many water utility officials, most of the water problems caused by Winter Storm Uri were not related to the water systems themselves, but rather due to the loss of electricity to water systems and to homes and businesses.

While isolate weather events like hurricanes, floods, and drought have compromised water systems in a city or one area of the state, Winter Storm Uri and its concomitant electricity loss affected virtually every part of the state simultaneously. Uri exposed critical weaknesses in much of the state's vital infrastructure for days.

In response to Uri, the Texas Legislature passed Senate Bill 3, relating to preparing for, preventing, and responding to weather emergencies and power outages; increasing the amount of administrative and civil penalties. While much of the bill dealt with preparing Texas's electric system and natural gas distribution system for the future events, the bill also imposed new weatherization and hardening standards on water utilities.

Section 13.1394, Water Code, was added to outline expected performance standards of water utilities, and to place the Texas Commission on Environmental Quality (TCEQ) in an oversight position of emergency preparedness plans developed by water utilities. Most importantly, the section requires that water utility "ensure the emergency operation of its water system during an extended power outage at a minimum of 20 pounds per square inch...as soon as safe and practicable following the occurrence of a natural disaster."

The section also requires that water utilities adopt and submit to the TCEQ an emergency preparedness plan that demonstrates the utility can provide service in emergency situations, along with a timeline for implementing the plan. If the TCEQ finds the plan acceptable, it approves the plan. The plan must provide for the following:

- (1) the maintenance of automatically starting auxiliary generators;

-
- (2) the sharing of auxiliary generator capacity with one or more affected utilities, including through participation in a statewide mutual aid program;
 - (3) the negotiation of leasing and contracting agreements, including emergency mutual aid agreements with other retail public utilities, exempt utilities, or providers or conveyors of potable or raw water service, if the agreements provide for coordination with TDEM;
 - (4) the use of portable generators capable of serving multiple facilities equipped with quick-connect systems;
 - (5) the use of on-site electrical generation or distributed generation facilities;
 - (6) hardening the electric transmission and distribution system serving the water system;
 - (7) for existing facilities, the maintenance of direct engine or right angle drives;
 - (8) designation of the water system as a critical load facility or redundant, isolated, or dedicated electrical feeds;
 - (9) water storage capabilities;
 - (10) water supplies delivered from outside the service area of the affected utility;
 - (11) the ability to provide water through artesian flows;
 - (12) redundant interconnectivity between pressure zones;
 - (13) emergency water demand rules to maintain emergency operations; or
 - (14) any other alternative determined by TCEQ to be acceptable.¹⁸

The major metropolitan water utilities have all reported to the committee that they have submitted the plans and the plans were approved. The plans, however, call for significant investments over the next few years, amounting to hundreds of millions of dollars. Senate Bill 3 mandates a higher level of performance during a natural disaster than was required prior to the passage of the bill. However, the bill itself did not provide money for any of the improvements that water utilities will have to make.

San Antonio Water System (SAWS) estimated that just cost of purchasing and installing backup generators would cost about \$131 million, and approximately \$200 million will be over the next seven or eight years to meet all the requirements. Of course, these costs will be in addition to the normal operating and repair costs the water utility faces every year as older pipes and equipment fail, and the planned infrastructure improvements and expansion that comes with being a growing city. Ratepayers will ultimately have to cover these costs.

SAWS also testified that TCEQ interpreted SB 3 to mean that being designated "Critical Load" was not sufficient to comply with the bill. (A critical load designation means that electric providers must avoid cutting off electric service to that customer during a disaster. Hospitals and

other vital organizations file these designations with electric providers so they can maintain operations.) So, utilities must develop other sources of onsite backup generation capacity across dozens of facilities.

There are, however, significant technical and financial challenges that accompany the requirement. Micro-grids are possible, but take time to develop and require a good deal of coordination, of then with the electric utility that isn't providing service in a disaster.

Onsite natural gas generators are also a possibility, but the failure of the natural gas delivery system was one of the primary causes of electrical outages during Uri, so it may not be the most dependable option. Many sites may not have sufficient space to place a generator onsite, so additional land may be necessary, perhaps purchased through the condemnation process. Easements may also have to be purchased to run gas lines to the facility.

Diesel generation may run into the same space issues, and it requires diesel to be stored onsite, perhaps over environmentally sensitive areas. Storing enough diesel to run generators for several days would involve larger tanks, and unconsumed diesel would have to change periodically. Refilling tanks could be difficult in dangerous driving conditions.

SAWS also notes that had the natural gas and electric systems been more reliable, many of the water issues would have been avoided.

Austin Water made similar comments regarding Winter Storm Uri but added its area faces flooding issues that can disrupt water operations. Heavy rains wash soil and silt into area lakes and increase the turbidity of the water. If the water's cloudiness exceeds the capacity of water treatment facilities, a boil water notice must be issued. Austin Water is investing \$12 million to better handles such events.

In Winter Storm Uri, Austin Water had many lift stations go offline when electricity to those stations was cut. The same also occurred at one of the city's water treatment plants. Burst pipes made it very difficult to keep the water pressure up as water poored into unoccupied buildings and homeowners couldn't determine how to shut the water off at the meter. In accordance with regulations, Austin issued boil water notices, and for the entire city, for some parts of the city, the notice lasted seven days.

Austin Water is estimating the improvements necessary to deal with its flooding issues and other emergency preparedness investment will total about \$400 million.

Houston Water was already working on two resiliency and conservation plans when Winter Storm Uri struck. Between 2015 and 2020 the region suffered six flooding disasters, including Hurricane Harvey. The COVID-19 pandemic challenged Houston Water, as it did most water utilities, by forcing workforce adaptations as essential workers became ill.

Taking lessons from all these events, Houston Water had planned or implemented many of the weatherization and system hardening measures called for in SB 3. The utility also has a list of additional measures it plans on taking. Houston Water did not provide the committee with an estimate of the costs to implement SB 3.

The City of Dallas Water Utilities (DWU) operates a very complicated system for Dallas and thirty suburban cities, with a population of about 2.5 million people. The system has 5,000 miles of water mains, 4,000 miles of sewer lines, and 2,000 miles of storm sewers. With such a large system, the utility averages about 1,100 main breaks per year, or about 3 per day. Pipes fail because of the material used, the age of the pipe, water pressure issues, the expansion and contraction of soil, and construction and digging activity.

For the seven-day period around Winter Storm Uri, the utility experienced 324 main breaks or about 36 per day. The sudden loss of electricity caused pressure surges that broke many mains. During the storm, DWU continued service throughout its service area, even with the breaks. The utility spent between \$150 million and \$170 million per year over the past 20 years making improvements to make its system more resilient.

SB 3 will require more improvements to the system. The backup generators will cost approximately \$131 million at 21 essential pump stations, and the technical issues mentioned earlier will also face DWU. The utility also estimates it will cost about \$200 million to install power generators at its treatment plants, which require three times more power than pumping stations.

The Fort Worth Water Department was not as fortunate as its neighbor during Winter Storm Uri. Demand jumped to 380 million gallons per day from 150 million gallons per day under normal conditions. Like other utilities the demand spiked when pipes burst in unoccupied buildings or customers could not shut water off. In the department's system about twenty percent of the pipe is cast iron, and those pipes account for about 85 percent of the main breaks. Boil water notices were required for the utilities North and West service areas. About 300,000 were affected.

The department estimates that it will need to spend about \$180 million to implement the measures in SB 3. In addition to the other obstacles mentioned in meeting SB 3's mandates, the

department also mentioned workforce concerns. It noted it has an aging workforce and finding skilled workers is difficult. The department also noted that it and all utilities face constant cyber attacks.

The major water utilities outlined the resiliency issues they are facing with the implementation of SB 3. These water utilities do not make up the entire water system. Generally, their responsibility ends at the water meter. From the meter into a building and throughout the building water pipes is the responsibility of the building owner.

Whether a house, a factory, or a skyscraper, if heat is lost due to power outages pipes are likely to freeze and burst. When that occurs, it will be difficult to keep a water utility to keep constant pressure through a city until the water supply to the leaks is shut off.

While this report details the testimony the committee received from the major urban utilities in the state, there are many more utilities facing the same problems. The major utilities in this report, excluding Houston which did not provide an estimate, detailed about \$1.1 billion in expenses to meet the requirements of SB 3. Some of the work required by SB 3 may have been done regardless of whether the bill passed to ensure the utility could serve its customers, however, the bill will require utilities to spend significant amounts of money, and ultimately ratepayers will pay for it all.

The additional spending will increase the cost of service, the cost of living, and the cost of doing business in Texas. But the state should have more reliable water delivery during disasters.

RECOMMENDATIONS

The Legislature should consider measures to help utilities defray the cost of reliability and resiliency improvements.

The Legislature should require routine reporting by the Texas Commission on Environmental Quality on the progress water utilities make toward meeting emergency preparedness plans and the costs incurred.

CHARGE V: MUNICIPAL FEES

Study municipal fees with respect to the function of the fee and the relationship of the fee to the cost of providing an associated municipal service. Make recommendations to address municipal fees that are disproportionate or unrelated to the cost of providing the associated service.

BACKGROUND

Texas cities often impose fees to help cover the cost of certain regulatory regimes. Texas generally has two types of cities - general law cities and home rule cities - that determine if a city can impose a fee. General law cities are smaller in population, usually 5,000 residents or fewer, and may adopt ordinances and regulations "not inconsistent with state law...." Once a city's population exceeds 5,000, the city is eligible to hold an election to approve a home rule charter. A home rule charter grants the governing board its powers and duties, and can "do anything that is not specifically prohibited by state law."¹⁹

Generally, "A home rule city may do anything authorized by its charter that is not specifically prohibited or preempted by the Texas Constitution or state or federal law. A general law city has no charter and may only exercise those powers that are specifically granted or implied by statute."²⁰

Both types of cities are granted their overall powers by Section 51.001, Local Government Code, which states:

The governing body of a municipality may adopt, publish, amend, or repeal an ordinance, rule, or police regulation that:

- (1) is for the good government, peace, or order of the municipality or for the trade and commerce of the municipality; and
- (2) is necessary or proper for carrying out a power granted by law to the municipality or to an office or department of the municipality.

With respect to establishing and charging fees, the Texas Constitution places some parameters on a city's actions. Article XI, Sec. 5, Texas Constitution, says that for home rule cities "no tax for any purpose shall ever be lawful for any one year, which shall exceed two and one-half percent." Stated another way, a tax may not exceed \$2.50 per \$100 of valuation. Article XI, Sec. 4, Texas Constitution, sets the rate for general law cities at no more than one and one-half percent.

Article VIII, Section 1, Texas Constitution, authorizes the Legislature to impose occupation tax

on people and business doing business in the state, except for those in mechanical and agricultural pursuits. It also authorizes local governments to impose occupation taxes, but those "shall not exceed one half of the tax levied by the State...." If the state has not imposed a tax on an occupation, any tax imposed by a local government on that occupation would exceed the limits of the constitution, and be unauthorized. The importance of this limit will be made clear shortly.

Some fees are authorized by state statute, and often those statutes determine the maximum amount a city may charge. For example, court technology fees and building security fees are authorized under such statutes and the amounts of the fee are capped. Other authorized fees include solid waste disposal service fees, concession fees, municipal court fees, and impact fees. Still other fees have been "carved out" of authority granted by courts or the attorney general. These include health inspection fees and parking fees.

A framework has developed, through court decisions mainly, for cities to consider before they adopt a fee ordinance or set a fee. First, is the purpose of the fee to advance a public purpose? What constitutes a public purpose is not clearly defined, and has evolved over time. Generally, the purpose should be beneficial to the city's residents and within the scope of municipal government.

Second, the fee should only raise enough money to pay for the program established to administer the advancement of the public purpose. Charging more than is necessary to run the program could change the fee to a prohibited tax.

In some cases fees that collect more money than is necessary to run the program could be considered an "occupation tax." If a fee were on a specific industry, such as billboards, and the fees were in excess of the amounts necessary for regulation, the fee could be considered a general tax on the billboard advertising industry. Thus it would be a tax on the "occupation" of billboard advertising. If the state has not authorized a tax on the occupation of billboard advertising, any local tax would be in excess of the limit in Article VIII, Section 1, Texas Constitution, and would be unauthorized.

The courts have applied a reasonableness standard to determining whether a fee amount is appropriate and constitutional. As the Texas Supreme Court noted in 1935 in *City of Ft. Worth v. Gulf Refining Co.*:

As to the reasonableness of a license fee, the rule is that the sum levied cannot be excessive nor more than reasonably necessary to cover the costs of granting the

license and exercising proper police regulation; or, as stated in another way, the sum levied should bear some reasonable relationship to the legitimate object of the licensing ordinances. McQuillin on Municipal Corporations (2nd ed.), vol. 3, p. 483, sec. 1102; Texas Jur., vol. 27, p. 893, sec. 47.

The courts have further opined that a fee that is fair and reasonable for one type of business may not be for another type. The courts have also stipulated that the "burden of proof" of excessiveness is on the one who asserts it. The courts generally defer cities in these cases, unless "unreasonableness" is demonstrated.

Thus, at the risk of greatly oversimplifying the statutory regime, for a city to impose a fee, the fee must be permissible, and within limits laid out by the Texas Constitution and the Legislature, and the amount of the fee must be reasonably necessary to cover a regulatory program, and should not be designed to raise revenue for a purpose other than the regulatory program. Whether a fee is excessive is a "finding of fact" and the burden of proof is on the complainant.

Beyond the legal structure, fees have an impact on the costs of the activities they regulate. Fees will undoubtedly increase costs, perhaps slightly, perhaps significantly. City commissioners and alderpersons must weigh the increased cost to consumers with the benefits regulations brings. Not surprisingly, people's opinions will differ on whether the benefits are worth the additional costs, and whether fees are appropriate.

The Texas Legislature has historically let city councils decide these issues within the broader parameters laid out in the constitution and statute, generally believing that the government nearest the people are best qualified to make such decisions. More recently, however, the Legislature has begun to exercise more control over city councils, primarily through budget constraints and spending on specific items, like law enforcement. Whether the recent trend continues remains to be seen. Either way, the limitations on fees are fairly clearly laid out.

Still, occasionally cities will stray outside those limits. Given the number of municipalities and the number of fees each charge, legal challenges to certain fees seem to be rare. Still, when an excessive fee occurs, the businesses and industries which must pay the fee, and ultimately the purchasers of the goods and services those businesses provide, may face considerable additional and unnecessary costs.

Most cities will try to comply with constitutional and statutory limits because they genuinely

attempt to comply with the law. Additionally, exceeding those limits may result in costly legal challenges and repayment of improperly charged fees. Any loss in court undermines the credibility of city government generally, and the individual commissioner's reputations. Thus, most cities will seek legal council, analyze the reasonable costs, then impose fees within the legal parameters.

Some cities have imposed fees not just to regulate certain activities, but to curtail or eliminate those practices. In these cases, the greater the fees, the greater the curtailment of activity. Some have argued that they are simply attempting to stop an activity that most of the city's population find undesirable. If, however, those activities are legal, establishing regulations or fees to eliminate those activities may make the fees illegal.

Some cities may be willing to risk losses in court in order to regulate that activity, knowing that the activity's practitioners must face upfront legal costs to challenge the fees. Unfortunately, the regulated businesses must weigh the costs of the fees against the cost of a legal challenge and the costs of a potential loss in court. Many argue that the overall scheme is unfair because an individual or a few businesses must fight the collective force of government financed by taxpayers' money.

In some cases, certain industries have asked the Legislature to prohibit cities from imposing certain regulations and fees, rather than going to court. In some of these cases, the regulations were legally imposed, but the industry convinced legislators that local governments were not the most knowledgeable regulatory entity or that those regulations had an impact well beyond the municipality imposing the regulation. In other cases, the regulations and fees themselves may have been illegal, but the industries could resolve the issue faster by obtaining legislative intervention.

While witnesses reported a few fees they believed were unreasonable, none suggested changes to the current constitutional or statutory limits or the criteria that courts use to determine whether a fee is excessive or illegal. Some fees are or will be challenged, while other fees may not be challenged because the fee, while perhaps excessive compared to regulatory costs, the overall cost of the fee is insignificant.

The Texas Legislature could attempt to find a less costly administrative method for judging the appropriateness of fees. The Legislature has imposed such systems, mostly when there is a state agency that generally regulates the activities of an industry. Because cities are political subdivisions of the state, the Texas Legislature generally established the limits of municipal power, and the courts adjudicate complaints. Whether the severity or number of challenges

warrants creating a new entity to adjudicate cases administratively is certainly debatable. That additional layer could lengthen a process that generally calls for posting notices of consideration, invites public testimony, and a couple of affirmative votes by the city commission, perhaps delaying a community's response to some problems. In the long run, it may be simply more efficient for the Legislature to intervene to restrict local regulations when it finds an individual case offensive, as the Legislature has done in the past.

RECOMMENDATIONS

The Texas Legislature should continue to monitor local governments' imposition of regulations and fees, and court cases that interpret the existing parameters for imposing regulations and fees. Should the Legislature find municipal regulation inappropriate, it should act to stop the regulation. When the Legislature believes a fee amount may be excessive, the Legislature should consider capping a fees as it has done in the past.



TEXAS HOUSE of REPRESENTATIVES

Gary Gates

State Representative, District 28

November 17, 2022

Chairman Philip Cortez
House Committee on Urban Affairs
P. O. Box 2910
Austin, Texas 78768-2910

RE: The House Committee on Urban Affairs Interim Report to the 88th Texas Legislature

Dear Chairman Cortez,

Thank you for sending a draft of the committee's interim report for members' review and input.

The purpose of this letter is to respectfully note concurrences and concerns and to offer suggestions regarding the interim report, specifically about interim charges II, III and V, for your consideration.

CHARGE II: WORKFORCE HOUSING

Evaluate the availability of workforce housing to support the dynamic economic growth of the state. Study the use of public-private partnerships and other tools to incentivize the development of housing that meets Texas' expanding workforce demands. Develop and include measures to ensure accountability and transparency associated with these tools.

The Interim Report failed to respond to the substantive and material challenge asserted in the charge. It ignored the resources provided to the committee for the hearing held on July 14, 2022, regarding the enormous cost to the public to support Public Facility Corporations operating under the Section 303.042(f) tax breaks for apartment developers.

The Legislature's intent to incentivize the development of workforce housing has been corrupted by certain public/private partnerships taking advantage of the 100% property tax exemption benefits throughout the state. By design, leasehold interest property tax exemptions and a sales tax exemption for materials are intended to provide local incentives for apartment developers to benefit low and medium income renters. However, as Heather Way, Entrepreneurship and Community Development Clinic Director at the University of Texas School of Law, has pointed out in a detailed report "Public Facility Corporations and the Section 303.042(f) Tax Break for Apartment Developments", as currently applied by developers, these benefits:

- do not require lower rents than the current market rent values;
- do not justify the enormous tax exemptions;
- do not honor the spirit of the legislature to address workforce housing shortages; and
- do not serve the intended population (the low and middle income families suffering housing challenges).

These developers are profiting excessively under §303.042(f) while neglecting to benefit workforce housing challenges in Texas.

Background:

Local Housing Authorities are authorized under Tex. Loc. Gov't Code Ann. § 392.006 to create Public Facility Corporations (PFCs) to address *Housing & Public Buildings, and Low Income Housing*. As such, public housing authorities are considered political subdivisions entitled to governmental benefits in the performance of their functions and may issue bonds to purchase the obligations, to finance public facilities and to acquire, construct, rehabilitate, renovate, repair, equip, furnish, or place in service public facilities. Tex. Loc. Gov't Code Ann. §§ 303.003(11), 303.021.

In doing so, the legislature intended PFCs created under the Act to be public nonprofit corporations, engaged exclusively in performance of charitable functions. Tex. Loc. Gov't Code Ann. §§ 303.002, 303.042.¹ Likewise, PFCs, like economic development corporations, are, in essence, intended to be nonprofit corporations that undertake discrete projects for the benefit of their sponsoring authority. The legislature enacted the Public Facility Corporation Act to be "engaged exclusively in performance of charitable functions."²

Thus, PFCs are required to have articles of incorporation, a board of directors, and are granted authority to, at its own discretion, alter its programs, structure, organization and activities, and at the direction of its board of directors, may purchases land.

Under Section 303.042(f) of the Texas Local Government Code, a tax benefit structure was created with the intent to stimulate housing development in areas needing to address housing for underserved low, middle income, and workforce populations.

The National Low Income Housing Coalition's 2022 Gap Report breaks down the need for housing units across the country at different levels of affordability. It states that the shortage of housing in Texas is most severe at the lowest household income levels, with just 29 affordable and available homes per 100 renter households at or below 30% average median income (AMI) and 51 homes per 100 households at or below 50% AMI. Our own research has shown that developments receiving 100% property taxes exemption fail to benefit the public good because 80% of the area market rate is equal to the market rate rents charged by tax paying developments.

We further found that families with children are discriminated against because developments are not required to adjust rental unit size for household size. For example, in the Houston area, a family of two with an 80% AMI equaling \$56,700 should not pay more for rent than \$1,417.50 per month. This couple can find a 700 square foot one bedroom unit for less than \$1,200 per month, which is the market rental rate. Yet a family of four with the same 80% AMI (which equals \$70,850) is not likely to find a two or three bedroom unit at 30% of their income (\$1,771.25 per month); the average cost of a multi-bedroom apartment is approximately \$2,121.04. The family of four can only afford to rent smaller units, such as the 1 bedroom,

¹ *Orion Real Estate v. Sarro*, 559 S.W.3d 599 (Tex. App.—San Antonio 2018). The legislature enacted the Public Facility Corporation Act to "authorize the creation and use of public facility corporations with the broadest possible powers to finance or to provide for the acquisition, construction, rehabilitation, renovation, repair, equipping, furnishing, and placement in service of public facilities in an orderly, planned manner and at the lowest possible borrowing costs." Tex. Loc. Gov't Code § 303.002. The legislature intended PFCs created under the Act to be public nonprofit corporations, "engaged exclusively in performance of charitable functions." Id. §§ 303.002, 303.042.

² Tex. Loc. Gov't Code Id. §§ 303.002, 303.042.

which do not have the appropriate square footage required for their family. Consequently, in no case does the development have to adjust for AMI and family size jointly because the market rate for the 1 bedroom already accommodates the statutory requirement that 50% of units be at 80% AMI. Unless rental limits are tied to household size, inclusionary affordable housing can not be achieved and families with children will continue to be disregarded.

We have also found that a developer profits again if the developer sells the development, particularly during the lease-up phase. For example, the development owner may sell the development above the market value since the 100% tax savings and term transfer with the development³, and the developer has already benefitted from a one time abatement on materials for the building project.

Due to a lack of transparency and accountability in the law, the lucrative tax-exempt deals are benefitting apartment developers statewide resulting in property tax savings of \$800,000 to \$2 million a year per property.⁴ Finally, the property tax savings from PFC leases to development partnerships extend up to 75 to 99 years.⁵

Recommendations to promote accountability and transparency, recommendations addressing flaws within Section 303.042(f) include:

- 1. reduce limits on the leasehold term from the current 75 to 99 years;**
- 2. require annual reports to be filed with the Texas comptroller or another state entity as well as local taxing entities;**
- 3. require compliance reviews including an annual audit;**
- 4. require an RFP process;**
- 5. require alignment of rent and income restriction policies with affordable housing industry standards;**
- 6. require deeper income targeting;**
- 7. omit voucher and income discrimination by requiring some percentage of leases to be at or less than 30% of the AMI;**
- 8. specify inclusionary affordable housing requirements to tie rental unit size to household size so that families with children are better served;**
- 9. impose limits on acquisition projects (the development of a state defined acquisition strategy to document, guide, identify risks, and formulate an approach to justify the 100% property tax investment);**
- 10. require the development to justify that 80% of the property tax exemption benefit is accomplishing the governmental purpose of the sponsor, with no delineated limitations on the definition of "governmental purpose".**

CHARGE III: MMD

Review the Municipal Management District Legislative Template with respect to representation and accountability. Make recommendations for improving the template.

³ For example, in 2022, CBRE, Inc., listed a San Antonio property, Brio at Lookout, touting "Unique 100% Tax Exempt Status Through PFC Structure." The listing further states, "Brio at Lookout is operated under a Public Facility Corporation (PFC) with a San Antonio Housing Trust ground lease which provides 100% tax-exempt status. ... Rental rates may not exceed 35% of the household income limit. Rental limits are not tied to household size."

⁴ Way, Heather. "Urban Affairs Committee July 14, 2022, Public Hearing." July 11, 2022.

⁵ Way, Heather. (2020). *Public Facility Corporations and the Section 303.042(f) Tax Break for Apartment Developments: A Boon for Affordable Housing or Windfall for Apartment Developers?* The University of Texas School of Law Entrepreneurship and Community Development Clinic, page 12-14.

I wholeheartedly agree with the language in the second paragraph of page 18 that "...a simple majority is sufficient should be enough (sic) to determine whether the district should continue to exist, especially since bondholders' interests are safe regardless of whether the board is abolished by a landowner petition."

For this reason, I recommend that the general law governing MMDs, as well as the special legislation for each MMD created by the legislature, be amended such that the threshold for dissolution of an MMD be a simple majority of property owners.

I'm also concerned about statements within the report. Please consider the following:

- The first paragraph of page 17 the report states,
 - "The governing structure of MMDs is generally that the owner or owners of a majority of the assessed property within the district nominate a slate of board members and submit the slate to the city with jurisdiction over district." However, according to the general law governing MMDs, Chapter 375 of the Local Government Code, Sec 375.064, the initial directors are in place at the creation of the district (usually through legislation), and as each term expires succeeding board members are recommended to the governing body by the existing board of directors.
 - In fact, the language of Chapter 375, as originally passed, provided that new board members be recommended by existing board members. It was not until legislation passed in 2019 that property owners could submit their own recommendations. This recent change represents progress towards accountability, but doesn't go far enough, as the governing body still has complete discretion to ignore property owners and side with recommendations of the existing board.
- It is factually incorrect to assert that, "...generally the owner or owners of a majority of the assessed property within the district nominate a slate of board members", as this is a new and rare occurrence, if indeed it has ever taken place in practice.
- The sixth paragraph of page 17 of the report is factually incorrect to state, "Because MMDs are usually created from territory that is raw, unimproved land, initially there may be only one property owner, be that an individual or a company, which makes initial elections unnecessary."
 - MMDs are not strictly about empty land development, yet language throughout the report seems to suggest that this is the standard application for all new MMDs. While it is true that recently many new districts have this end in mind, the language used in the report is misleading by suggesting that this is the only case worth considering and using this one case to dismiss a greater need for accountability in all cases.
 - The report makes it clear that the most concentrated use of MMDs is in the Houston area, most of these Districts are not the "undeveloped land, single owner" type of situations that the report describes, but rather well-developed areas in need of economic revitalization where MMDs are expected to serve as "mini chambers of commerce".
 - These MMDs, along with any other MMDs that continue to exist beyond initial development of land, have little to no direct accountability to assessment payers.
 - It is misleading and potentially hazardous for the committee to consider only undeveloped land, and not any of the other vastly different degrees of development that might exist in an area prior to the creation of an MMD.
 - Any discussion of a template contemplates the broadest number of cases possible; language such as, "Because MMDs are usually created from territory that is raw, unimproved land, initially there may be only one property owner, be that an individual or a company, which

makes initial elections unnecessary” fails to address the concerns that exist in a significant number of other applicable cases.

- A major part of the discussion in the July 14, 2022, hearing focused on lack of accountability to the assessed commercial property owners, which was not noted in the report. Numerous concerned parties approached the committee about their own negative experiences, and it is disconcerting the report does not address this matter.
- The current language of the template requires a petition of a majority of property owners by assessed value in order to levy an assessment; however, many MMDs created by the legislature require a much smaller threshold. For example, in some well-developed districts with over 500 individual property owners, all that is required to levy an assessment on every property owner is a petition from any 25 assessed owners – regardless of property value.

Recommendations:

1. The legislature should consider for Chapter 375, the general law governing MMDs, as well as the special legislation for each MMD created by the legislature, be amended to allow for the threshold for dissolution of an MMD to be a simple majority of property owners.
2. The legislature should contemplate ensuring that a governing body is required to approve any slate of directors recommended by a petition of property owners according to Sec 375.064, superseding entirely the board’s own recommendations in the case that both sets of recommendations exist.
3. The legislature should deliberate redressing situations where small minorities of property owners can petition to levy assessments on whole MMDs and amend the laws governing each special district to give more power to affected property owners, as the current situation is tantamount to taxation without representation.

CHARGE V: MUNICIPAL FEES

Study municipal fees with respect to the function of the fee and the relationship of the fee to the cost of providing an associated municipal service. Make recommendations to address municipal fees that are disproportionate or unrelated to the cost of providing the associated service.

After studying municipal fees with respect to the function of the fee and the relationship of the fee to the cost of providing an associated municipal service, and after finding that many cities are becoming creative in generating revenue through such assessments, the following is noted:

- Cities cannot charge unauthorized taxes.⁶
- Fees that bring in more money than it costs to regulate an activity or provide a service can be found by a court to be unauthorized taxes.⁷

The following recommendations address municipal fees that are disproportionate or unrelated to the cost of associated services:

Limit municipal fees by setting minimum statewide standards

⁶ Tex. Const. Art. XI, § 5. Fees that generate revenue in excess of what is needed to operate the program can be found by a court to be unauthorized taxes – often called “occupation taxes.” All Fees Must Have A Clear Legal Basis.

⁷ *City of Corpus Christi v. Bayfront Assocs.*, 814 S.W.2d 98, 1991 Tex. App. LEXIS 1574

- a. **establishing a threshold on fees to prevent disproportionate or unrelated costs that are in excess of the cost of providing the associated service;**
- b. **eliminating fees that fail to meet a specific public purpose requirement.**

Sincerely,



Gary Gates
State Representative, House District 28

cc: House Committee on Urban Affairs Committee Members and Enrique.Marquez@speaker.texas.gov

ENDNOTES

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- ² Texas Rent Relief Program Dashboard, TDHCA, <https://app.powerbi.com/view?r=eyJrIjoiOTQzMjI5ZDctY2MxMy00ZGJlLWI2YjAtOTg3ODZiZGZhYWQzIiwidCI6ImEwZTYxZGNkLTUxYTItdm3NC05ZmEyLWJiMmFiNjBjNWl2MyIsImMiOiN9>
- ³ Texas Legislative Council Memorandum to Urban Affairs Committee, Data Processing and Analysis of Rent Relief Program Assistance, September 20, 2022
- ⁴ Texas Homeowner Assistance Fund provide \$19.2M in assistance, serves 2,800 households. TDHCA Press Release, April 28, 2022, <https://www.tdhca.state.tx.us/ppa/press/220428-TxHAF-19million-2800households.html>
- ⁵ Texas Homeowner Assistance Fund Program Dashboard, TDHCA, <https://app.powerbi.com/view?r=eyJrIjoiMDE4NTBIZTQtZmM5S00ZGUwLWl2N2Q0ZDI0MjMwNjdmZmI3IiwidCI6IjZhN2I0YTc4LThmM2EtNDk1YyIiZmM4LWRiNTBjMDFmMTEiYiIsImMiOiN9>
- ⁶ Workforce Housing: Barriers, Solutions, and Model Programs, pg. 3, Richard M. Haughey, Urban Land Institute, June 2002,
- ⁷ New "Paycheck to Paycheck" Study Finds Homeownership Still Unaffordable for Many Key Community Workers, Despite Low Interest Rates and Home Prices, Andrea Nesby, National Housing Conference. March 23, 2010.
- ⁸ Whither Workforce Housing? Mathew J. Parlow, Fordham Urban Law Journal, Pgs. 1658 - 1658. November 12, 2013..
- ⁹ Bobby Wilkinson, Executive Director, Texas Department of Housing and Community Affairs, Testimony before the House Committee on Urban Affairs, July 14 2022.
- ¹⁰ Roger Arriaga, Texas Affiliation of Affordable Housing Providers, Testimony before the House Committee on Urban Affairs, July 14, 2022.
- ¹¹ David Wheaton, Texas Housers, Testimony before House Committee on Urban Affairs, July 14, 2022.
- ¹² Austin, TX Rent Prices, zumper.com, October 29, 2022, <https://www.zumper.com/rent-research/austin-tx>
- ¹³ Wither Workforce Housing? Parlow, Pg. 1657.
- ¹⁴ Ibid, Pg. 1658
- ¹⁵ U.S. Census Bureau Quick Facts. <https://www.census.gov/quickfacts/fact/table/houstoncitytexas/INC110220>
- ¹⁶ Texas Housing Prices on the Rise, Fiscal Notes, Texas Comptroller of Public Accounts, March 2018, <https://comptroller.texas.gov/economy/fiscal-notes/2018/march/housing.php>
- ¹⁷ In Battle for Workers, Companies Build Houses, Disney, meatpacker JBS and others launch plans to add affordable housing near job sites, a Vail, Colo., project draws opposition, Chip Cutter and Lauren Weber, The Wall Street Journal, May 22, 2020, <https://www.wsj.com/articles/in-battle-for-workers-companies-build-houses-11653217201>
- ¹⁸ Bill Analysis for Senate Bill No. 3, Enrolled Version, June 6, 2021, Senate Research Center, pg. 19. <https://tlis/tlisddocs/87R/analysis/pdf/SB00003F.pdf#navpanes=0>
- ¹⁹ Alphabet Soup: Types of Texas Cities, Pg. 5, Texas Municipal League, <https://www.tml.org/DocumentCenter/View/244/Types-of-Texas-Cities-PDF#:~:text=A%20home%20rule%20city%20may.granted%20or%20implied%20by%20statute.> December 2017.
- ²⁰ Ibid. Pg. 10.