

Public Facility Corporations and the Section 303.042(f) Tax Break for Apartment Developments

A boon for affordable housing or windfall for apartment developers?



A Report by The University of Texas School of Law
Entrepreneurship and Community Development Clinic

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The University of Texas at Austin
**Entrepreneurship and Community
Development Clinic**
School of Law

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Public Facility Corporations and the Section 303.042(f) Tax Break for Apartment Developments: A boon for affordable housing or windfall for apartment developers?

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Executive Summary

Public Facility Corporations and the Section 303.042(f) Tax Break for Apartment Developments in Texas

A boon for affordable housing or windfall for apartment developers?

This research report examines a recently adopted property tax exemption for private apartment developers available under Section 303.042(f) of the Texas Local Government Code. While the amendment received little notice when it was adopted, the use of this exemption is rapidly growing and delivering property tax breaks to apartment developers of close to \$1 million a year per property on average—or an average of \$7,400 a year per income-restricted unit. New construction projects are also eligible for a 100% sales tax exemption on construction materials, resulting in an additional, one-time exemption of \$1.3 million on average per new apartment development. The costs of the tax breaks are large, and, on scrutiny, the public benefits are comparatively few.

To receive the exemption, a private apartment developer transfers land to a public facility corporation (PFC) set up by a local government entity—such as a public housing authority, county, or city—which then leases the land and any buildings on the land (including those built in the future) back to a limited partnership controlled by the developer. The local government entity gets paid to participate in the venture.

Other local government entities—such as school districts—have no say over these property tax breaks to for-profit apartment developers, even though the tax breaks directly impact these other entities’ property tax base and bottom line. In contrast, the state’s other property tax break programs supporting economic development by for-profit entities provide taxing units with the option to participate in the tax break. The ability of public housing authorities to approve exempt projects under Section 303.042(f) is particularly troubling since the housing authorities are not impacted by any of the lost property tax revenue and their boards consist entirely of unelected officials who lack any political accountability to taxpayers.

Section 303.042(f) also lacks the protections provided in the state’s property tax exemption statutes for nonprofit-owned affordable housing developments—such as reporting requirements, rent restrictions, and other protections meant to ensure transparency, accountability, and delivery of strong public benefits. The Section 303.042(f) exemption comes with no restrictions other than a requirement that at least 50% of the units in projects sponsored by public housing authorities’ public facility corporations be reserved for occupancy by households earning less than 80% of the area median family income.

The report’s specific findings include:

- **Texas has seen a rapid growth in Section 303.042(f) exempt projects.** Since 2016, at least **30 apartment** complexes in Texas have been acquired, developed, or are in active development under this tax-exempt structure, with **17 of these deals approved in 2019**. Housing authorities, cities, and counties report an

FIG. 1
Tax-Exempt Apartments Sponsored by PFCs under Section 303.042(f)



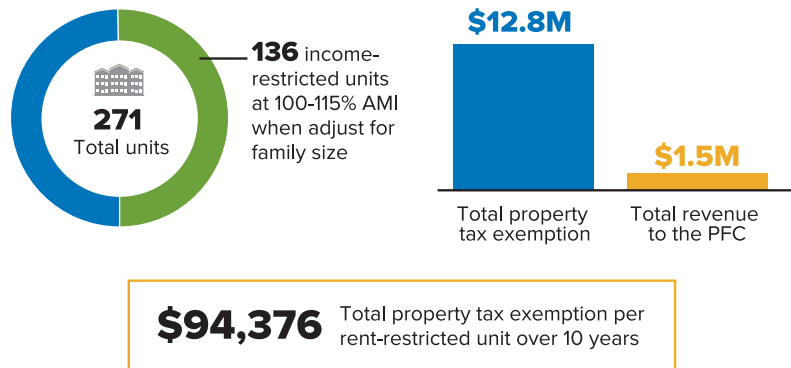
(acquired, completed, or under development 2016-2020)



on-going onslaught of proposals by apartments developers to convert existing apartment complexes as well as develop new apartment complexes under this structure in order to obtain the Section 303.042(f) exemption. To date, these projects have been concentrated in the state’s largest cities (especially San Antonio and Houston) but are spreading into suburban areas and smaller cities. See Appendix 2 of the report for an inventory of exempt projects.

- **The Section 303.042(f) exemption’s marginal financial returns to PFCs are outstripped by the property tax losses.** In exchange for entering into a leasehold interest structure with a private apartment developer, public facility corporations receive some form of revenue from the project. However, in the projects approved to date, the amount of revenue flowing to PFCs from these deals pales in comparison to the value of the property tax exemption. See, for example, Figure 31. If recent trends continue, the Section 303.042(f) exemption could remove more than **\$12 billion** in property values off the tax rolls by 2026, resulting in a loss of approximately **\$326 million a year** in revenue to local taxing districts and the state public education budget. See Figure 12 in the report. Despite the mismatch in financial returns and tax revenue losses, public housing authorities—which are struggling financially to maintain their properties—have a perverse incentive to approve these exempt projects since they are not impacted by the loss of property tax revenue.

FIG. 31
The Baldwin: Revenue to the City of San Antonio vs Property Tax Exemptions 2019-2029

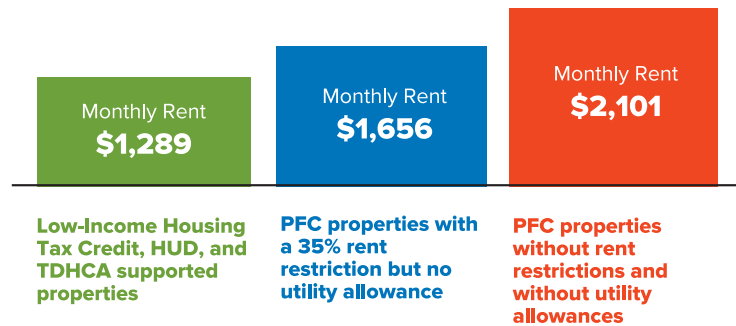


- **The Section 303.042(f) exemption fails to serve the state’s affordable housing needs.** A core public policy rationale for the Section 303.042(f) exemption is that it generates affordable housing. But because Section 303.042(f)’s income restrictions do not require adjustments in household size, the income restrictions utilized at the exempt properties **end up largely targeting middle-income renters making 100-115% of the area median income (AMI)**—a group of renters adequately served by the market. Figure 22 shows the actual income targeting of PFC projects approved to date once household size is taken into account (which is the standard in affordable housing programs). **Only 3% of the units in Section 303.042(f) exempt properties are restricted to serving renters making less than 60% AMI**—renters whose housing needs are largely not served by the market. Close to half of renters making up to 60% AMI in the state’s five largest metro areas pay more than half their income on rent, meaning they are severely cost burdened under federal guidelines.
- **Texas’ middle-income renters do not need deeply subsidized rental housing.** For-profit apartment developers tout the Section 303.032(f) exemption as a tool to promote middle-income rental housing (controversially termed “workforce housing”). However, the subsidy provided through the exemption is very large—**an average of \$7,400 a unit a year, or \$148,000 per unit over 20 years**—which is on par with the rental subsidy for tenants with Housing Choice vouchers, whose average income is below the poverty line. But, unlike renters living in poverty, the middle-income renters served by properties with a Section 303.042(f) exemption do not need deep subsidies for their housing. Texas actually has a surplus of units that are available and affordable to households making up to 80% and 100% of the Area Median Income. Even in the state’s most populated counties, there is a surplus of units for middle-income renters, and only a very small fraction of these renters are extremely cost burdened.

- Most Section 303.042(f) exempt properties lack rent restrictions.** In contrast to most other affordable housing subsidy programs, Section 303.042(f) does not require any rent restrictions on the income-restricted units. As a result, **close to 60% of properties with a Section 303.042(f) exemption have no rent restrictions**, and there is thus no guarantee that the rents will be affordable to low-income renters. Of the 12 exempt properties with rent restrictions, none require a utility allowance to be deducted from the maximum rent and five impose rent restrictions at 35% of the applicable AMI restriction level, rather than the affordable housing program standard of 30%, making it more difficult for renters to cover other essential living expenses.

FIG. 17
Maximum Rents Allowed at Apartment Complexes for 2-Bedroom Units Restricted to Renters Making up to 80% AMI (2020)

(= based on 4-person household making up to \$63,040 in the Houston metro area)



- PFC projects discriminate against tenants with vouchers.** Very few properties with a Section 303.042(f) exemption accept tenants with rental vouchers from their local housing authority. For example, none of the PFC-sponsored properties in San Antonio with a Section 303.042(f) exemption accept tenants with vouchers. In contrast, other major affordable housing subsidy programs—such as the Low Income Housing Tax Credit program—prohibit apartment complexes from discriminating against voucher holders. The failure to accept voucher holders is troubling, especially given that housing authorities are sponsoring most of these projects. Housing authorities’ largest group of clients are voucher holders, who are predominantly African-American and Hispanic. Many of these renters face enormous challenges securing a unit with their vouchers, especially in high opportunity neighborhoods with access to strong schools, transit, and jobs.

Recommendations

The findings in our report raise important questions about the 100% property tax exemption under Section 303.042(f) and whether it should continue. And even if local governmental entities should have the authority to exempt their own tax base to subsidize apartment developments, should they have the authority to exempt the tax base of other taxing authorities? These are important questions that deserve further public scrutiny. Assuming that the Section 303.042(f) exemption does continue, we make the following recommendations on ways to strengthen the exemption.

TRANSPARENCY AND ACCOUNTABILITY

- Require annual reports.** At a minimum, state law should require local governments to submit annual reports to the Texas Comptroller and local taxing entities regarding all apartment complexes receiving an exemption under Section 303.042(f).
- Require compliance reviews including an annual audit.** PFCs should engage in regular compliance monitoring of the conventionally-financed properties they are sponsoring under Section 303.042(f). And private developers receiving a property tax exemption under Section 303.042(f) should be required to obtain an annual audit regarding the property’s compliance with all the affordability restrictions imposed on the property
- Require an RFP process.** Developers partnering with local governments on PFC projects under Section 303.042 should have to go through a competitive request for proposal process. Proposals should be

submitted via an application process and scored according to specific criteria based on goals adopted by the local government's governing body, to ensure that partnerships via Section 303.042 are awarded to projects best qualified to meet the community's needs. The application should be reviewed by an independent real estate finance expert to evaluate the project's finances and weigh the cost-benefits of awarding a 100% exemption on the property.

AFFORDABILITY MEASURES

4. **Require alignment of rent and income restriction policies with affordable housing industry standards.** All properties receiving an exemption under Section 303.042(f) should be required to follow affordable housing industry standards by adjusting their AMI targeting levels for family size and adopting rent restrictions based on 30% of the applicable AMI restricted levels as established by HUD. The rent restrictions should also incorporate a utility allowance. Finally, the income screening should consider the income of everyone living in the unit and not just the person listed on the lease.
5. **Require deeper income targeting.** In order for a property to qualify for Section 303.042(f) exemption, a good portion of the property's rents must be restricted at significantly lower rates than market rents for the area. Ideally at least 25-50% of the units at the property would be restricted at affordable rates for households making less than 60% of the Area Median Income with the affordable units spread across the bedroom sizes and a small percentage of the units restricted to renters with vouchers from the local housing authority to result in truly mixed-income housing.
6. **Ban source of income discrimination.** Property developers receiving a Section 303.042(f) exemption should be barred from discriminating against tenants with a housing voucher that covers part of their rent. This means that properties also need to be barred from applying minimum income policies to exclude voucher holders—the minimum income policy should only be applied to the tenant's portion of the rent. Public entities should also consider requiring the exempt properties in high opportunity neighborhoods to dedicate up to ten percent of the units for tenants with vouchers.
7. **Engage in affirmative marketing.** Housing authorities should actively market the 303.042(f) exempt properties to their voucher clients, including listing these properties on their websites. Cities and counties should also actively market all of their exempt properties. Property managers of PFC-sponsored properties should be required to market the affordable units on the property's website and include references about the availability of affordable units at the property in all public marketing materials. The property managers should also be required to notify the housing authority's Housing Choice Voucher program when vacancies arise in the income-restricted units.
8. **Adopt enhanced protections for renters.** In order for a property to qualify for the 100% property tax exemption under Section 303.042(f), the property should be required to include enhanced protections for tenants for the life of the property. These protections should include a right to cure any lease deficiencies, a right to organize, and a ban on lease non-renewals without cause. The City of Austin requires similar protections in all apartment developments it funds as well as private activity bond projects it approves.
9. **Serve families with children.** The affordable units in a property receiving an exemption under Section 303.042(f) should be distributed proportionately across bedroom/bathroom categories and not concentrated in the smaller units. PFCs should also require that the affordable units in the larger bedroom sizes be marketed to families with children.
10. **Impose limits on acquisition projects.** If a PFC is taking an existing apartment complex off the tax rolls, the property should have to meet criteria similar to the requirements in Section 11.825 of the Tax Code to justify the removal of the property off the tax rolls. Under Section 11.825, rehabilitation projects are eligible for the exemption only if (1) the original construction was completed at least 10 years prior to rehabilitation, (2) the prior owner owned the property for at least five years, and (3) the organization spent at least \$5,000 per unit on rehabilitation costs, or an amount required by the lender, if greater. If a PFC partners on an acquisition project it should be required to pay for tenant relocation costs at a standard equivalent to the federal Uniform Relocation Act for any tenants displaced as a result of the acquisition.

Introduction

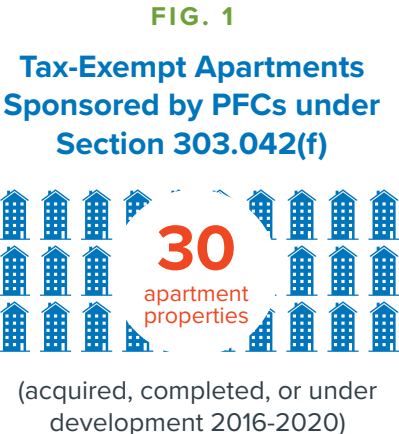
In 2015, the Texas Legislature adopted a new 100% property tax exemption for apartment complexes developed through a special type of public facility corporation structure—one where a private developer rather than a public entity controls a long-term leasehold interest in the apartment complex. The 100% exemption, created under Section 303.042(f) of the Texas Local Government Code, delivers property tax savings to private developers of close to \$1 million a year per property on average. New construction projects are also eligible for a 100% sales tax exemption on construction materials, resulting in an additional, one-time exemption of \$1.3 million on average per new property.

The projects receiving a Section 303.042(f) exemption by and large target middle- and upper-income renters. Only 4% of the 8,906 units in current tax-exempt projects are restricted for households with incomes of 0 to 65% of the Area Median Income, and only 12% of units are restricted for households with incomes of 65-80% of the Area Median Income, once family size is considered.

Since 2016, at least 30 apartment complexes in Texas have been acquired, developed, or are in active development under this tax-exempt leasehold interest structure, with 17 of these deals approved in 2019. At least six additional deals with this structure have received preliminary approval by a public facility corporation board. Eight of the approved deals involved the acquisition of an existing apartment complex versus new construction. Housing authorities, cities, and counties report an on-going onslaught of proposals by apartments developers to convert existing apartment complexes as well as develop new apartment complexes under this structure in order to obtain the Section 303.042(f) exemption.

The 100% property tax exemption on all 30 of these properties, once they are completely developed in a few years, will remove an estimated \$1.2 billion in property values from the tax rolls. The fiscal impact is significant, with local taxing jurisdictions, including counties, cities, school districts, as well as the state’s public education fund, seeing a loss of over \$32 million in annual tax revenue from these 30 apartment complexes alone once they are completed. With the recent rapid growth in these exemption deals and the deluge of apartment developers seeking to benefit from this exemption, the exemption could remove more than \$12 billion in property values off the tax rolls by 2026 with a cumulative property tax exemption of \$326 million a year. These tax impacts are explored in more detail in Part Five.

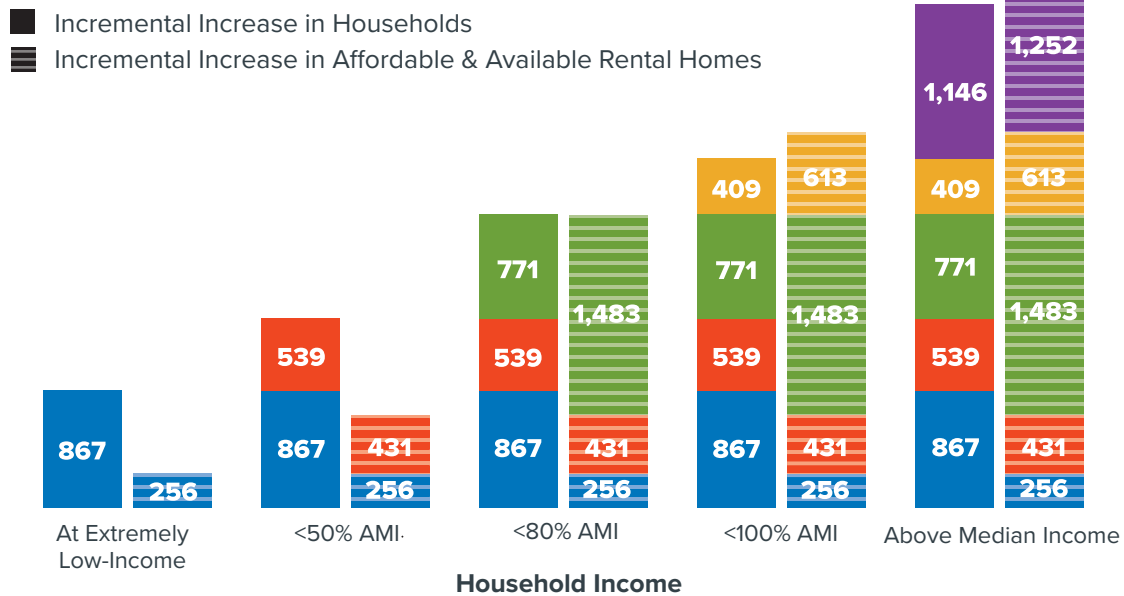
At the same time these tax-exempt projects are being approved, Texas faces an on-going affordable rental housing crisis for Texas’s 1.4 million renter households who make less than 50% of the Area Median Income, with a severe shortage of rental units that are affordable to these households. Thirty-three percent of renters who make less than 50% of the Area Median Income are extremely cost burdened.³ In contrast, only six percent of renters making 65 to 80% of the Area Median Income are extremely cost burdened, and only one percent of renters making over the Area Median Income are extremely cost burdened.⁴ Texas actually has a surplus of units that are available and affordable to households making up to 80% and 100% of the Area Median Income.⁵ See Part Five for a discussion on affordable housing needs by specific metro areas. Even in the state’s most populated counties, there is a surplus of units for middle-income renters and only a very small fraction of these higher income renters are extremely cost burdened. See Part Five, Figure 25.



Total property values when completed: **\$1.2 billion¹**

Value of total annual property tax exemption when completed: **\$32 million²**

FIG. 2
Renter Households and Affordable & Available Rental Homes, Texas, 2018
(in 1,000s)



Source: NLIHC Tabulation of 2018 ACS PUMS data

While the new exemption available under the 2015 amendments has come under criticism on several fronts,⁶ stakeholders engaged in these deals, including financiers, developers, and local government housing agencies, tout the exemption for advancing three primary public policy goals:

1. **Affordable housing:** Creates affordable housing serving middle-income renters in the workforce who are not served by either the market or most government affordable rental housing programs. A few housing agencies also tout the exemption as a way to incentivize the inclusion of more deeply affordable housing serving lower-income households.
2. **Funding:** Fills government housing agencies' coffers with funds they can use to support more deeply affordable housing projects.
3. **Economic development:** Incentivizes new Class A, market-rate apartment development in disinvested low-income neighborhoods or other areas where the market will not build higher-end apartments. Spurs other economic development in the area.

In this research paper, we seek to shed light on this fairly new tax break tool, which was created quietly without any public scrutiny via an amendment on the Texas Senate floor. We believe scrutiny and strong oversight of this tool is needed, as with any tax breaks provided to private companies, to determine whether the tax breaks further worthwhile public policy goals and whether the tax breaks' benefits outweigh their costs. We focus in particular on the touted affordable housing benefits. We examine ways in which the exemption tool is being utilized around the state and how it can be strengthened to best serve the state's affordable housing needs.

Parts One and Two of this research paper provide background on public facility corporations in Texas and the genesis of the new exemption for PFC-sponsored apartment complexes created by the 2015 legislation. Part Three discusses the inventory we created of local jurisdictions using public facility corporations to sponsor apartment developments under Section 303.042(f), along with apartment projects benefitting from the exemption or in the pipeline to benefit. In Part Four, we discuss the process for how an apartment project becomes sponsored by a PFC and how these deals are structured. Part Five then analyzes the public

policy rationales and costs of the exemption, with a focus on whether and how the tool is filling the state's affordable housing needs. Finally, in Part Six, we offer recommendations for strengthening the exemption and maximizing its public benefits as well as public transparency.

As part of our research, we reviewed the legal documents for 23 PFC deals receiving a Section 303.042(f) exemption (such as memoranda of understanding, ground leases, regulatory agreements, and partnership agreements, as available). We also spoke with many stakeholders involved in these deals, including officials from public housing authorities, cities, and counties; apartment developers; attorneys for PFCs and developers; and leasing agents.

Part One. Background on Public Facility Corporations and Government-Sponsored Rental Housing Development: Pre-2015

Chapter 303 of the Texas Local Government Code provides for the creation of public facility corporations and endows them with very broad powers to finance, acquire, construct, and repair public facilities, among other functions. A public facility is defined broadly to mean any “real, personal, mixed property, or an interest in property devoted or to be devoted to public use, and authorized to be financed, refinanced, or provided by sponsor obligations or bonds issued under this chapter.” § 303.003(7). A “sponsor obligation” includes leases and contracts to provide a public facility. § 303.003(12). Property owned by a public facility corporation is eligible for a 100% tax exemption. Tex. Local Govt Code, § 303.042(c).

A sponsor of a public facility corporation can be a municipality, county, school district, housing authority, or special district. § 303.003(11). Public facility corporations were originally used primarily to issue tax-exempt bonds (with no public vote required) and shield public entities from liability for the construction of large public facilities such as correctional facilities and school buildings. A local jurisdiction for example, can create a public facility corporation to develop a facility and pay for that facility through revenue bonds, which are paid from leasing the improvements to the county with an option to purchase the improvements. Public facility corporations have also been used to develop convention center hotels, as in the case of the City of Austin’s convention center hotel, which was developed and financed through tax-exempt revenue bonds issued by the convention center’s public facility corporation and, via a long-term contract, is managed and operated by Hilton.

Public facility corporations (PFCs) were likely first used to sponsor multifamily rental housing development after the 1995 amendments to the Public Facility Corporation Act, via Senate Bill 1646. In those amendments, the Texas Legislature authorized public housing authorities (PHAs) to create PFCs and issue tax-exempt bonds through their PFCs, in response to an attorney general opinion that the AG would no longer authorize PHAs to issue bonds unless the legislature established such statutory authority. Under the amendments, a nonprofit corporation created by a PHA is automatically considered to be a public facility corporation. § 303.022.

In 1999, the Texas Legislature adopted House Bill 2209, which added Section 392.066 to the Local Government Code and cemented the authority of public housing authorities to create PFCs and make capital contributions and loans to them to provide housing. Similar to the 1995 amendments, the 1999 legislation was also adopted in response to an attorney general opinion, this time questioning PHAs’ authority to issue grants or loans to its public facility corporations. Under the 1999 amendments, any housing development project using funds provided by a PHA under Section 392.066 must benefit households making no more than 60% of the area median income, adjusted for family size, in the same proportion that the funds provided by the PHA bear to the overall cost of the housing development or other program. See § 392.066(e). So, for example, if a housing development costs \$10 million and the PHA’s public facility corporation contributes \$1 million, then 10% of the units must be affordable to households making at least 60% of the area median family income. The income targeting in Section 392.066 only applies if the PHA is contributing funds to its PFC under Section 392.066 and not other sections of the Local Government Code.

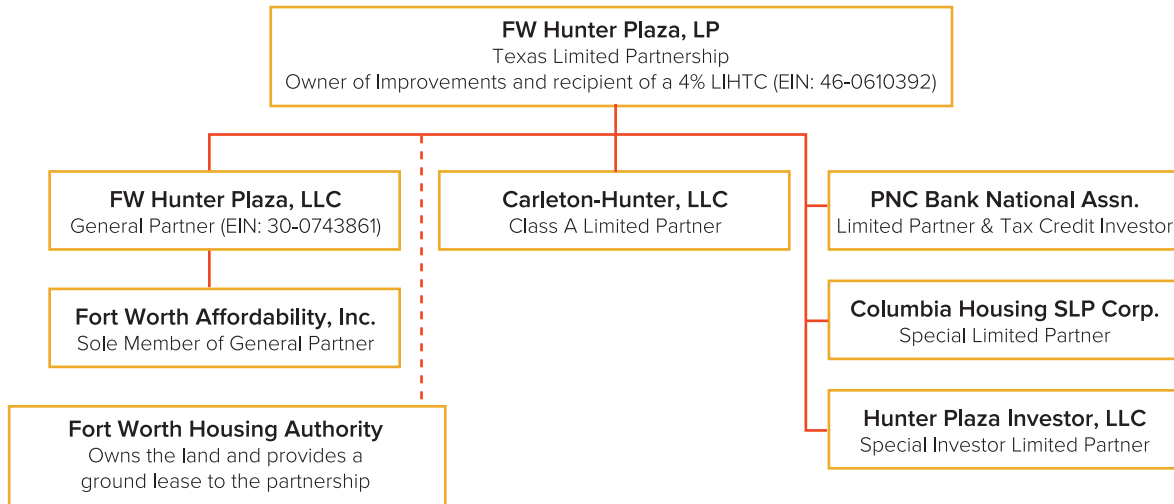


In 2001, in response to concerns that apartment developments sponsored by PHAs’ public facility corporations were receiving a 100% property exemption in exchange for scant affordable housing, the Texas Legislature imposed income limits on all PHA public facility corporation sponsored developments, not just those receiving funding from the PHA. See Senate Bill 929 (77th Regular Session). In order to obtain a 100% property tax exemption, at least 20% of the units in a development must be reserved as public housing units or at least 50% of the units must be reserved for occupancy by households making less than 80% of the

area median family income. For this latter group of properties, the housing authority must also hold a public hearing to approve the development at one of its regular board meetings. § 303.042(d).

FIG. 3

**Typical Entity Structure for a Rental Housing Development with a Public-Private Partnership and Low Income Housing Tax Credits
(from Hunter Plaza Apartments, Fort Worth Housing Authority)**



Prior to 2015, when a PHA decided to partner with a private developer on an affordable rental housing development, it typically did so through a nonprofit corporation it created and controlled (and which, after the 1995 legislation, was treated as a public facility corporation under Section 303.022). The PHA nonprofit corporation would lease land to a limited partnership and served as the partnership’s general partner (or the PHA’s nonprofit corporation was the sole member of another subsidiary entity, such as an LLC, that served as the general partner), while the private investors and developers served as the limited partners. The limited partnership then built and owned the improvements on the land, while the PHA subsidiary retained an option to purchase the improvements. See Figure 3. These developments usually, but not always, relied upon public financing such as federal Low-Income Housing Tax Credits, which were often combined with tax-exempt bonds. These developments benefit from a 100% tax exemption under Section 392.005 of the Local Government Code (see Appendix 1 for a discussion of this exemption). Depending on the source of public financing, the developments often included deeper income targeting than required under state law. This is still the structure PHAs use for all developments receiving federal Low-Income Housing Tax Credits.

A few years prior to 2015, the City of San Antonio also began utilizing public facility corporations to partner with private developers in creating affordable apartment complexes with subsidized rents, using a structure similar to that utilized by public housing authorities outlined above. San Antonio’s first PFC-sponsored housing development was developed in 2012 through its subsidiary, the San Antonio Housing Trust, in partnership with a private developer, the NRP Group. The housing development, Cevallos Lofts, was financed with federal Low-Income Housing Tax Credits and other subsidies and included 63 affordable units for households at or below 50% Area Median Income, along with 189 market rate apartments.

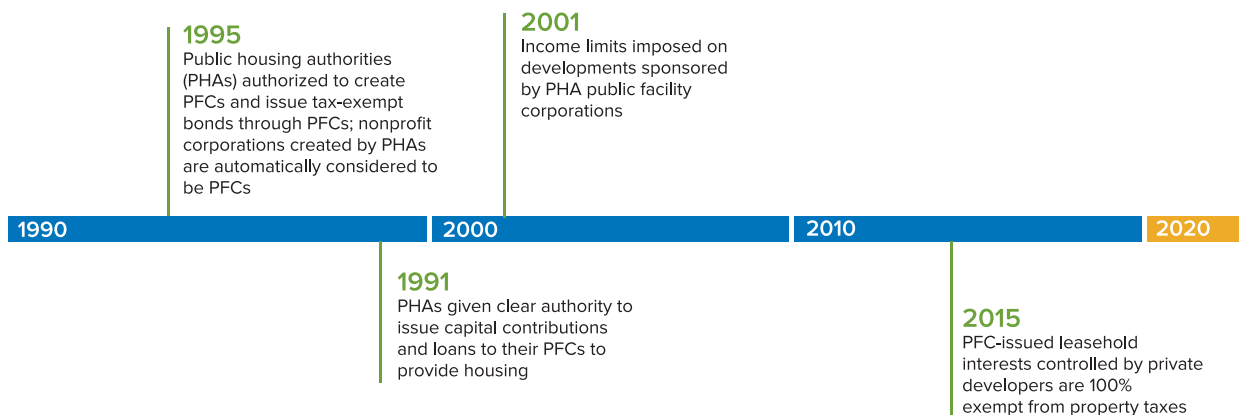
Part Two. Overview of the 2015 Addition of Section 303.042(f)

In 2015, the Texas Legislature extended the PFC tax exemption in Chapter 303 to leasehold interests controlled by private entities, thus paving the way for a whole new form of housing development that is eligible for a 100% exemption from property taxes. A “leasehold interest” describes the real property interest that is created when a landowner leases real property to a third party via a ground lease. Prior to 2015, when a public facility corporation’s real property was leased for more than a year to a private, for-profit entity, the leasehold interest was fully taxable under Sections 303.042(a)-(b) of the Local Government Code and Section 25.07(a) of the Tax Code.

Section 25.07(a) applies to real property that is exempt from taxation, such as publicly-owned property that is used for a public purpose. Leasehold interests of greater than a year in such properties are listed on the tax rolls in the name of the lessee (i.e., the tenant, also known as the owner of the “possessory interest”) rather than the property owner (i.e., the landlord). As a result, absent an exception in the code, when a local public entity enters into a long-term lease of real property to a private party, the public entity’s tax exemption does not extend to that leasehold interest and the private party must pay taxes on that interest unless the lessee is also subject to an exemption from property taxes.

FIG. 4

Legislative History: Public Facility Corporations’ Role in Rental Housing Development



The 2015 amendments added Section 303.042(f) to the Local Government Code, which, in a highly convoluted and roundabout manner, exempted PFC-issued leasehold interests from the tax treatment of leasehold interests under Section 25.07(a). As a result, when a public facility corporation—such as one created by a PHA or city or county—leases land and improvements built on that land to an entity controlled by a private, for-profit development entity, that leasehold interest is now taxed in the name of the public facility corporation and is 100% exempt from property taxes.

The amendments thus opened up a new opportunity for housing developers to receive a 100% property and sales tax exemption on apartment complexes, whereby the local governmental entity no longer has to control the development via a general partnership interest. With the local government as only a minor limited partner, the leasehold interest can be easily flipped to new buyers without the authorization of the local governmental entity, making it a highly liquid asset that is attractive to private equity investors.

The 100% exemption on PFC-issued leasehold interests controlled by private developers stands in stark contrast to exemptions for affordable rental housing controlled by non-public tax-exempt entities. For example, unlike the 50% property tax exemption for qualified nonprofit organizations developing affordable housing (see Appendix 1 for an overview of this and other affordable housing exemptions), the PFC leasehold exemption comes with no rent restrictions or monitoring provisions, and no restrictions on converting existing apartment complexes into tax exempt properties. These differences are discussed further in Part Five.

The only statutory restrictions on a PFC-issued leasehold interest to qualify for a 100% exemption are the income targeting restrictions imposed under Section 303.042(d) of the Local Government Code, which apply only to developments sponsored by public housing authorities' PFCs. As discussed above, these restrictions require at least 20% of the units in a development to be reserved as public housing units or at least 50% of the units to be reserved for occupancy by households making less than 80% of the area median family income.

In addition, the exemption must comply with the Texas Constitution's provisions requiring that property be publicly-owned and used for a public purpose or owned by an institution engaged primarily in public charitable functions. See Tex. Const. Art. VIII, § 2(a); Art XI, § 9. Apartment developers and their attorneys have asserted that the Constitution's public purpose test can be met as long as an apartment complex meets the Section 303.042(d) income restrictions on projects sponsored by a PHA's public facility corporation, i.e., by reserving half the units in the development for households making less than 80% of the area median income ("50% at 80% AMI restriction"). In other words, even though the 50% at 80% AMI restriction in Section 303.042(d) applies only to public facility corporations created by a public housing authority, lawyers have advised other public entities using the PFC leasehold interest structure to apply the same 50% at 80% AMI restriction as a precaution to help ensure the property meets the Texas Constitution's public purpose requirement. Whether the 100% property tax exemption applied to these privately-controlled leasehold interests does in fact pass muster under the Texas Constitution is an issue beyond the scope of this report but one that merits further investigation.

FIG. 5
How a PFC Partnership Works for New Construction Projects with a Section 303.042(f) Exemption

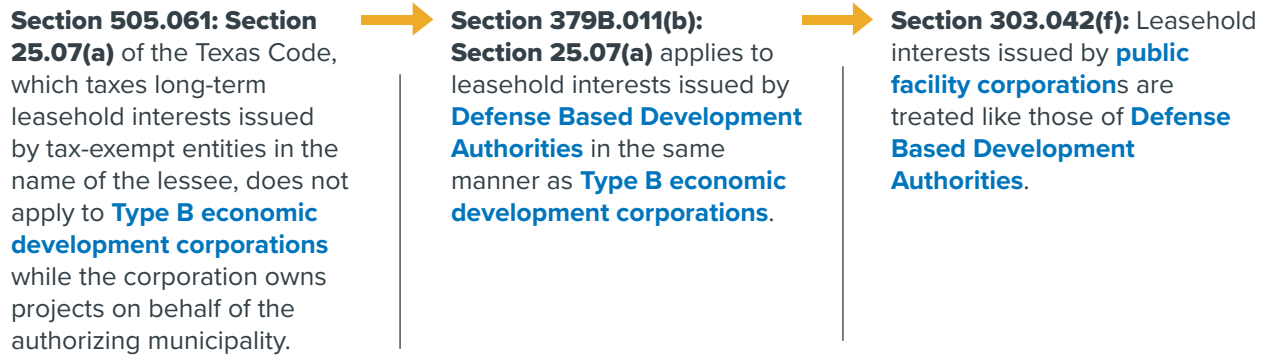


HOW TO READ THE 2015 AMENDMENT

The convoluted structure of the 2015 amendment makes it very difficult to understand its import. Here's a breakdown of the amendment:

- 1** The newly added Section 303.042(f) in the Local Government Code provides that a leasehold interest "shall be treated in the same manner" as a leasehold or other possessory interest in real property granted by an authority under Section 379B.011(b) of the Local Government Code.
- 2** Section 379B.011(b), which applies to defense base development authorities, provides that Section 25.07(a) of the Tax Code applies to a leasehold interest granted by a defense base development authority in the same manner as it applies to leasehold interests in real property constituting a project described by Section 505.061 of the Local Government Code. Section 25.07(a) is the provision requiring leasehold interests of longer than a year to be taxed in the name of lessee versus the lessor and thus makes the leasehold interest taxable if the lessee is not exempt.
- 3** Section 505.061 provides that Section 25.07(a) of the Tax Code does not apply to a leasehold or other possessory interest granted by a Type B economic development corporation during the period the corporation owns projects on behalf of the authorizing municipality.

Here's another way of breaking down how the new exemption is structured in the Local Government Code, by reading the relevant statutory provisions in reverse:



Given the legislative history behind the 2015 public facility corporation exemption, most legislators likely did not know they were creating a new property tax exemption for private apartment developers. Section 303.042(f) was added to the Local Government Code as part of House Bill 2679 in a Senate Floor amendment.

When House Bill 2679 was initially introduced in the House, it lacked Section 303.042(f) and the tax exemption extension provided by that section. Jim Plummer, a private real estate attorney representing the City of San Antonio Housing Trust's public facility corporation, testified in committee that the bill created no substantive changes and was merely a "clean-up bill" with only "technical" changes, which was the case with the legislation when it was heard in committee.⁷ While the bill was being considered on the floor of the Senate, Senator Craig Estes introduced a floor amendment that added Section 303.042(f)⁸. After Senator Estes introduced the amendment, the following dialogue ensued on the floor with one of his Senate colleagues:

Senator Seliger: "Senator Estes, my understanding is that these are public facility corporations, but can they transfer these tax exemptions from leasehold agreements to non-governmental entities, and thereby pass on a tax exemption that they get to a private entity that has not applied for a tax exemption and would not otherwise be getting one?"

Senator Estes: "Senator, only if they continue in that non-profit status."

Senator Seliger: "I'm sorry I didn't hear you."

Senator Estes: "Only if they continue in that non-profit status."

Senator Seliger: **"And so what you are saying is that the non-government entities would be non-profits, not for profits?"**

Senator Estes: **"That's correct. Yep, that's correct."**

With these assurances that only nonprofit entities would benefit from the exemption, the floor amendment and legislation passed, giving rise to the new 100% exemption in Section 303.042(f) on leasehold interests held by private for-profit entities.

In 2019, additional attempts were made to further broaden the availability of the property tax exemption available under Section 303.042(f). Both chambers of the Texas Legislature passed Senate Bill 1861, which, but for the Governor's veto, would have amended Section 303.042(f) of the Local Government Code to explicitly allow multifamily residential developments leased by public facility corporations to private developers to receive a 100% exemption even if none of the units were affordable, as long as the development accomplished

a “governmental purpose” of the sponsor, with no delineated limitations on the definition of “governmental purpose.” Alternatively, a project could qualify for the exemption if at least 50% of the units were leased to households earning less than 80% of the area median family income.

Part Three. Inventory of Post-2015 PFC-Leasehold Interest Deals

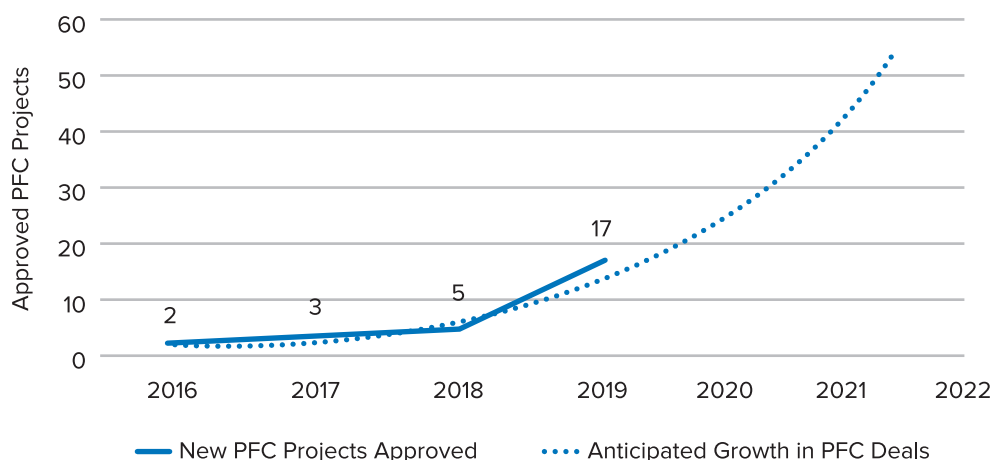
The 2015 amendments to the Public Facility Corporation Act have ushered in dozens of apartment deals that are eligible for a 100% tax exemption under Section 303.042(f) of the Local Government Code. These deals include both new construction projects as well as the acquisition of existing apartment complexes.

One of the primary goals of our research project was to develop an inventory of PFC apartment deals facilitated by the 2015 amendments to Section 303.042(f), to allow for a deeper examination of the impacts of the new exemption. We thus concentrated our research on deals where public facility corporations partnered with private developers utilizing a privately-controlled leasehold interest structure (where the PFC serves as the limited partner of the limited partnership). These deals are all conventionally financed and do not utilize tax-exempt bonds or housing tax credits.

However, in the latter stages of our research, we identified several recent conventionally-financed public-private partnerships where the public entity is serving as the general partner of the limited partnership holding the leasehold interest in the property. This is the case for PFC deals sponsored by the Dallas Housing Authority and non-PFC deals sponsored by the Travis County Housing Finance Corporation. Primarily for comparisons purposes, we included these deals in our inventory, but only if they relied solely on conventional financing, and we noted the different structure in the inventory. This latter set of deals would be tax-exempt even without the 2015 amendments, given the PFC's general partner interest in the entity holding the leasehold interest. See Appendix 1 for a further discussion of the statutory provisions governing the 100% property tax exemption allowed under this latter structure, via Section 11.11(a) of the Tax Code and Sections 392.005 (public housing authorities) and 394.905 (county and city housing finance corporations) of the Local Government Code.

The inventory we developed of PFC apartment deals facilitated by the 2015 amendments is available in Appendix 2 and includes both completed projects and projects under development. The inventory also includes several projects in negotiation, but this category of projects is less comprehensive given the fluctuating nature of negotiations and difficulty we faced identifying earlier stage projects. We welcome input on any projects we may have missed. One challenge we ran into is that there is no public database or required reporting of these deals, and a few public entities were non-responsive to our public information requests amidst the challenges raised by the COVID-19 pandemic. For those entities that did respond to our inquiries, some shared with us in-depth information about their projects, while others provided only cursory information.

FIG. 6
PFC Approval of Apartment Projects
Under Section 303.042(f): 2016-2019



A main take away from the inventory is that PFC support for privately-controlled apartment development projects under Section 303.042(f) moved at a slow pace in the two years immediately following the 2015 amendments but then really took off beginning in 2019, with the approval of 17 new deals that year. See Figure 6. Out of the total 30 apartment projects sponsored by PFCs under 303.042(f) (including projects sponsored in 2020), 22 have been new construction projects, while 8 projects have involved the acquisition and conversion of existing apartment complexes to the tax-exempt PFC structure. We identified at least eight new PFC-sponsored projects in negotiation as of June 2020.

The largest benefactor of the 2015 amendments by far has been the apartment development firm the NRP Group, which helped craft the 2015 amendments. Nine of the 30 tax-exempt PFC deals completed or under development with a privately controlled leasehold interest have been led by the NRP Group, which has at least three additional PFC-leasehold deals with preliminary approval from the local governmental entity and in the development pipeline.

FIG. 7
PFC Deals: Acquisition vs New Construction Projects, as of July 2020

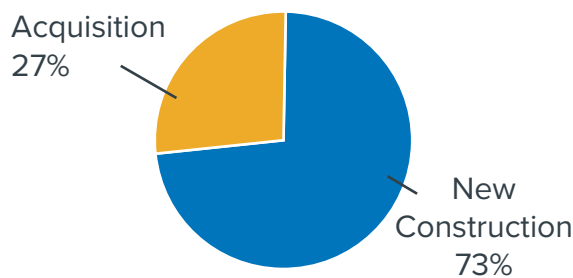
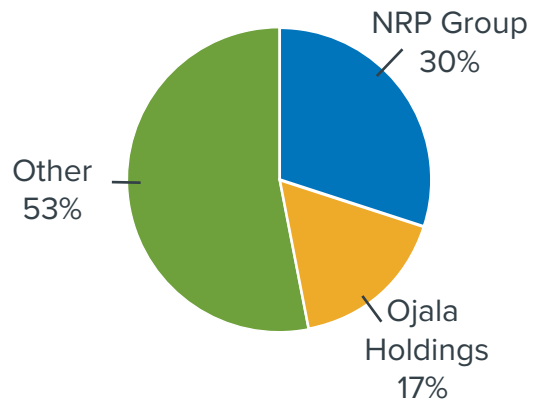


FIG. 8
Private Developer Beneficiaries of the Section 303.042(f) Property Tax Exemption

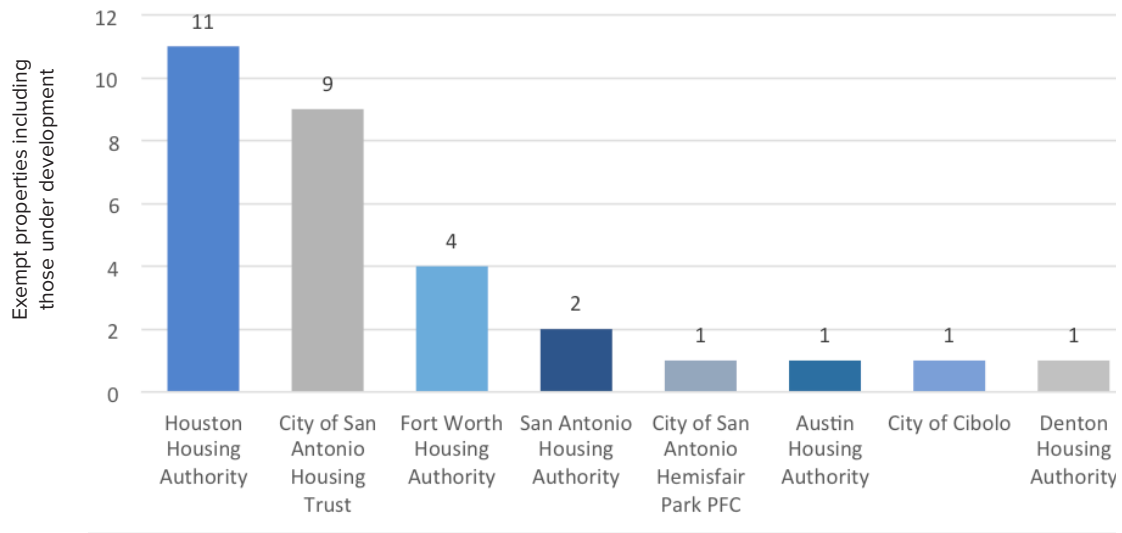


These exempt projects are concentrated largely in the state’s largest metro areas of Houston, Dallas-Fort Worth, San Antonio, and Austin. The two largest producers of PFC-sponsored apartment projects with a privately-controlled leasehold interest have been the Houston Housing Authority (10 deals completed or under development) and the City of San Antonio Housing Trust (9 deals completed or under development). Other public entities partnering with private developers or in negotiations for projects pursuant to this structure include the Fort Worth Housing Authority, the Austin Housing Authority, the City of Cibolo, Huntsville Housing Authority, the Denton Housing Authority, the City of Boerne, and San Marcos Housing Authority. The Dallas City Council also recently authorized the creation of a public facility corporation to pursue projects under this structure.

As noted above, the Dallas Housing Authority has also used PFCs to sponsor several conventionally-financed projects with a 100% property tax exemption, but with the PFC controlling the general partnership interest of the limited partnership with the leasehold interest in the property. And the Travis County Housing Finance Corporation has also recently been sponsoring conventionally-financed projects that will be 100% tax exempt, but not through a PFC.

FIG. 9

Public Entities Utilizing the PFC Tax-Exempt Leasehold Interest Structure under Section 303.042(f): 2016-July 2020



Additional Entities with Section 303.042(f) Exempt Projects in Negotiation
Huntsville Housing Authority | San Marcos Housing Authority | City of Boerne

Part Four. Process and Structure of PFC-Leasehold Interest Deals Under Section 303.042(f)

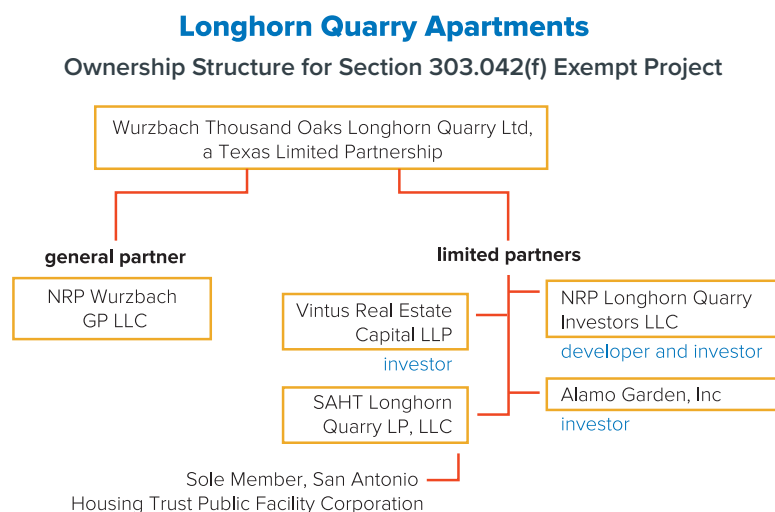
While the process for how local governments end up partnering with private developers in apartment development and acquisition projects for purposes of the Section 303.042(f) exemption varies, most come about when a private apartment developer pitches the deal to the local housing authority or other local government entity. Many of the local jurisdictions we spoke to reported receiving an ongoing flood of requests from developers to partner in a PFC transaction for purposes of securing a 100% property tax exemption under Section 303.042(f) and, for new construction projects, an additional 100% sales tax exemption on construction materials.

If the staff member overseeing housing development projects for the local governmental entity is interested in the deal and thinks it merits support, the staff or general counsel will negotiate a memorandum of understanding (MOU) with the developer containing core terms of the proposed partnership. The MOU will then be presented to the PFC’s board of directors for final approval. If the MOU is approved by the PFC board, then the PFC staff and developer will enter into further negotiations leading up to the execution of a final ground lease and partnership agreement. More recent PFC deals also often include a regulatory agreement, which is recorded in the deed records, and sets forth additional specificity concerning the income and any rent restrictions on the property as well as a process for certifying renters’ eligibility for the income-restricted units. The PFC collaborates with the private developer in communications with the local appraisal district to secure the 100% property tax exemption from the appraisal district on the leasehold interest. If the exemption is lost within five years of the commencement of construction as a result of a legislative change or any reason that is not the fault of the developer, a standard provision in many PFC deal documents requires the PFC to assign over its ownership interest (i.e., fee simple interest) in the property (both land and improvements) to the private developer and investors for \$0 or \$1.⁹

In exchange for the local jurisdiction participating in the partnership in a way that allows for a 100% tax exemption on the project, the developer offers the local jurisdiction some form of financial incentives, which typically, but not always, include an up-front fee (e.g., a developer or acquisition fee). Most PFC deals also offer the local governmental jurisdiction a percentage cut of the net cash flow (10-25%) from the property after the equity investors receive their preferred return on investment (typically 10-15%). However, the actual payment to the PFC will typically end up being minimal by the time the property’s expenses (including debt) and the investors’ returns on equity are paid. More details on these cash benefits—and how they compare to the property tax exemptions—are discussed in Part Five.

The PFC and developer must also agree on the different ranges of affordable housing benefits that will be required. As discussed above, the minimum threshold required under Section 303.043 for housing authorities entering into PFC deals is for at least 50% of the units to be restricted to households making 80% of the Area Median Income, which is usually not adjusted for family size. More on the ranges of affordable housing benefits included in these deals is discussed in Part Five. These commitments are contained in the ground lease for the project and also, in more recent projects, in the regulatory agreement that is recorded in the deed records.

FIG.10



The decision to enter into a leasehold interest deal with a private developer—and thus effectively abate all of the property taxes on the property under Section 303.042(f)—is ultimately made by the governing body of the public facility corporation. For county and city public facility corporations, the PFC’s governing body consists of all or a subset of the county commissioners or city council members. For example, San Antonio Housing Trust’s PFC board consists of five city council members. For housing authorities, the public facility corporation’s governing body typically consists of the board of commissioners for the housing authority.

One issue with the housing authorities’ process for partnering on a leasehold interest deal with a private apartment developer is that the housing authority’s governing board does not consist of any local elected officials. As a result, county, city, and other impacted taxing entities have no say over a decision by an unelected board to exempt 100% of these taxing entities’ property taxes on a project, potentially in perpetuity. One pitch that the proponents of the Section 303.042(f) exemption make is that it provides an important cash flow source to PHAs who are under tremendous financial pressure and unable to fund all of their maintenance needs because of ongoing federal funding shortfalls. However, as a result, PHAs may also then feel more pressure than other public entities to approve these PFC partnerships—even if the “public benefits” from partnering on a Section 303.042(f) project do not outweigh the costs of the 100% tax break, since the housing authorities are not impacted by the loss of tax revenue that arises out of these partnerships.

In contrast, the two largest property tax saving tools available in Texas for economic development projects require approval of the local taxing entities impacted by the property tax relief program.

Other Texas Laws Providing Property Tax Relief on Economic Development Projects

Tax Abatements, Texas Tax Code, Chapter 312: Cities, counties, and special taxing districts, via their governing bodies, may enter into tax abatement agreements with private property owners for a period not to exceed 10 years, and must follow written guidelines and criteria governing the adoption of the agreements. The abatement only covers that taxing entity’s share of property taxes.

Texas Economic Development Act, Texas Tax Code Chapter 313: Allows for economic development agreements with school districts (approved by the school board) that limit the appraised value of large-scale manufacturing, research and development, and other investment projects, in exchange for investments beginning at \$100 million for larger urban areas (reduced for areas with a lower tax base). The limit applies to the taxable property value for school district maintenance and operating tax purposes.



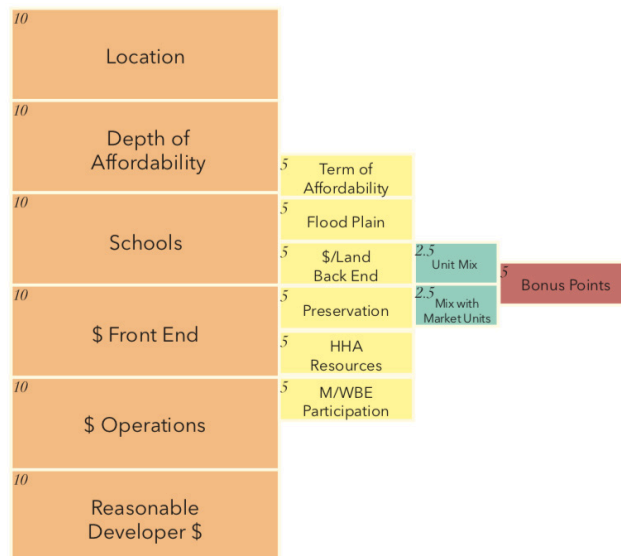
A public facility corporation’s process for entering into the partnerships that result in the 100% tax exemption on these privately-controlled developments is typically outside of a formal application or underwriting process and is instead very ad hoc, often relying on the personal relationships between the PFC staff and the developer. One PFC staff member, for example, reported to us that he chose to partner with a particular developer on a conventionally-financed PFC deal because of their work on prior deals together. The staffer also reported that particular housing terms were not required in the legal documents because he trusted the developer would do the right thing.

A 2020 report by the National Association for Latino Community Asset Builders (NALCAB) on the City of San Antonio’s PFC-sponsored affordable housing projects highlights the problems of not having any delineated

policy goals and formal underwriting criteria for objectively weighing the respective merits of apartment development projects proposed to a local governmental entity.¹⁰ In San Antonio, close to a third of the city’s PFC deals have been with one particular developer, the NRP Group, which formerly employed the PFC’s general counsel. Meanwhile, the same general counsel effectively played the role of the PFC’s executive director in selecting which PFC deals to bring to the board. The general counsel’s roles included “managing communications with developer partners, assessing potential housing projects, negotiating the financial terms of projects with private developers, preparing agendas and materials for board meetings, and acting as the primary presenter during board meetings.”¹¹ Each of the deals then included a provision approving the attorney’s law firm as the closing attorney without any procurement process.¹² When the deals were presented to the five councilmembers on the PFC board, the board members were “left to rely primarily on the advice” of the general counsel serving as a pro bono advisor “to discern the adequacy of deals presented to them.”¹³ The NALCAB assessment team for the report was “unaware of any other agency in which members of Council make financial decisions of similar scope and scale with comparably little advice and support.”¹⁴

The Houston Housing Authority is the only local governmental agency we could identify with in-depth written criteria for evaluating PFC deals pitched by private developers. Under these criteria, which were adopted in 2019 and recently revised, any proposals for partnerships with the Houston Housing Authority must be submitted pursuant to the Housing Authority’s Qualification Based Solicitations, along with a \$2,000 application fee.¹⁵ Proposals are then scored by an evaluation committee, using the score card included in the application packet, before they are then presented to the HHA’s board. The score card looks at a range of criteria by which projects are evaluated, including whether the site is located in a high opportunity area or other priority location, the depth of affordability, the quality of the schools serving the project, the developer’s fee percentage and return on investment, and the financial benefit to the HHA. See Figure 11.

FIG. 11
Houston Housing Authority
Development Scorecard



Once a PFC project is approved by the governing body of the local jurisdiction—such as the board of directors of a housing authority—the public entity and private developer enter into a limited partnership, with the private developer serving as the general partner via a subsidiary entity it controls, and with the developer and equity investors serving as limited partners. The public entity receives a special limited partner interest, typically of less than 0.1%. Once a public entity enters into one of these partnerships, its role is very limited. See Figure 10 for what the typical entity structure looks like for a Section 303.042(f) exempt project.

For new construction projects, the developer typically sells the land for the development to the local government entity, which then leases the land along with the to-be-built improvements to the limited partnership via a long-term ground lease running for 70 to 99 years. The local jurisdiction then secures a property exemption on the leasehold interest, which includes both the land and improvements. If the property tax exemption is revoked within the first five years of the deal through no fault of the developer, then the local jurisdiction is typically to transfer the fee estate (i.e., the entity’s ownership of the land and improvements) to

the limited partnership for \$0 or \$1. In some of the deals, the local jurisdiction is also required to transfer its ownership interest if the exemption is revoked after five years.

There is typically no maximum time period required for the units to remain income-restricted. At any time, the private developer and investors could decide to stop including any income-restricted units, at which time the property loses its property tax exemption and is then subject to property taxes.

The PFC-sponsored properties are also eligible for a 100% sales tax exemption on construction materials because the PFC serves in name as the general contractor for the construction project. The sales tax exemption is estimated to average \$1.3 million per new construction project. Absent the sales tax exemption, about 75% of sales taxes would go to the state, and 25% would go to the local taxing jurisdictions (city, county, transit authorities).

These PFC deals are structured in anticipation of the leasehold interest being sold to a third party after the property is leased up, usually within five years of construction, with the developers and private equity investors exiting the investment. According to industry officials, the internal rate of return to the investors on these deals has ranged from 15-20%. The PFC has no control over whom the property is sold to. When the leasehold interest is sold, the local governmental entity typically has the option to stay in the partnership, which results in the continuance of the property tax exemption and affordable housing commitments.

The first three tax-exempt PFC leasehold deals in San Antonio have already been sold to third parties, with the City of San Antonio choosing to stay in the partnerships. For example, at the Baldwin in San Antonio, the NRP Group, which was the developer, sold the property for \$62 million after two years of being developed, with profits of \$10 million to the NRP Group and investors (who had made an equity investment in the property of around \$10 million).¹⁶ When the property was sold, one option available to the City of San Antonio was to receive 10% of the net proceeds of the sale, which was approximately \$949,000, and put the property back on the property tax rolls. The City chose instead to remain as a limited partner and keep the property off the tax rolls in exchange for receiving a portion of the net cash flow from the property. This deal is discussed further in Part Five.

PFC Partnership Process Under Section 303.042(f)

- 1 A developer pitches an acquisition or new construction of an apartment complex to a public housing authority or city/county housing finance corporation.
- 2 The developer and local government staff negotiate the financial benefits to the local jurisdiction and the affordability restrictions or terms to be included.
- 3 The public entity's governing body approves the deal (i.e., the Housing Authority Board of Commissioners, the City Council, or County Commissioners Court).
- 4 For new construction projects, the developer sells the land to the PFC and the PFC leases the land and to-be-built improvements to a limited partnership entity controlled by the developer (typically for 75-99 years). For acquisition projects, the developer sells the land and improvements to the PFC, which are then leased back to the limited partnership.
- 5 A 100% property tax exemption is secured on the property from the local appraisal district.
- 6 The developer, via the limited partnership entity, builds and rents out the apartment complex (for new construction projects), with a 100% sales tax exemption on construction materials.
- 7 At year three to year five, the developer and investors typically cash out of the deal, and the leasehold interest is sold to a third party. The PFC can choose to remain in the partnership, which extends the property tax exemption on the property.

Part Five. Public Costs and Benefits

In this section we provide a more in-depth examination of the property and sales tax impacts from the 100% exemptions on these privately-controlled properties along with the public benefits produced by these projects, with an emphasis on the affordable housing benefits.

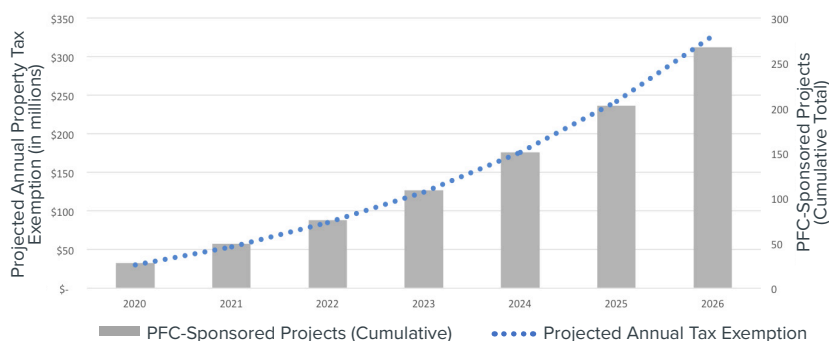
PROPERTY AND SALES TAX IMPACTS

Since Section 303.042(f) was enacted, at least 18 completed PFC-sponsored apartment projects have received a 100% property tax exemption under Section 303.042(f), and another 12 properties are under development and will receive a 100% exemption on the completed development in the next one to two years. The property tax exemption on the 18 completed projects averages close to \$950,000 per property a year. We estimate that the annual exemptions on all 30 of these properties, once completed, will total more than \$32 million a year. The average property exemption for each income-restricted unit comes out to approximately \$7,400 a year, or \$616 a month per restricted unit.

With the use of this property tax exemption tool really taking off in 2019 (with 17 projects approved compared to 10 projects in the prior three years), the next five years could see hundreds more conventionally-financed apartment projects use this structure. Assuming a 25% annual growth in new PFC-sponsored apartment projects with conventional financing, by the close of 2026, Texas could see more than 267 of these apartment complexes off the tax rolls with property values of more than \$12 billion—resulting in a loss of approximately \$326 million a year in property tax revenue to local taxing districts and the state public education budget.¹⁷

For PFCs sponsoring apartment projects for economic development purposes, one rationale put forward for the tax exemption available under Section 303.042(f) is that the new construction projects would not have been built without the exemption. As a result, proponents assert that the exemption on these projects does not result in a net loss of property tax revenue. This argument relies on an assumption that the land would otherwise remain vacant and never be developed on, although even in that case the land would have continued to generate property tax revenue.

FIG. 12
Projected Property Tax Exemptions in 2026
on PFC-Sponsored Apartment Projects under Section
303.042(f)¹⁸



PFCs utilizing the exemption to promote economic development also assert that certain apartment projects, depending on their location, can spur additional development in the area and produce additional property tax revenue for the local taxing jurisdictions served by the development. We did not evaluate the extent to which this has occurred so far, but we believe it is worth investigating further as more apartment projects are developed with an exemption under Section 303.042(f). See the discussion below under public benefits for some of the issues raised by this economic development rationale.

• Impact on Local Jurisdictions

In San Antonio and Houston, the two cities with the largest number of these deals, the fiscal impact from PFC-sponsored projects under Section 303.042(f) is as follows, both in terms of projects already approved as well as projections for what the property exemptions will look like in 2026, assuming the local governmental entities in each city enters into four new deals a year from 2020-2025, which is the number of deals that were approved in San Antonio in 2019 and less than the number of new deals approved in Houston in 2019.

FIG. 13

San Antonio: PFC-Sponsored Apartment Projects under Section 303.042(f) and Property Tax Impacts

12 Approved PFC Projects as of June 2020

3,406 TOTAL UNITS

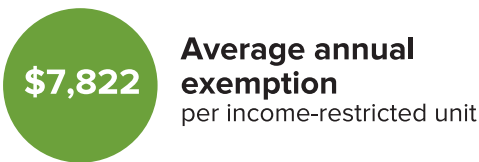
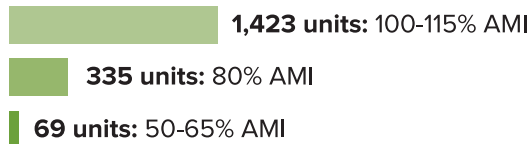


1,679 MARKET UNITS



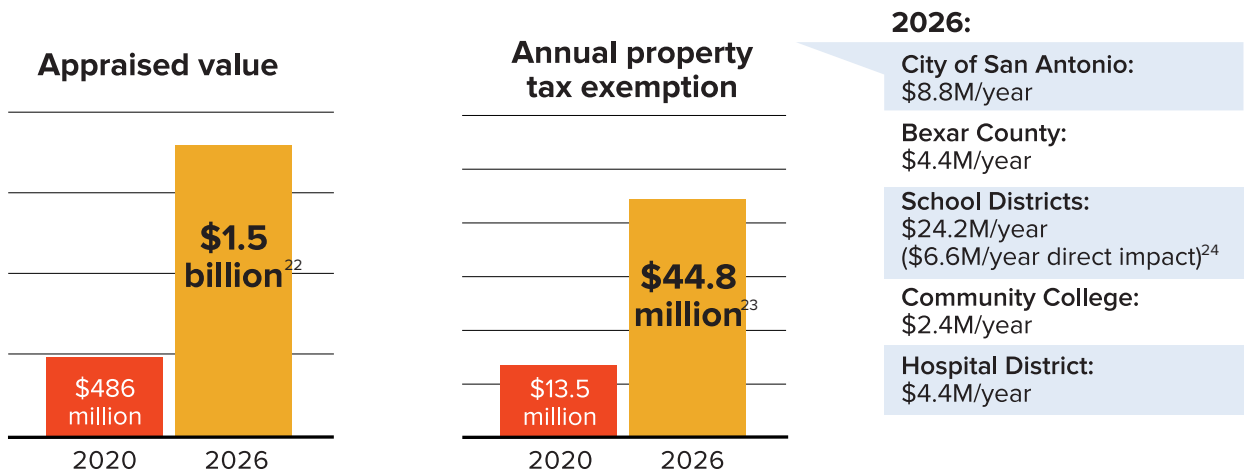
1,727 INCOME-RESTRICTED UNITS

Income restrictions when adjusted for family size



City of San Antonio:	\$2.7M/year
Bexar County:	\$1.3M/year
School Districts:	\$7M/year (\$1.9M/year direct impact) ²¹
Community College:	\$724,000/year
Hospital District:	\$1.3M/year

Projected Property Tax Impacts in San Antonio in 2026 for 36 PFC Projects*



*36 projects = 12 projects approved as of 2019 + 4 new projects approved each year for 2021-2025

FIG. 14

Houston: PFC-Sponsored Apartment Projects under Section 303.042(f) and Property Tax Impacts

11 Approved PFC Projects as of June 2020

3,152 TOTAL UNITS



1,501 MARKET UNITS



1,651 RENT-RESTRICTED UNITS

Income restrictions when adjusted for family size

815 units: 100-115% AMI

621 units: 80% AMI

215 units: 50-65% AMI

\$6,662 Average annual exemption per income-restricted unit

\$446 million²⁵

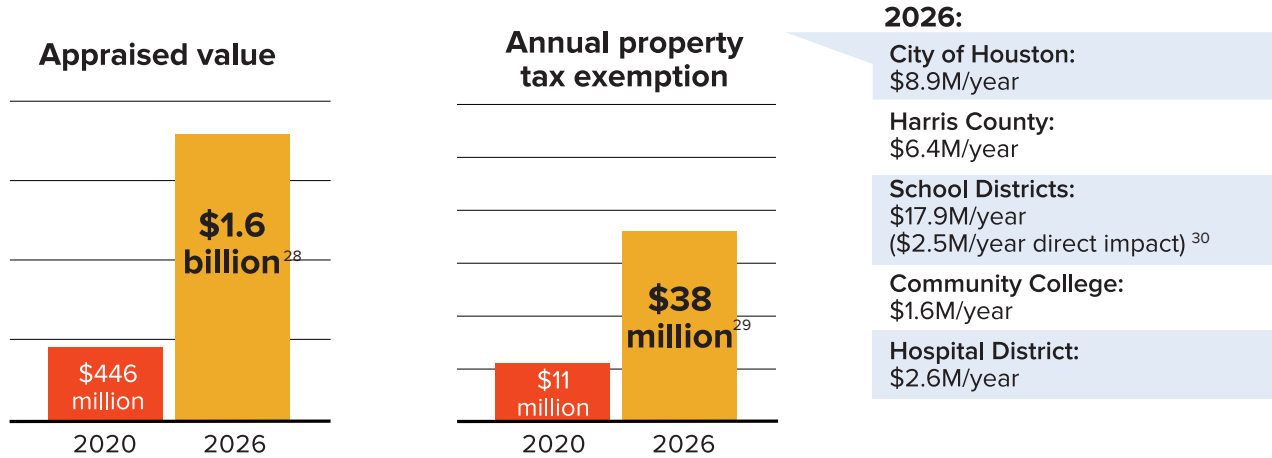
Appraised value

\$11 million²⁶

Annual property tax exemption

City of Houston:	\$2.5M/year
Harris County:	\$1.8M/year
School Districts:	\$5.2M/year (\$725,000/year direct impact) ²⁷
Community College:	\$447,000/year
Hospital District:	\$735,000/year

Projected Property Tax Impacts in Houston in 2026 for 34 PFC Projects*



*34 projects = 10 projects approved as of 2019 + 4 new projects approved each year for 2021-2025

• **Impact on Public Schools**

About half of all property taxes are levied by school districts in Texas. Assuming at least 267 PFC properties will be tax exempt in 2026, Texas would see at least a \$163 million loss in funding in that year for public education through the PFC exemption.³¹

Counties, cities, and housing authorities approving these tax-exempt deals have emphasized that their approval of these tax-exempt structures does not impact local public education funding, but that is not the case. A school district’s portion of the property tax bill is based on two different types of tax rates. The first tax rate is called the “interest and sinking” (I&S) rate, which is used to cover debt service for bonds approved by taxpayers to build schools, pay for new technology equipment, and cover other capital costs. The second rate is for maintenance and operation (M&O) and covers the bulk of public education expenses such as teacher and staff salaries.

When a 100% property tax exemption is awarded to a property, the school district loses out directly on 100% of the I&S portion of the property tax bill. For a property appraised at \$45 million (the average exemption for approved PFC projects), this amounts to around \$55,000 (Austin ISD) and \$208,000 (San Antonio ISD) a year per property in lost tax revenue to the school district, although the loss could be as high as \$320,000 a year for districts with higher I&S rates.³² Over 20 years, the impact in Houston and San Antonio would be around \$1.6 million to \$4.2 million per property (not accounting for increases in tax rates or values) that would otherwise go towards building and technology equipment expenses in the city’s school districts.³³ And by 2026, if a city like San Antonio were to have 36 of these exempt properties (as per the projections above), the school districts in the city would experience a direct loss of \$6.6 million or more a year in I&S tax revenue for these important capital expenses.

For the M&O part of the tax bill, the same PFC property appraised at \$45 million is exempted from paying around \$483,000 a year in property tax revenue to the local school district (based on Austin ISD’s tax rate of \$1.079% and San Antonio ISD’s rate of 1.068%). This portion of the exemption doesn’t necessarily have a direct impact on the school district, however, given the way public education revenues are redistributed to districts based on a range of complicated formulas. But it does result in an overall reduction in public education dollars going to the state and then being distributed for public education across the state. The more exempt properties there are, the less money our state has to fund public education across the state, which ultimately impacts each school district. If San Antonio ends up with 36 exempt PFC-sponsored properties, that means a loss of approximately \$17.6 million a year in M&O revenue for public education across the state.³⁵

• **Sales Tax Impacts**

PFC-sponsored apartment developments are also eligible for a 100% sales tax exemption on the construction materials for the development, because the PFC serves in name as the general contractor on the project. About 75% of sales taxes are paid to the state, with the rest going to the city, county, public transit agencies, and other local governmental entities. We estimated the average exemption on new construction

FIG. 15

PFC Property Tax Exemption: Impact on Schools in San Antonio³⁴



Direct impact on capital expenses (e.g., buildings, technology equipment, etc.):

\$4.2 million per property over 20 years

\$6.6 million a year for projected 36 exempt properties in 2026



Indirect impact on public education revenue

\$11.2 million per property over 20 years

\$17.6 million a year for projected 36 exempt properties in 2026

FIG. 16

Loss of Sales Tax Revenue from 21 PFC-Sponsored Apartment Developments (2016-2020)

Average sales tax break per property: **\$1.3M**

Total sales tax break: **\$25M**

properties sponsored by PFCs to be approximately \$1.3 million per project, with the precise amount depending on the size and type of development. We calculated this average by assuming \$50,000 in construction material costs per unit, based on input from an affordable apartment developer, for an average sales tax exemption per unit of \$4,125. We estimated the sales tax exemption provided on all 21 new construction projects approved from 2016 to present to be approximately \$25 million. We attempted to obtain the exact exemption amount on actual PFC-sponsored projects, but when we asked the local PFC officials about the sales tax exemptions they were providing to private developers through their partnerships, they did not know how much of a sales tax break they were giving up in these deals.

PUBLIC BENEFITS

As mentioned in the introduction, the following three benefits are touted as a justification for the 100% property tax exemption on these PFC-sponsored projects:

1. **Affordable housing: Creating affordable housing serving middle-income renters in the workforce who are not served by either the market or most government affordable rental housing programs.** A few housing agencies also tout the exemption as a way to incentivize the inclusion of more deeply affordable housing serving lower-income households.
2. **Funding stream: Filling government housing agencies' coffers with funds they can use to support more deeply affordable housing projects.**
3. **Economic development: Incentivizing new Class A, market-rate apartment development in disinvested low-income neighborhoods or other areas where the market will not build higher-end apartments.** Spurring other economic development in the area.

We examine each of these benefits in turn, with an emphasis on the affordable housing benefits.

• Public Benefit: Affordable Housing

The most common rationale put forward for allowing a 100% property tax exemption on these apartments projects is that the exemption promotes the creation of affordable housing. In particular, proponents of the exemption for PFC leasehold deals in Section 303.042(f) say that the exemption incentivizes the development of rental housing that is affordable to middle-income households not currently served by the market, with an emphasis on households making around 80% of the Area Median Income (AMI).

As pointed out by one local housing agency official, one of the key issues and challenges with an exemption on these conventionally financed projects is that, unlike traditional affordable rental housing finance programs, the PFC exemption comes with no standards or guidelines other than the requirement in Section 303.042(d) that at least 50% of the units are reserved for occupancy by individuals and families earning less than 80% of the median family income. And this requirement only applies to projects sponsored by public housing authorities. As a result, each local housing agency using this exemption tool is essentially creating a new housing program from scratch, often through their negotiations with private developers who will benefit from the exemption, and often without knowing what the best practices are for ensuring the best affordable housing outcomes possible. None of the agencies using this tool appear to be talking to each other about issues that have arisen as well as best practices.

In our examination of dozens of conventionally-financed PFC leasehold interest deals, local market data, local housing needs, and national best practices, we identified a number of issues with the ways in which Section 303.042(f) is being implemented as a tool to promote affordable housing. Several local government housing officials working on these deals have pointed out they recognize these issues and have been working to strengthen the affordable housing components of their PFC projects. A common theme we heard in our conversations with local jurisdictions is that the first round of deals they completed “could have been done better.”

Issue #1: No rent restrictions.

Unlike most every other affordable housing subsidy program, as well as the state's other major property tax break for affordable housing development (under Section 11.1825 of the Tax Code), the exemption available under Section 303.042(f) does not require any rent restrictions on the income-restricted units. As a result, out of 28 properties that are exempt under Section 303.032(f) and that we could obtain the legal documents for, only 7 follow the affordable housing industry standard of capping the rent of the income-restricted units at 30% of monthly income for a household at 80% AMI (or other applicable AMI restriction level). Sixteen of the properties with a Section 303.042(f) exemption have no rent restrictions whatsoever, while the other five properties impose rent restrictions at 35% of the applicable AMI restriction level. See the PFC Inventory in Appendix 2 to see what rent restrictions, if any, are being utilized at the specific exempt properties.

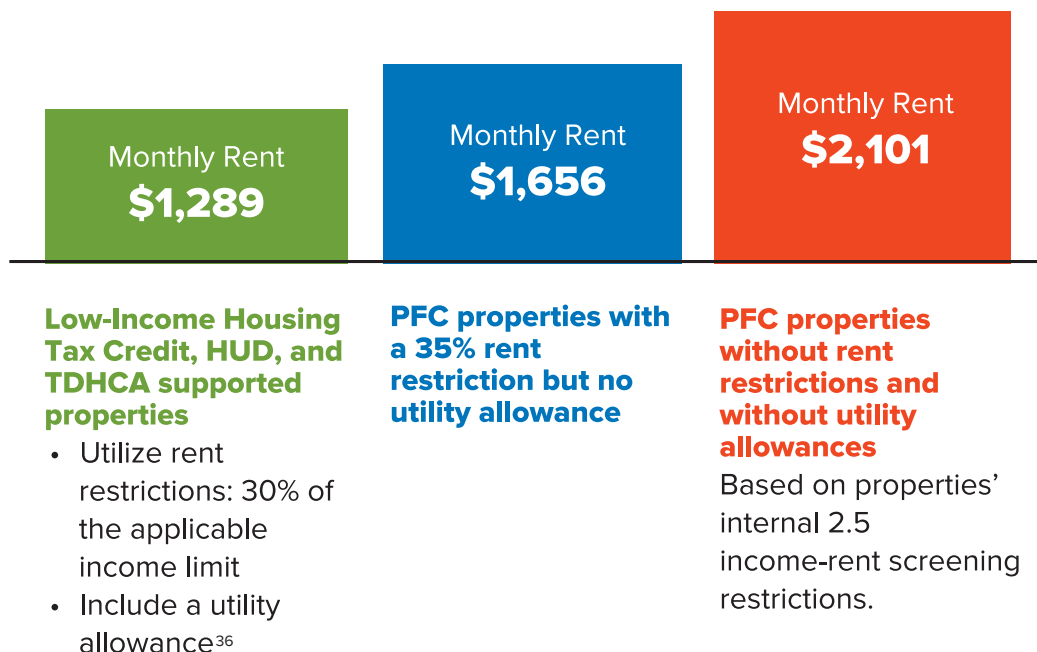
For income-restricted units without a rent restriction, the implication is that the rents do not have to be set at a rate that is considered to be affordable to a household at that income level. Most of the PFC-sponsored properties require as a matter of policy (based on apartment industry standards) that households have incomes of at least 2.5 times the rent, which means a renter making 80% AMI could be paying up to 40% of their income on rent to the extent the market supported such rents.

In contrast, most other government-sponsored affordable rental housing programs cap rents at a level totaling not more than 30% of a household's monthly income at the relevant income targeting level, to help ensure the household has enough money for other important household expenses. Under these standards, for example, for a unit restricted to a household making up to 80% AMI, the unit's rent cannot exceed 30% of the monthly income for an 80% AMI household. Under HUD policies, a low-income household that pays more than 30% of their income on rent is considered to be cost burdened and will have difficulty paying for other essential living expenses.

FIG. 17

Maximum Rents Allowed at Apartment Complexes for 2-Bedroom Units Restricted to Renters Making up to 80% AMI (2020)

(= based on 4-person household making up to \$63,040 in the Houston metro area)



The largest and most established affordable housing programs in the country (such as the Low Income Housing Tax Credit program, the Home program, Housing Choice vouchers, and public housing) also incorporate a utility allowance into the 30% rent cap, to take into account what a tenant is likely to spend in utilities at the complex. When a utility allowance is incorporated into the rent restriction for a unit restricted at 80% AMI, the unit’s rent together with the utility allowance cannot exceed 30% of the monthly income for an 80% AMI household (although households making below 80% AMI end up paying a larger percentage of their income towards rent). We could not identify any PFCs that require a utility allowance in their Section 303.042(f) exemption deals.

In summary, while the Section 303.042(f) exemption is touted as a way of promoting affordable housing, the implication of not having restrictions in place that cap rents at 30% of monthly income for a household at 80% AMI is that the developer is not required to offer the rents at a level that is actually affordable to renters at that income level. This in turns makes the renters much more vulnerable to losing their housing and more difficult for the renters to cover other basic household needs. If the rents end up being affordable at the complex, that is only because the market does not support the developer charging higher rents. But there is no guarantee that the rents will remain affordable if and when market conditions support higher rents. And for renters whose income fall below the 80% AMI cap, their share of monthly income needed to live at the property will be even higher.

Issue #2: No adjustment in area median income for household size.

Another major issue is that the 80% AMI restriction in the PFC statute is not required to be adjusted for household size—and most of the PFC-sponsored apartment complexes with an exemption under Section 303.042(f) do not require an adjustment of the income restrictions based on household size (also referred to as family size in affordable housing programs). In contrast, a standard requirement in other affordable housing programs is to adjust the income restrictions for family size, i.e., based on the number of persons living in the same unit. That’s because average household incomes vary broadly based on the number of workers in the household. A single-person household with one worker, for example, on average makes less than a household with two workers. Each year HUD releases updated AMI levels that are adjusted for family size to take into account these income differences across household sizes, combined with assumptions about the number of bedrooms required to house families of different sizes.

A one-bedroom unit restricted at 80% AMI adjusted for family size will target households with lower incomes than a two-bedroom unit restricted at 80% AMI. When coupled with rent restrictions, the rent caps will also be lower in a one-bedroom unit compared to the larger units. The sharp contrast in income and rent restrictions depending on whether the AMI levels are adjusted for family size can be seen in Figures 18-20 below.

FIG. 18

Comparison of Income Restrictions Based on Adjustment for Family Size in the Houston Metro Area

Income restriction at a PFC-sponsored apartment complex with 80% AMI restrictions not adjusted for family size: **\$63,040**

VS

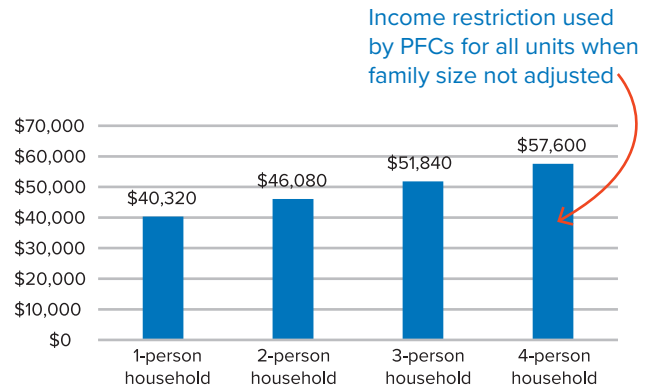
Income restrictions adjusted for family size

Household size	80% AMI	100% AMI	115% AMI	120% AMI
1-person household	\$44,150	\$55,188;	\$63,465	\$66,200
2-person household	\$50,450	\$63,063	\$72,522	75,600
3-person household	\$56,750	\$70,938	\$81,578	\$85,100
4-person household	\$63,050	\$78,813	\$90,634	\$94,550

HUD, FY2020 MFI, Houston-Woodlands-Sugarland, TX, HUD Metro Area

When the AMI is not adjusted for family size in a PFC-sponsored project, an 80% AMI restriction actually ends up targeting households making up to 100%-115% AMI for the efficiency and one-bedroom units (which is where the vast majority and often all of the income-restricted units in PFC deals are concentrated). For example, in the Houston region, the 2020 AMI estimate released by HUD is \$78,800, and 80% of the AMI is \$63,040.³⁷ According to HUD, for a one-person household, 80% of the AMI in the Houston region is \$44,150, and for a two-person household 80% of the AMI is \$50,450.³⁸ If a PFC's legal documents do not require that the AMI be adjusted for family size, then a Houston development, for example, can serve renters making up to \$63,040 even if that household is a one-person household. But, when family size is taken into account, a \$63,040 income limit is actually targeting a one-person household making 115% of the AMI and a two-person household making 100% of the AMI—a group of renters who are served very well by the rental housing market and do not have a need for government-subsidized rental housing. In all five of the largest counties in the state, there is a surplus of units that are affordable and available for rental households making 100-115% of the AMI—and only a tiny fraction of renters at these income levels face a severe cost burden in the rental housing market. See Figures 25 and 26 below.

FIG. 19
80% AMI Adjusted for Family Size in San Antonio



Even when a PFC has adopted a 30% rent restriction, when the incomes are not adjusted for family size, the rent restrictions on the efficiency and one-bedroom units in a PFC-development are much higher than the rent restrictions under other affordable rental housing programs. For example, in San Antonio, a single person living in an 80% AMI efficiency unit under a standard affordable housing program could be legally charged no more than \$932 a month in rent. Whereas that same person living in a rent-restricted apartment

FIG. 20

Comparison of Rent and Income Limits for Government-Subsidized Housing in the San Antonio-New Braunfels HUD Metro Area Based On Whether Adjustments Are Made for Family Size, 2020

HUD 80% AMI: Income and Rent Limits³⁹
AMI adjusted for family size

- utilizing a 30% of 80% AMI rent restriction
- utility allowance included

PFC 80% AMI: Income and Rent Limits
AMI not adjusted for family size

- utilizing a 30% or 35% of 80% AMI rent restriction
- no utility allowance

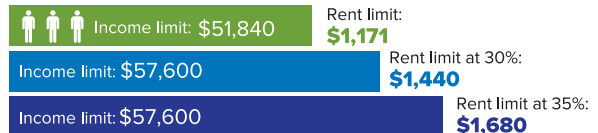
Efficiency unit



1-bm unit



2-bm unit



unit sponsored by a PFC could be legally charged up to \$1,440 a month for that unit. See Figure 20. This comes out to a difference in rent of \$508 a month. For a single person making \$40,000 a year (which is 80% AMI for a one-person household), a \$1,440 monthly rent would result in the person paying 45% of their income on rent and utilities. The contrast in the maximum allowable rents for efficiency units with 35% rent restrictions based on whether the property must adjust the AMI for family size is even higher: a difference of \$748 a month. See Figure 21. While the market might not actually support rents at these higher levels, without an adjustment for family size, the PFC has no way of guaranteeing that its target populations will be served with rents that are actually affordable.

In summary, if a PFC wants to guarantee it is addressing its city’s housing needs and actually serving households making up to 80% AMI with rents they can afford, the PFC needs to require both rent restrictions and AMI adjustments for family size in the developments it is sponsoring under Section 303.042(f).

A related issue we identified when it comes to income targeting is that many of the PFC-sponsored projects’ legal documents only require the property to consider the income of the person on the lease and not the entire household. As a result, if there are other income earners living in the unit, their income will not be considered, making it more likely that the unit could end up serving a household over the income limit. The standard in the affordable housing industry is for the household income to take into account everyone living in the unit—and not just the person on the lease.

Issue #3: Failure to target households in need of rental subsidies.

By targeting mostly one- and two-person households making 80%-115% AMI, the very generous tax subsidies provided to apartment complexes under Section 303.042(f) end up serving higher-income renters who are already, by and large, adequately served by the market—in contrast to households with lower-incomes. And the rents on the 80-115% AMI restricted units at these properties end up being comparable to market rents of other newer, non-subsidized apartments.

Given that the average property exemption per income-restricted unit at properties with a Section 303.042(f) exemption is \$7,400 a year, or \$616 a month (dividing the total value of the exemption by the number of income-restricted units at each property), the property should at least be guaranteeing affordable rents at levels that are significantly below market rents offered at other new non-subsidized properties in the area. An attorney involved in PFC leasehold deals under Section 303.042(f) mentioned that local government entities creating PFCs have been taking a closer look at the gaps between

FIG. 21
Comparison of 80% AMI Rent Caps: Affordable Housing Industry Standards vs PFC Projects in San Antonio Metro Area

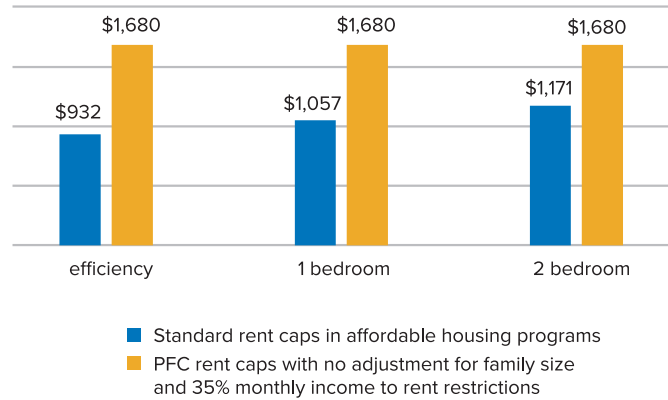
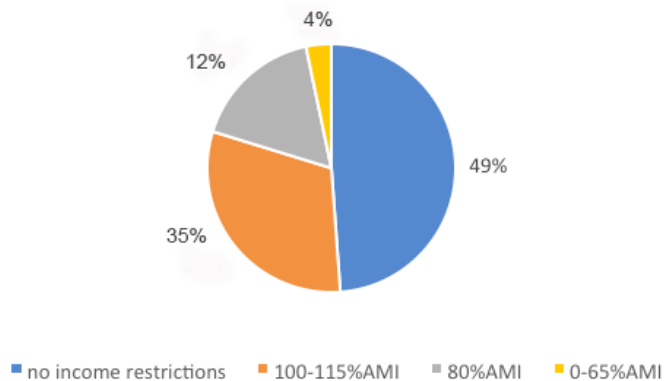


FIG. 22
Income Targeting Levels for 8,906 Apartment Units at Properties with the Section 303.042(f) Exemption When Adjusted for Family Size*



*Assuming that the four PFC properties with unknown AMI policies actually do adjust the AMI for family size

the market rents and PFC property rents and at least one entity has been trying to lock in a rent differential of \$150-\$200 a month. However, none of the entities have successfully required a rent differential yet.

Other housing subsidy programs go much further in bridging affordability gaps and serving households in need. For example, a 2015 study found that the average annual housing subsidy for voucher households and public housing residents was \$7,600 a year—comparable to the annual PFC tax subsidy per each income-restricted unit. But, in contrast to the Section 303.042(f) tax subsidy, which almost exclusively targets households making above 80% AMI, the average income of voucher holders is well below 30% AMI.⁴⁰

FIG. 23

San Antonio: 12 PFC Projects with Section 303.042(f) Exemption Approved as of June 2020

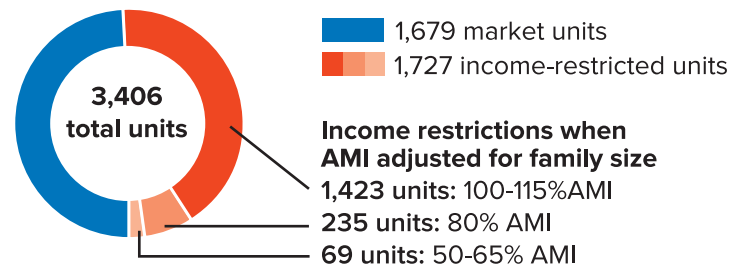
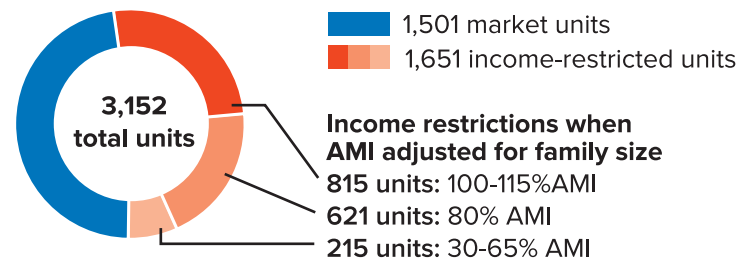


FIG. 24

Houston: 11 PFC Projects with Section 303.042(f) Exemption Approved as of June 2020

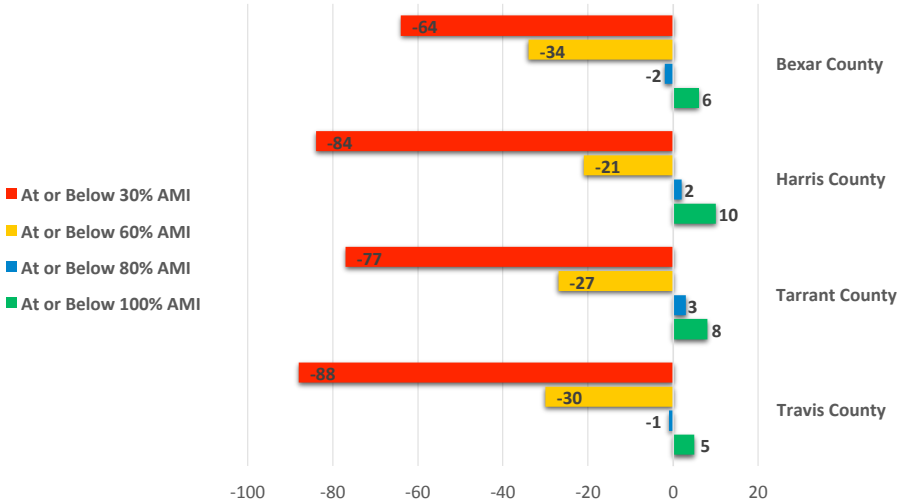


Out of 8,906 units in completed properties or properties under development receiving a property tax subsidy under Section 303.042(f) in Texas, only 4% of the units have income restrictions targeting households making 0-65% AMI once the AMI is adjusted for family size. And only 12% of the units target households making 80% of the Area Median Income once the AMI is adjusted for household size. The bulk of the income-restricted units target households making at or above the median income. That’s because, as discussed above, the 80% AMI restriction used in most of these properties is not adjusted for family size and thus the restriction allows the property to actually serve one-person and two-person households making the equivalent of 100%-115% AMI for households of that same size in the metro area.

The marginal benefits that the Section 303.042(f) exemption has provided to renters in need of subsidized housing San Antonio and Houston can be seen in Figures 23 and 24.

In the state’s metro areas where almost all the Section 303.042(f) exempt properties are concentrated, the housing market is overall doing a good job of serving households at 60%-115% AMI. As shown in Figure 25, Harris, Dallas, Bexar, Tarrant, and Travis Counties all have a surplus of rental housing for renter households making up to 100% AMI as well as those making above the median income. And both Tarrant and Harris Counties have a surplus of units for households making up to 80% AMI. Less than 3-5% of households making 61% or above the AMI face a severe cost burden in these five counties. See also Figure 2 for statewide data regarding surplus units. In contrast, 47-54% of renters making up to 60% AMI in the same metro areas are severely cost burdened. See Figure 26.

FIG. 25
Deficit or Surplus of Affordable and Available Rental Units
Per 100 Rental Households at or Below AMI Thresholds



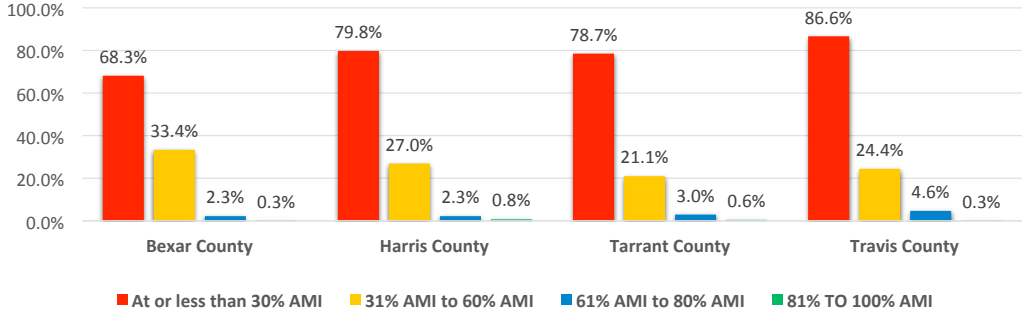
Source: National Low-Income Housing Coalition tabulations of 2018 ACS PUMS

While Bexar and Travis Counties each have a small deficit of rental units that are affordable and available for households making up to 80% AMI, the biggest gaps between market rents and affordable rents are in two- and three-bedroom units, not in the efficiency and one-bedroom units where the PFC-sponsored properties are concentrating the income-restricted units.

In Bexar County and the surrounding metro area, the average rent for market-rate efficiency and one-bedroom units built within the past ten years is below the 80% AMI affordable rent for efficiencies and one-bedroom units issued by HUD, which is adjusted for family size. The same is true for Travis County and the surrounding metro area. See Figures 27 and 28.

As part of our research, we obtained the rents at newer apartment complexes built without subsidies that are located near PFC-sponsored properties in four different cities. Specifically, we calculated the median rents

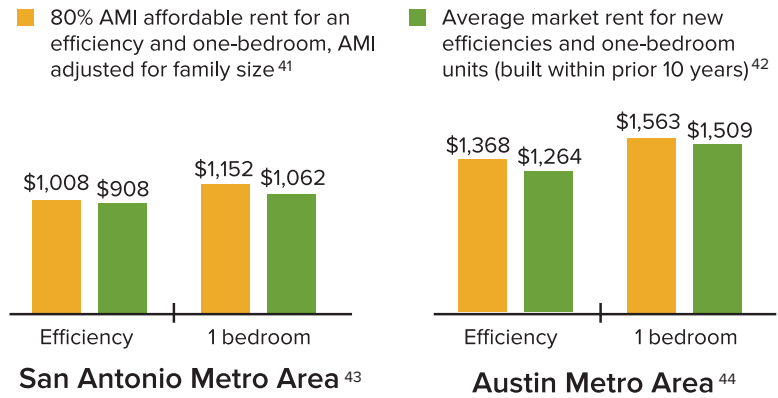
FIG. 26
Percent of Renter Households with Severe Cost Burden
(Paying More than 50% of Income on Rent)



Source: National Low-Income Housing Coalition tabulations of 2018 ACS PUMS

FIG. 27

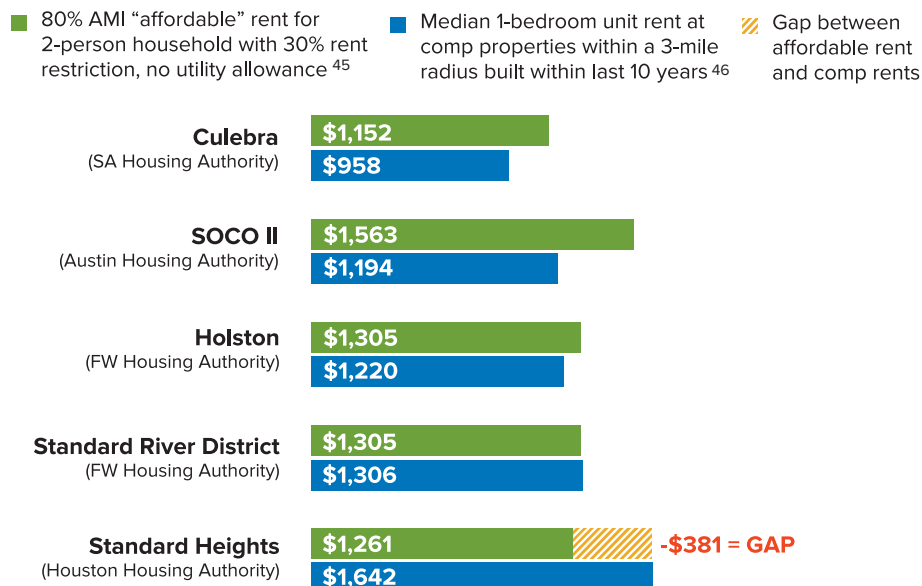
Comparison of 80% AMI Rents and Market Rents at New Non-Subsidized Apartments



charged for one-bedroom units at non-subsidized properties built in the prior ten years and located within a three-mile radius of five apartment complexes with a Section 303.042(f) exemption. We then compared these median “comp” rents for these one-bedroom units with the rents that are affordable to a two-person household in the region making 80% AMI adjusted for family size, based on a 30% rent restriction but not utilizing a utility allowance since none of the PFC properties utilize an allowance. At four of the five PFC-sponsored properties, the median comp rents for one-bedroom units in the area were basically the same or lower than an affordable 80% AMI rent. The fact that the median comp rents were not higher than the affordable rents calls into question the public policy rationale for providing a property tax exemption on these PFC-sponsored properties. In contrast, at the fifth PFC-sponsored property, the median comp rents for one-bedroom units were significantly higher than what a renter at 80% AMI could afford, providing stronger support for a tax exemption on this particular property.

FIG. 28

Comparison of 80% AMI Affordable Rents and Median Rents at PFC Comp Properties for 1-Bedroom Units



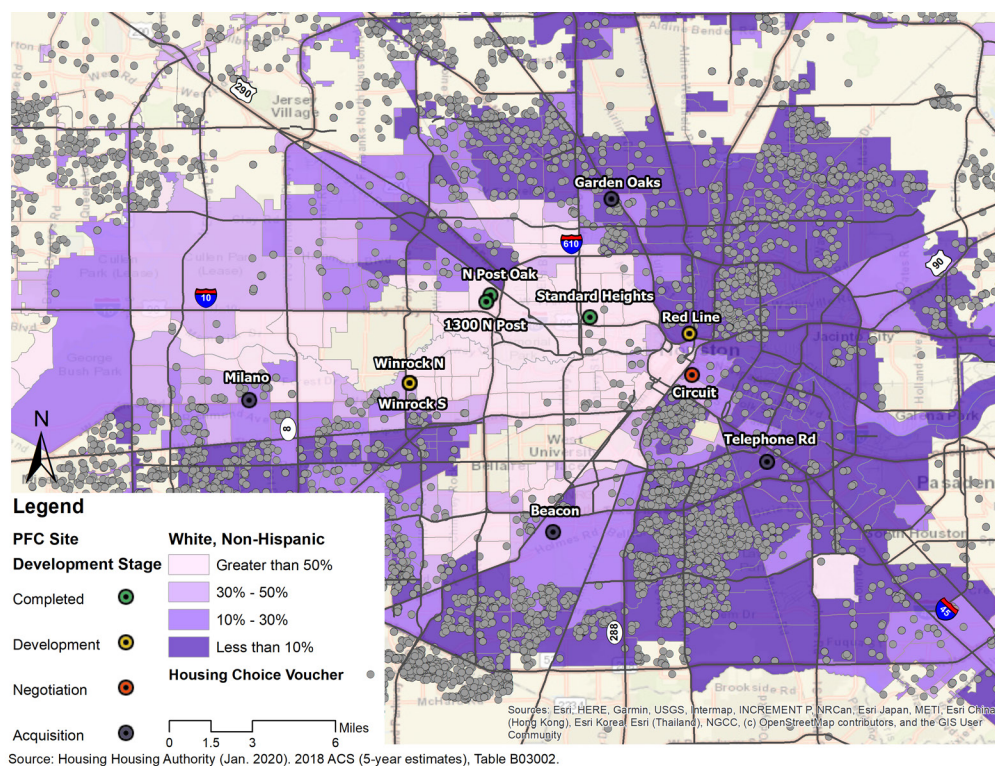
Issue #4: Discrimination against voucher holders.

Another issue we identified is that most PFC-sponsored apartment complexes with an exemption under Section 303.042(f) are allowed to discriminate against tenants with Housing Choice vouchers from their local housing authority or other form of rental housing assistance. The Housing Choice voucher program is the largest subsidized-housing program in the United States for renters in poverty. Through the program, the housing authority (via funding from HUD) pays a monthly subsidy to participating landlords and the tenant covers the remainder of the rent.

For example, none of the PFC-sponsored properties in San Antonio with a Section 303.042(f) exemption accept tenants with vouchers. Our PFC inventory in Appendix 2 includes information on whether a property accepts voucher holders based on our review of the property's legal documents as well as calls to leasing agents. In several instances where local housing officials reported that their PFC-sponsored projects are required to accept Housing Choice vouchers, the leasing agents at the properties reported to us that the property does not accept any renters with housing vouchers.

The failure of most apartments with an exemption under Section 303.042(f) to accept voucher holders is troubling, especially given that housing authorities are sponsoring most of these projects. Housing authorities' largest group of clients are voucher holders, who are predominantly African-American and Hispanic. Many of these renters face enormous challenges securing a unit with their vouchers, especially in high opportunity neighborhoods with access to strong schools, transit, and jobs. As a result, many voucher holders end up in high poverty, highly-segregated neighborhoods with low performing schools and other challenging neighborhood conditions. For example, see the map for the City of Houston below, which shows how voucher holders are concentrated in neighborhoods with high percentages of African-American and Hispanic residents, while several PFC-sponsored projects are located in more integrated neighborhoods. Opening up opportunities in PFC-sponsored projects for voucher holders will promote fair housing by increasing voucher holders' ability to access less segregated neighborhoods.

The Location of Housing Choice Vouchers, PFC Properties, and Percent of White, Non-Hispanic Residents by Census Tract in Houston, TX



A related issue we identified is the lack of marketing of the PFC-sponsored affordable units to voucher holders and other tenants looking for affordable housing, especially given that these properties typically market themselves as “luxury apartments.” From the way these properties are marketed, there is no way for a low-income tenant looking for an affordable unit to know that these properties offer income- or rent-restricted units.

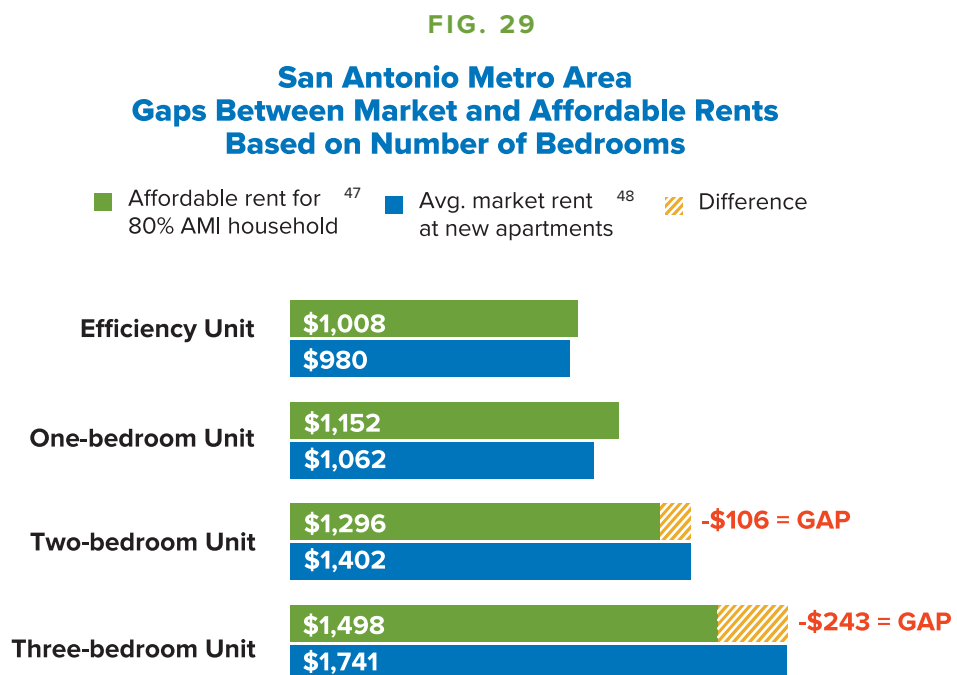
Issue #5: Lack of compliance monitoring.

Some of the PFC-sponsored projects require compliance monitoring to help ensure the property complies with any relevant income and rent restrictions, while others do not. The lack of monitoring at some properties was borne out in calls we made to four PFC properties where the leasing agents told us the property did not include any type of income restrictions or special income screening on any of the units, which was in violation of the property developer’s legal commitments to PFC. See the inventory in Appendix 2 for a list of these properties. Compliance monitoring mechanisms appear to be more common in the newer PFC deals, many of which require a recorded regulatory agreement that requires the developer submit an annual compliance certificate with the PFC, obtain income certifications from the tenants, and allow the PFC to inspect the books and records of the property. It doesn’t appear that any PFCs have actually started conducting compliance reviews of these properties.

A standard best practice in affordable housing programs is to provide some form of monitoring of the project to ensure that a developer receiving government subsidies is complying with the relevant affordable housing restrictions in the program. Compliance is typically monitored through some type of annual reporting requirement where the property has to provide income certifications, rent rolls, and other information about the project to confirm compliance with any applicable rent and income restrictions. Some programs require independent audits of the property. For example, the other major property tax exemption for affordable housing, in Section 11.1825 of the Texas Tax Code, requires nonprofits receiving the 50% property tax exemption available under that statute to submit an annual independent audit confirming compliance with the programmatic requirements, with a copy of the audit submitted to the Texas Department of Housing and Community Affairs and the chief tax appraiser. Properties with federal Low Income Housing Tax Credits must submit an annual compliance report to the Texas Department of Housing and Community Affairs.

Issue #6: Not serving families with children.

A final issue we identified with PFC deals related to their affordable housing terms is their failure, by and large, to serve low-income families with children. In most of the PFCs properties leasing today, the income-restricted units are limited to the efficiency and one-bedroom units. Only a few properties require the affordable housing units to be included in the 2- and 3-bedroom units. That’s likely because market rents on efficiencies and



one-bedroom units in Texas metro areas are usually very close to, and often below, 80% AMI adjusted for family size. As a result, a developer restricting a one-bedroom unit for a household at 80% AMI can charge the same rent on that unit that the developer could charge for a one-bedroom unit that is not restricted. In other words, the market rent on a new one-bedroom unit is the same or lower than the rent that can be charged on a unit restricted at 80% AMI adjusted for family size.

In contrast, market rents on new two-bedroom and three-bedroom units are usually above 80% AMI adjusted for family size, so imposing an affordability restriction on those units results in rents dropping below what could be charged without a restriction. As a result, unless a developer is required to include income and rent restrictions in some of the two- and three-bedroom units, the income-restricted units will end up in the efficiency and one-bedroom units.

TABLE 1

Comparison of Property Tax Exemptions Available for Apartment Development in Texas

	Qualified Nonprofit Organizations: Section 11.1825 of the Texas Tax Code	Publicly Owned Properties: TX Tax Code, § 11.11(a); Local Govt Code Chapter 392 (housing finance corps), Sec. 392.005 (public housing authorities)	Public facility corporations and privately controlled leasehold interests: Section 303.042(f)
Summary of nonprofit or public entity role	Qualified nonprofit organization is general partner; must have 501c3 exemption; majority of board must reside in Texas + other board restrictions	Public entity either owns or maintains control over land and improvements; can be through a general partner interest	Public entity leases the land and improvements to a general partnership entity controlled by private developer
Amount of property tax exemption	50%	100%	100%
Income targeting	At least 50% of units rented to households at or below 60% AMI or state AMI, adjusted for family size.	For public housing authorities: At least 50% of units at 80% AMI. For housing finance corporations: At least 90% of the units must be occupied by persons of low and moderate income (including all occupants of unit) (as defined by the HFC)	For public housing authorities: At least 50% of units at 80% AMI. No restrictions on other PFCs except must meet TX Constitution’s public purpose requirement
Rent restrictions	Rent cannot exceed 30% of the area median family income adjusted for family size and as established by HUD	None	None
Other requirements	Restrictions on rehab property eligibility; annual audit submitted to TDHCA and chief appraiser; annual application required; for 3 largest counties—must apply to each taxing entity	None	None

- **Public Benefit: Funding Stream for Affordable Housing**

A second public benefit that is touted as a public policy justification for the 100% property tax exemption on the PFC-sponsored apartment complexes is that these public-private partnerships generate revenue for local governmental entities that can be used to fund more deeply affordable housing projects. As discussed in Part Three, each of these deals generates some form of revenue for the sponsoring entity. However, in the projects we reviewed and could obtain cash flow information on, the amount of revenue flowing to PFCs from these deals is just a fraction of the property taxes being exempted from the property. In particular, public housing authorities—which are struggling financially to maintain their properties but not impacted by the loss of property tax revenue from these deals—have a perverse incentive to approve these PFC deals for the sake of the revenue being generated to the PHA rather than ensuring that the overall level of public benefits provided by each project is justified by the loss in tax revenue.

The typical sources of revenue are as follows:

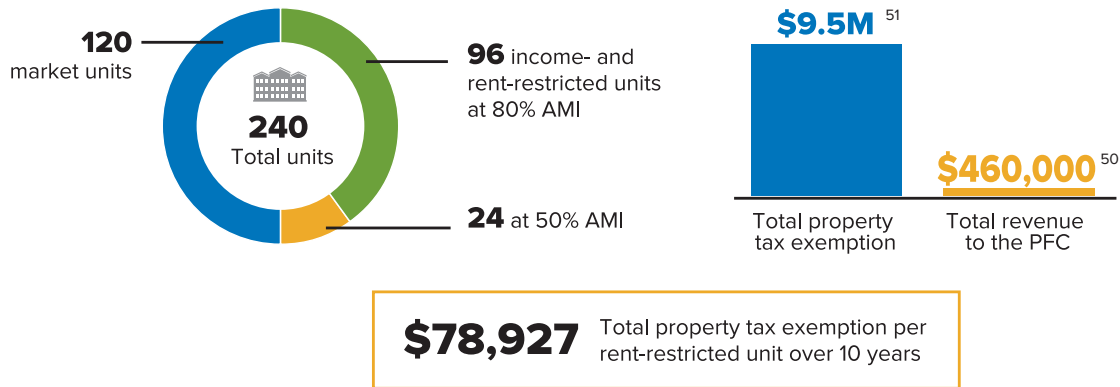
1. **Application fee.** Also called a due diligence fee. This fee must be paid by the developer in order for the PFC to vet the apartment deal proposed by the developer. This fee typically ranges from \$3,000 to \$15,000 per project.
2. **Origination fee.** Also called a developer fee or acquisition fee. This fee typically varies from 0.5 to 1% of the development costs, or \$200,000 to \$600,000 per property. The San Antonio Housing Trust (SAHT) has received \$250,000 as an up-front fee for each of its first eight conventionally-financed PFC deals. The Housing Houston Authority's up-front fees on its first eight conventionally-financed projects varied from \$150,000 to \$611,000. For some PFCs, a portion of the fee is not paid out until the property is refinanced.
3. **Net cash flow.** This revenue source consists typically of a 10-25% cut of the net cash flow from the property after the property expenses are covered and equity investors receive their preferred return on investment. This annual revenue source usually does not kick in until after the leasehold interest has been sold several years into the project given that the cash flow is first used to cover debt and the investors' preferred returns. Even then, the actual payment to the PFC from the cash flow will typically end up being very minimal. For example, the net cash flow on one project was projected to average \$30,000 a year. Out of SAHT's six new construction apartment projects that originated prior to 2019, only two have generated any rental cash flow to the PFC to date, which was after the leasehold interests were sold to new investors. These two properties, which went online in 2017-2018, have paid out total rental fees of \$32,927 as of June 2020—\$21,271 for the Upton at Longhorn Quarry Apartments and \$11,656 for the Baldwin at St. Paul Square Apartments. Looking ahead, as examples, SAHT expects to receive around \$102,000 a year on average over the next ten years for sponsoring the South Flores Lofts project, and \$145,000 a year on average over the next ten years for sponsoring the Baldwin project.
4. **Asset management fee.** This fee is also called administrative rent or a compliance fee. Some properties also include an annual fee that is paid after the project is leased up (usually after two to three years), but whether this is ever paid out depends on whether the legal documents require the fee to be paid before the investors receive their return. The annual fees we identified range from \$12,000 to \$25,000 a year per property. For SAHT's PFC deals, this fee of \$25,000 a year fee is not paid until the latter of rent stabilization or 36 months after the ground lease date.
5. **Net sales revenue.** When the leasehold interest is sold to a third party, a PFC may be eligible to receive 10-25% of the net sales revenue, depending on the structure of the deal. In its first three PFC deals, SAHT was eligible for 10% of the net sales proceeds when the leasehold interest was sold, but the SAHT PFC board voted to remain in the partnership and was thus ineligible to collect this revenue (e.g., for the Baldwin, the net sales revenue would have been \$949,000 and for the Veridian \$1.3 million). One attorney working with PFCs reports they are working hard to obtain a strong return to the PFC when the

leasehold interest is sold and that some deals could eventually produce millions in returns to a PFC upon sale.

As an example of fairly typical PFC deal terms, the Houston Housing Authority’s partnership with Ojala for the acquisition of the Smart Living at Telephone Road Apartments removed a \$32 million property from the property tax roll, providing an exemption worth \$768,000 a year.⁴⁹ In exchange, the Housing Authority received a one-time \$160,000 origination fee when the property was acquired. While the HHA is also eligible to receive 15% of the property’s net cash flow after the investors receive a preferred return, this revenue is projected to be around \$30,000 a year. If the property remains in the leasehold interest structure for the entire 75-year lease term, the total property exemption will total at least \$147 million. See Figure 30.

FIG. 30

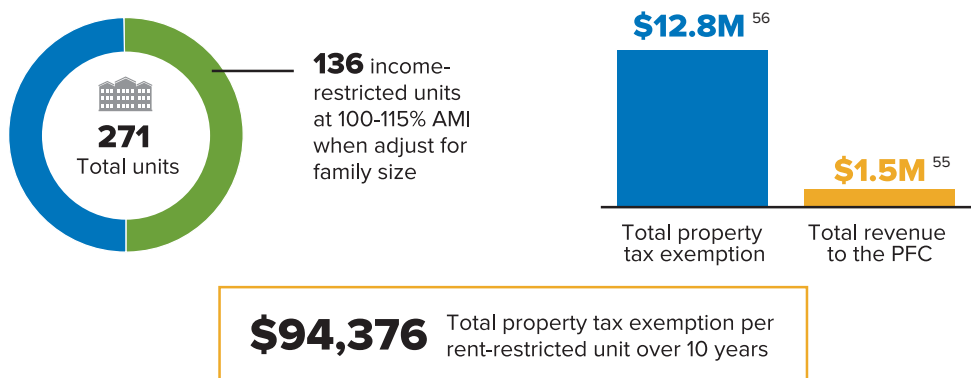
**Smart Living at Telephone Road:
Revenue to the Houston Housing Authority vs
Property Tax Exemptions
2019-2029**



As an example from San Antonio, the Baldwin at St. Paul Square Apartments—the San Antonio Housing Trust’s second conventionally-financed PFC project, which was sold to a new partnership in 2019—the PFC estimated it will receive \$89,080 in year one from the new partnership, growing to \$205,865 by year 10, a total of \$1.5 million (\$1.1 million NPV) compared to \$12.8 million in property taxes abated on the property over the same period.⁵² Over the remainder of the 75-year lease, the PFC estimates it will receive revenue of \$37 million, or \$6.3 million net present value.⁵³ The property’s 100% ad valorem exemption (estimated at \$1.1 million for 2020) will result in over \$179 million in lost property taxes over the same period.⁵⁴ See Figure 31.

FIG. 31

**The Baldwin: Revenue to the City of San Antonio vs
Property Tax Exemptions
2019-2029**



Below are more detailed examples of the financial benefits that have flowed to the San Antonio Housing Trust so far from its first two conventionally-financed PFC projects, including the Baldwin.

TABLE 2
The Upton at Longhorn Quarry (opened for leasing in 2017)

Revenue		Tax Savings	
Application fee (one-time, up-front fee)	None	Property tax exemption	Total: \$2.6 million 2020: \$445,942 (pro rata as of July 2020) 2019: \$891,884 2018: \$892,804 2017: \$373,112
Origination fee (one-time, up-front fee)	\$250,000	Estimated sales tax exemption (one-time)	\$1.3 million
Cumulative asset management fees (\$25,000 annual fee once project is leased)	\$47,916	Total tax savings, as of June 2020	\$3.9 million
Cumulative share of rental revenue (annual fee)	\$21,271		
Total revenue to the PFC, as of June 2020	\$319,188		

TABLE 3
The Baldwin at St. Paul Square (opened for leasing in May 2018)

Revenue		Tax Savings	
Application fee (one-time, up-front fee)	\$3,000	Property tax exemption	Total: \$2.1 million 2020 (pro rata): \$532,128 2019: \$1,042,726 2018: \$371,624 2017: \$133,165
Origination fee (one-time, up-front fee)	\$250,000	Estimated sales tax exemption (one-time)	\$1.1 million
Cumulative asset management fees (\$25,000 annual fee once project is leased)	\$16,666	Total tax savings, as of June 2020	\$3.8 million
Cumulative share of rental revenue (annual fee)	\$11,656		
Total revenue to the PFC, as of June 2020	\$281,322		

- **Public Benefit: Economic Development**

A third policy goal put forward for providing tax breaks to conventionally-financed apartments under Section 303.042(f) is that the tax break is a tool to incentivize the development of higher-end apartment development and kickstart market-rate development in disinvested low-income neighborhoods and other hard-to-develop areas, such as vacant infill properties. For example, in Cibolo, the city is using the property tax break tool in Section 303.042(f) to attract a new high-end apartment development in an area that is expected to fuel other higher-end projects in the area. The City of Boerne is working on a potential PFC-sponsored project for the same reason—to incentivize developers, via the lucrative 100% property tax exemption, to build a high-end apartment complex in the city. The focus of these deals is not on generating rental housing with below-market rents.

Spurring market-rate apartment development in areas that would otherwise not attract private capital to invest in market-rate projects has also been a primary rationale underlying many of the conventionally-financed projects sponsored by the San Antonio Housing Trust’s PFCs. For example, the property tax tool in Section 303.042(f) is being utilized to help incentivize the development of an apartment complex—the Friedrich Lofts—on a longtime vacant property in San Antonio’s near Eastside that was previously occupied

by an air conditioner company, with several unsuccessful prior attempts to redevelop the property. The City Council approved \$2.3 million in additional subsidies for the development, including funds from the local tax increment reinvestment zone fund and fee waivers.

The public subsidies for both the Friedrich Lofts and a second nearby PFC-sponsored development, Redberry Estates, have been criticized by opponents for fueling inequities through the gentrification of the City's Eastside. The Friedrich Lofts, for example, is anchored in between two of the city's fastest gentrifying neighborhoods with rents priced at levels out of reach to many long-time residents in the area.

In other areas of San Antonio, the tool has also been justified as a needed subsidy to attract private capital to invest in the development of market-rate apartments. See Appendices 4 and 5 for maps with the locations of Section 303.042(f) exempt properties in San Antonio and information on census tracts with high concentrations of poverty and percentages of White, non-Hispanic residents. Because household incomes and market rents are lower in San Antonio than they are in the state's other major metro areas, proponents of the PFC structure argue that a property tax break is needed there to generate cash flow at a high enough level of return on investment (20%) to attract private equity investors for market-rate projects. Otherwise, proponents of Section 303.042(f) argue, these projects would not be built and middle-income renters seeking market-rate units would put greater pressure on the city's limited "naturally occurring" affordable housing supply, exacerbating housing challenges for the city's lower-income renters. Although, as a counterpoint, it's worth exploring whether a better use of a subsidy for middle-income rental housing worth \$158,000 per unit over a 20-year term could be applied through a property tax exemption to help the renters buy their first home.

Conducting an in-depth evaluation of this particular policy rationale was outside the scope of our research on PFCs but merits further investigation. But outside of difficult-to-develop tracts, this economic development rationale for subsidizing market-rate development carries much less weight—as it does in PFC deals involving the acquisition of existing apartments. And even in difficult-to-develop tracts, as a matter of equity, any property receiving such a large level of public subsidy should include some units serving renters most in need of subsidized housing. Moreover, if a primary concern driving these public partnerships is market-rate renters placing pressure on the city's naturally occurring affordable housing supply for lower-income renters, it seems like a more direct and effective approach is to invest the city's precious tax dollars in the acquisition and preservation of these "market-affordable" units.

Plenty of market-rate apartment development has been happening recently in San Antonio for projects not receiving a property tax exemption. Earlier this year 2020, the city was described to be undergoing an apartment boom—with 22 apartment complexes and 5,945 total units opening in the region in the prior year, with an additional 16 communities under construction and 55 complexes under consideration.⁵⁷ As of the first quarter of 2020, the city had a healthy Class A apartment occupancy rate of 89.8%.⁵⁸



According to data compiled by the National Low Income Housing Coalition, Bexar County actually has a large surplus of 12,648 rental units that are affordable and available for renter households making up to 100% AMI—which is the income restriction actually being used in most PFC properties when the AMI is not adjusted for family size (see the discussion above under "affordable housing, issue #2"). In contrast, Bexar County has a deficit of 46,238 rental units for renter households making up to 30% AMI and a 39,560-unit deficit for households making up to 60% AMI. The county has a small deficit (3,344 units) for households making up to 80% AMI, which could serve as a justification for subsidizing some rental units at this price point, as long as they were truly income- and rent-restricted for households making less than 80% of the AMI (i.e., adjusted for family size) and targeting 2- and 3-bedroom units, which is where there is a consistent gap between market rates and what a household making 80% AMI can afford. See Figures 25 and 29.

As shown in Figure 25, and as discussed further above, Texas' other four most-populated counties also have a surplus of rental housing for renter households making up to 100% AMI as well.

Part Six. Recommendations

The findings above raise important questions about the 100% property tax exemption under Section 303.042(f) and whether it should continue. And even if local governmental entities should have the authority to exempt their own tax base, should they have the authority to exempt the tax base of other taxing authorities? These are important questions that deserve further public discussion. Discussion is especially due given the way in which this exemption was created, via an 11th hour amendment on the floor of the Texas Senate without any public hearing and with a misrepresentation about who would benefit from the exemption. Further investigation is also warranted concerning the state constitutionality of the property tax break on the leasehold interests issued by PFCs for apartment complexes, including (1) whether the properties are adequately used for public purposes; (2) whether there are issues with a private entity controlling the leasehold interest—one of the “bundle of sticks” of real property ownership—and (3) whether there are issues with the PFC ground leases essentially gifting the property back to the private developer if and when the property tax exemption is ever revoked. See Tex. Const. Art. VIII, § 2(a); Art. XI, § 9.

Assuming that the property exemption does continue for privately-controlled apartment complexes utilizing a PFC leasehold interest structure, we make the following recommendations on ways to strengthen the exemption.

TRANSPARENCY AND ACCOUNTABILITY

1. **Require annual reports.** At a minimum, Section 303.042 should require local governments to submit annual reports to the Texas Comptroller and local taxing entities regarding all apartment complexes receiving an exemption under Section 303.042(f) of the Local Government Code through a partnership with the local government. The report should include a copy of all legal agreements between the local government and private developers for each complex exempted under Section 303.042(f) as well as reporting on renter incomes and demographics. Chapter 312 of the Tax Code requires similar reports for local governments entering into tax abatement agreements with private developers. Reports should also be made available on the Comptroller’s website for public access.
2. **Require compliance reviews including an annual audit.** PFCs should engage in regular compliance monitoring of the conventionally-financed properties they are sponsoring under Section 303.042(f). And private developers receiving a property tax exemption under Section 303.042(f) should be required to obtain an annual audit regarding the property’s compliance with all the affordability restrictions imposed on the property. Section 11.1825 of the Tax Code requires nonprofit entities to submit such an audit to the Texas Comptroller for all properties owned by the nonprofit receiving a 50% property tax exemption under that section. As part of meeting the audit requirements, developments with a Section 303.042(f) exemption should be required to utilize income certifications at their properties, to verify household income for the income-restricted units, and confirm that the households’ comply with the property’s income restrictions, as many PFC-supported properties have already begun requiring. Finally, property owners should be subject to stiff penalties if they fail to comply with the affordable housing restrictions on the property.
3. **Require an RFP process.** Developers partnering with local governments on PFC projects under Section 303.042 should have to go through a competitive request for proposal process. Proposals should be submitted via an application process and scored according to specific criteria based on goals adopted by the local government’s governing body, to ensure that partnerships via Section 303.042 are awarded to projects best qualified to meet the community’s needs. The application should be reviewed by an independent real estate finance expert to evaluate the project’s finances and weigh the cost-benefits of awarding a 100% exemption on the property. The scoring should then be reviewed by a housing investment committee composed of community representatives with expertise in planning and housing development. The committee would not make any final binding recommendations concerning applications but instead forward their input to the local government staff for review. The committee’s input would then be included with any staff recommendations about the project when they are forwarded

to the local government's governing body for a final vote regarding whether to approve the partnership. This is similar to the review process that the City of Austin follows for all housing development projects seeking city or federal funding. The Houston Housing Authority has started to use an RFP process for all of its Section 303.042(f) partnership projects, and the National Association of Latino Asset Builders recommended that the San Antonio Housing Trust follow a RFP or other public process for vetting its public-partnership projects. The City of Dallas also recently adopted criteria that PFC-sponsored projects will have to meet.

AFFORDABILITY MEASURES

4. **Require alignment of rent and income restriction policies with affordable housing industry standards.** All properties receiving an exemption under Section 303.042(f) should be required to follow affordable housing industry standards by adjusting their AMI targeting levels for family size and adopting rent restrictions based on 30% of the applicable AMI restricted levels as established by HUD. The rent restrictions should also incorporate a utility allowance. Finally, the income screening should consider the income of everyone living in the unit and not just the person listed on the lease.
5. **Require deeper income targeting.** In order for a property to qualify for the 100% property tax exemption under Section 303.042(f), a good portion of the property's rents must be restricted at significantly lower rates than market rents for the area. Ideally at least 25-50% of the units at the property would be restricted at affordable rates for households making less than 60% of the Area Median Income with the affordable units spread across the bedroom sizes and a small percentage of the units restricted to renters with vouchers from the local housing authority to result in truly mixed-income housing. For nonprofit housing providers receiving a 50% exemption under Section 11.1825 of the Texas Tax Code, at least half of the total square footage of the property's dwelling units must be affordable to households making up to 60% AMI as established by HUD.
6. **Ban source of income discrimination.** Property developers receiving any type of property exemption or other public benefit on their development should be barred from discriminating against tenants based on their source of income, such as tenants who need to use a voucher from a housing authority to pay for part of their rent. This means that properties also need to be barred from applying minimum income policies to exclude voucher holders—the minimum income policy should only be applied to the tenant's portion of the rent. The Low Income Housing Tax Credit program includes a similar ban on source of income discrimination. Even better than banning source of income discrimination, in order to ensure that a property ends up accepting voucher holders, public entities should consider requiring the developers it partners with to dedicate up to ten percent of the units at the complex for tenants with vouchers for all properties in high opportunity neighborhoods.
7. **Engage in affirmative marketing.** Housing authorities should actively market the PFC-sponsored properties to their voucher clients, including listing these properties on their websites. Cities and counties should also actively market all of their PFC-sponsored properties. Property managers of PFC-sponsored properties should be required to market the affordable units on the property's website and include references about the availability of affordable units at the property in all public marketing materials. The property managers should also be required to notify the Housing Authority's Housing Choice Voucher program when vacancies arise in the income-restricted units.
8. **Adopt enhanced protections for renters.** In order for a property to qualify for the 100% property tax exemption under Section 303.042(f), the property should be required to include enhanced protections for tenants for the life of the property. These protections should include a right to cure any lease deficiencies, a right to organize, and a ban on lease non-renewals without cause. The City of Austin requires similar protections in all apartment developments it funds as well as private activity bond projects it approves.

9. **Serve families with children.** The affordable units in a property receiving an exemption under Section 303.042(f) should be distributed proportionately across bedroom/bathroom categories and not concentrated in the smaller units. For example, if half the units at a property are income restricted, then half of the 1 bedroom/1 bath units should be income restricted, half of the 2 bedroom/2 bath units should be income restricted, and half the 3 bedroom/3 bath units should be income restricted. Another way to incentivize family-friendly units is to require the affordability to be applied to the leasable square footage rather than the unit count. PFCs should also require that the affordable units in the larger bedroom sizes be marketed to families with children.

10. **Impose limits on acquisition projects.** If a PFC is taking an existing apartment complex off the tax rolls, the property should have to meet criteria similar to the requirements in Section 11.825 of the Tax Code for nonprofit acquisition projects receiving an exemption under that section. Under Section 11.825, rehabilitation projects are eligible for the exemption only if (1) the original construction was completed at least 10 years prior to rehabilitation, (2) the prior owner owned the property for at least five years, and (3) the organization spent at least \$5,000 per unit on rehabilitation costs, or an amount required by the lender, if greater. If a PFC partners on an acquisition project it should be required to pay for tenant relocation costs at a standard equivalent to the federal Uniform Relocation Act, for any tenants displaced as a result of the acquisition.

Appendix 1: Other Statutory Property Tax Breaks for Affordable Rental Housing Developments in Texas

In addition to the 100% property tax exemption for apartment complexes on leasehold interests granted by public facility corporations, Texas provides two additional primary statutory mechanisms by which an affordable rental housing development can receive an exemption from ad valorem taxes, along with a third mechanism for certain pre-2003 properties. This section provides an overview of these statutes.

(1) 50% Exemption for Rental Housing Owned by Qualified Nonprofit Organizations: Section 11.1825 of the Texas Tax Code

Rental housing owned by a qualified nonprofit organization is eligible for a 50% exemption from ad valorem taxes if at least half of the total square footage of the property's dwelling units are rented to households whose incomes do not exceed the greater of 60% of the property location's area median income (adjusted for family size) or the state area median income (adjusted for family size), as established by the United States Department of Housing and Community Development (HUD). The annual rent for the affordable units cannot exceed 30% of the area median family income as adjusted for family size and established by HUD. Texas Tax Code §§ 11.1825(f)-(h).

The exemption is available to new construction projects built after January 1, 2004. Rehabilitation projects are eligible for the exemption only if they meet the criteria in Section 11.825(l)-(p), including requirements that (1) the original construction was completed at least 10 years prior to rehabilitation; (2) if the property was acquired, the prior owner owned the property for at least five years; and (3) the organization spent at least \$5,000 per unit on rehabilitation costs, or an amount required by the lender, if greater. The owner must also maintain a replacement reserve totaling at least \$300 per unit per year or another amount if required by the lender. §§ 11.1825(k)-(n).

A qualified nonprofit organization must have a federal 501(c)(3) exemption, be qualified as "charitable" under the Texas Tax Code, and have a purpose of providing low-income housing. A majority of the organization's board members must have their principal residence in Texas—and at least two board members must be low-income Texans, reside in an economically disadvantaged census tract in Texas, or be appointed as the representative of a low-income neighborhood association in the state. Texas Tax Code § 11.1825(b). For-profit entities can partner in a development via a limited partnership structure without jeopardizing the exemption as long as the qualified nonprofit organization owns 100% of the general partner. Texas Tax Code § 11.1825(c). This structure facilitates financing from the federal Low Income Housing Tax Credit program.

To receive the 50% property tax exemption, the qualified nonprofit organization must apply each year for the exemption with the appraisal district. For apartment projects in counties with a population of at least 1.8 million (i.e., Harris, Dallas, and Tarrant Counties), the nonprofit organization must instead apply and receive approval for the exemption from each taxing unit's governing body (e.g., school board, county commissioners court, city council, etc.). These taxing authorities have the discretion whether to grant or deny the exemption. Texas Tax Code §§ 11.1825(v-y). Taxing entities in other jurisdictions do not have this discretion.

As a condition of qualifying for the exemption, the qualified nonprofit organization must also obtain an annual audit prepared by an independent auditor in accordance with generally accepted accounting principles. The audit must provide an opinion on whether the organization has complied with the terms and conditions in Section 11.1825. Texas Tax Code § 11.1826(b). The audit must be delivered to the Texas Department of Housing and Community Affairs and the chief appraiser no later than 180 days after the last day of the organization's most recent fiscal year. Smaller properties, with 36 or less units, do not require a formal audit if the owner submits a detailed report and certification. Texas Tax Code § 11.1826(d).

(2) 100% CHDO exemption for pre-2004 grandfathered properties: Section 11.182

Prior to the adoption of Section 11.1825 in 2003, nonprofit housing providers designated as Community Housing Development Providers, or CHDOs, were able to obtain a 100% property tax exemption under Section 11.182 of the Tax Code. Properties that have already received the Section 11.182 exemption are able to maintain their exemption as long as the property meets the statutory requirements, including the annual audit requirement.

The 100% exemption in Section 11.182 was overhauled (via amendments to 11.182 and the adoption of 11.825, discussed above) in response to widespread concerns about the 100% exemption under 11.182 resulting in a significant loss of local tax revenue with little or no net gain in affordable housing, as well as a lack of transparency over what public benefits were provided in exchange for the exemption. Particular concerns included multifamily rehabilitation projects and removal of these projects from the tax rolls with minimal public benefit. Concerns were also raised about “fake” CHDOs being set up solely for the purpose of receiving the exemption without adequate ties to the community.

During hearings on the different attempts to overhaul 11.182, stakeholders emphasized that the CHDOs receiving the property tax exemption “should be held accountable for the revenue taken away from the taxing unit and be responsible for adding public benefit to the local community.” Multiple witnesses testified as to how the public benefits from the exemption should be easy to trace and audit, and that the exemption would be better directed to serve the housing needs of Texans making 50% or less of the area median income. Local government representatives expressed concerns with one governmental unit being able to usurp the taxing ability of another.

Among other reforms, CHDOs grandfathered under 11.182 are now required to spend at least 40 percent of the total amount of property tax savings from the exemption on social, education, or economic development services, capital improvement projects, or rent reduction, unless the property received tax-exempt bond financing between 1997 and 2001. Texas Tax Code § 11.182(d).

(3) 100% Exemption for Apartment Developments Owned by Political Subdivisions and Their Instrumentalities

Under Section 11.11(a) of the Tax Code, property owned by the state or a political subdivision of the state is 100% exempt from property taxes if the property is used for a public purpose. This exemption is authorized under the Texas Constitution, which authorizes the Legislature to “exempt from taxation public property used for public purposes.” Article VIII, Section 2(a). See also Article XI, Section 9, which exempts from taxation “property of counties, cities and towns, owned and held only for public purposes.” **To qualify for this 100% exemption, a property must be both publicly owned and used for public purposes.**

In addition to Section 11.11(a), Section 392.005 of the Local Government Code provides a 100% property tax exemption for property owned by public housing authorities or nonprofit corporation created and controlled by the PHA, including public facility corporations, subject to the requirements discussed below. Section 394.905 of the Local Government Code exempts property owned by housing finance corporations (HFCs) created by counties and cities. Counties and cities typically utilize a housing finance corporation to participate in housing development projects, but a growing number of counties and cities are utilizing public facility corporations.

Publicly owned: As for meeting the Texas Constitution’s and state statutes’ public ownership requirement, the exemption provisions in Chapters 392 and 394 do not provide guidance on what role a for-profit entity can play as an owner of a housing development in order for the property to still qualify for the 100% exemption. In instances where a public entity is not the sole owner of property, Texas court rulings and an opinion from the

Texas Attorney General provide that property used for public purposes qualifies for an exemption as long as it is “equitably owned” by a public entity. Equitable ownership means that the local governmental entity has the “present right to compel legal title.”

Whether property is equitably owned by a public housing authority or city or county housing finance corporation is a fact-specific determination. The case law and AG guidance have been interpreted by apartment industry attorneys, appraisal districts, lenders, and investors to support a 100% tax exemption on apartments developed and owned through a public-private partnership when the following conditions exist:

- (1) The land is owned in fee simple by the housing authority or housing finance corporation (or their instrumentalities) and leased for at least 50 years to a limited partnership;
- (2) The improvements are owned by the limited partnership, but the public entity has control over the conditions it can fulfill to compel transfer of legal title to the property to the public entity, such as an option to acquire the property;
- (3) The public entity (or its instrumentalities) is the general partner of the limited partnership (or owns at least a 51% interest in the general partnership), while the investors and other for-profit partners are limited partners;
- (4) The public entity has a right of first refusal to acquire the property if a purchase offer is received by a third party; and
- (5) The public entity has the right to cure financing defaults by the partnership.

Public purpose: Texas statutes do not provide much in the way of restrictions when it comes to limiting the incomes or rents that must be imposed on a publicly-owned rental property to further a public purpose under the Texas Constitution and thus qualify for the 100% property and sales tax exemption. Public housing authorities and their instrumentalities (such as a public facility corporation) are eligible for the 100% exemption as long as (1) the development includes at least 20% of its units as public housing units, or (2) the authority holds a public hearing at a regular meeting of the PHA and at least 50% of the units are reserved for households earning less than 80% of the area median family income. Texas Local Government Code § 392.005(c). For city and county housing finance corporations to qualify for the 100% exemption, at least 90% of a residential development must be used or “intended to be occupied by persons of low or moderate income,” as those terms are defined by the housing finance corporation. Texas Local Government Code § 394.004.

Most apartment complexes with a 100% tax exemption that are owned through partnerships with a city or county public housing finance corporation are receiving some sort of public financing, such as tax-exempt bonds or federal Low Income Housing Tax Credits—and, in the case of tax credits, come with deeper income targeting, rent restrictions, compliance requirements, and other restrictions. While tax-exempt apartment projects sponsored by a housing finance corporation were not the focus of our research unless the exemption arises out of the 2015 amendments to the Local Government Code—that is, the project has a long-term leasehold interest controlled by a private entity—we came across several exempt projects where the HFC is serving as the general partner of the entity controlling the leasehold interest and included these properties in our inventory in Appendix 2.

Appendix 2: Inventory of Tax-Exempt, Conventionally-Financed Apartment Projects Sponsored by Public Facility Corporations in Texas Since 2015

City of San Antonio Housing Trust

Name of apartment complex	Address	Year PFC partnership approved, type of project, # of units, developer	Income targeting; housing vouchers	Tax Exemptions	Notes
Upton at Longhorn Quarry Apartments	4906 Wurzbach Parkway, 78233	2016, new construction, 305 units NRP Group (leasehold interest sold in 2019)	50% at 80% AMI; 50% at market No vouchers accepted	Property tax exemption: \$891,884 Sales tax exemption: \$1,258,125	No rent restrictions; AMI not adjusted for family size
Baldwin @ St. Paul Square Apartments	239 Center Street, 78202	2017, new construction, 271 units NRP Group (leasehold interest sold in 2019)	50% at 80% AMI; 50% at market No vouchers accepted	Property tax exemption: \$1,064,256 Sales tax exemption: \$1,117,875	No rent restrictions; AMI not adjusted for family size
Viridian Apartments (AKA Montabella Point II)	5415 North Foster Road, 78244	2017, new construction, 321 units NRP Group (leasehold interest sold in 2020)	50% at 80% AMI; 50% at market No vouchers accepted	Property tax exemption: \$873,94 Sales tax exemption: \$1,324,125	No rent restrictions; AMI not adjusted for family size
Copper Pointe Apartments	6410 S New Braunfels Ave, 78223	2017, new construction, 252 units LDG Development	50% at 80% AMI; 50% at market Not required to accept vouchers	Property tax exemption: \$741,888 (110 units completed) Sales tax exemption: \$1,039,500	No rent restrictions; AMI not adjusted for family size
Salado at Red Berry Apartments	902 Gembler Rd, 78219	2018, new construction, 330 units NRP Group	50% at 80% AMI; 50% at market No vouchers accepted	Property tax exemption: \$1,115,853 Sales tax exemption: \$1,361,250	No rent restrictions; AMI not adjusted for family size
Flats at River North (Broadway Jones) Apartments	1011 Broadway Avenue	2018, new construction, 282 units (under development) NRP Group	50% at 80% AMI; 50% at market Not required to accept vouchers	Property tax exemption: \$1,312,369 Sales tax exemption: \$1,167,375	

San Pedro Creek Apartments (aka West Cevallos Apartments)	418 West Cevallos Street, San Antonio	2019, new construction, 325 units (under development) NRP Group	40% at 80%AMI; 50% at market; 10% at 60% AMI (if cash flow available) Not required to accept vouchers	Property tax exemption: \$1,151,142 Sales tax exemption: \$1,340,625	Regulatory agreement in place: rent restricted at 35% of 80% and 60% AMI; AMI not adjusted for family size and no utility allowance; 60% AMI rents paid for via PFC share of cash flow
Lookout Apartments	1604 & Lookout Road	2019, new construction, 293 units (under development) Versa Development	40% at 80% AMI; 10% at 60% AMI for 15 years; 50% at market; Not required to accept vouchers	Property tax exemption: \$1,145,920 Sales tax exemption: \$1,208,625	Regulatory agreement in place: rent restricted at 35% of 80% and 60% AMI spread across different unit types; AMI not adjusted for family size and no utility allowance
Friedrich Lofts	1617 E. Commerce St.	2020, new construction, 350 units (approved; under re-negotiation) Provident Realty Advisors	50% at 80% AMI (14 units at 60% AMI); 50% at market Not required to accept vouchers	Property tax exemption: \$1,631,692 Sales tax exemption: \$1,443,750	
Beitel Creek Flats Apartments	East Corner of Thousand Oaks & Wurzbach Parkway	2019, new construction, 348 units (preliminary approval) NRP Group	40% at 80% AMI; 10% at 60% AMI for 15 years; 50% at market	Property tax exemption: \$857,537 Sales tax exemption: \$1,394,250	
South Flores Lofts (Soflo)	1334 Flores St.	2020, new construction, 292 units (preliminary approval) Athena Domain	40% at 80% AMI; 10% at 60% AMI for 15 years; 50% at market	Property tax exemption: \$1,361,297 Sales tax exemption: \$1,204,500	
Ridgeline Flats Apartments	26 acres on N side of 1604 between IH-10/Bitters	2020, new construction, 349 units (preliminary approval) NRP Group	40% at 80% AMI; 10% at 60% AMI for 15 years; 50% at market	Property tax exemption: \$1,461,483 Sales tax exemption: \$1,439,625	

San Antonio Housing Authority

Name of apartment complex	Address	Year PFC partnership approved, type of project, # of units, developer	Income targeting; housing vouchers	Tax Exemptions	Notes
Culebra Crossing	Culebra Road and Loop 1604	2019, new construction, 326 units (under construction) Lynd Company	50% at 80% AMI; 50% at market Not required to accept vouchers	Property tax exemption: \$1,083,508 Sales tax exemption: \$1,344,750	Income not adjusted for family size; no rent restrictions
Arroyo Seco	12311 Culebra Rd. 78253	2019, acquisition, 200 units Post Investment Group	40% at 80% AMI; 20% at 60% AMI; 40% at market No vouchers accepted	Property tax exemption: \$568,729	Leasing agent: no income restrictions; rents are all market rents and the same across all 1-bedrooms (\$899) and 2-bedrooms (\$1225) In legal docs: AMI is adjusted for family size; rent restrictions of 30% applicable AMI; no utility allowance Includes right of first refusal agreement

City of San Antonio Hemisfair Park Public Facilities Corporation

Name of apartment complex	Address	Year PFC partnership approved, type of project, # of units, developer	Income targeting; housing vouchers	Tax Exemptions	Notes
The '68 Apartments at Hemisfair	623 Hemisfair Boulevard, 78205	2016, new construction, 151 units David Adelman	50% market; 5% at 80-110% AMI; 45% at 80% AMI. Within 80% AMI units: 3 units at 50-60% AMI; 3 at 60-70 % AMI, 3 at 70-80% AMI (with rent restrictions) Vouchers not accepted	Property tax exemption: \$1,515,132 Sales tax exemption: \$651,750	AMI is adjusted for family size; no rent restrictions except for 16 units with restrictions of 25% of income.

Houston Housing Authority

Name of apartment complex	Address	Year PFC partnership approved, type of project, # of units, developer	Income targeting; housing vouchers	Tax Exemptions	Notes
Milano Apartments	2500 Woodland Park Drive 77077	2018, acquisition (property built in 1997), 330 units Ojala	51% at 80% AMI; 49% at market Vouchers not accepted	Property tax exemption: \$977,369	Leasing agent said they don't participate in any affordable housing programs and don't have any rent restrictions on units; AMI not adjusted for family size
Standard Heights	609 Waverly Street 77007	2018, new construction, 301 units Ojala	51% at 80% AMI; 49% at market Vouchers not accepted	Property tax exemption: \$541,321 Sales tax exemption: \$1,155,000	No rent restrictions; AMI not adjusted for family size

Smart Living at Telephone Road	3852 Telephone Road 77023	2019, acquisition (property built in 2016), 240 units Conrad	41% at 80% AMI; 10% at 50% AMI; 49% at market Vouchers not accepted	Property tax exemption: \$767,464	Leasing agent reported this property does not include any affordable units; legal docs require 50% at 80% AMI adjusted for family size; rent restrictions of 30% AMI with no utility allowance
Winrock Phase 1	1950 Winrock Blvd (aka 2030 Winrock) 77057	2019, new construction, 435 units Ojala	46% at 80% AMI; potential 21 PBVs at 110-120% FMR; 49% at market	Property tax exemption: \$833,314 Sales tax exemption:	AMI not adjusted for family size; rent restrictions at 35% of 80% AMI
Winrock phase 2	1950 Winrock Blvd 77057	2019, acquisition (property built in 1970), 227 units Ojala	40% at 65% AMI; 24% at 80% AMI; potential 23 PBVs at 110%-120% FMR; 25% at market	Property tax exemption: \$1,063,747	AMI not adjusted for family size; rent restrictions at 35% of 80% AMI
North Post Oak Lofts	1255 N. Post Oak	2019, new construction, 330 units NHP Foundation	51% at 80% AMI; 49% at market; potential 23 PBVs	Property tax exemption: \$1,619,420 Sales tax exemption: \$1,361,250	AMI adjusted for family size; rent restrictions of 30% AMI with no utility allowance
1300 North Post Oak	1300 N. Post Oak	2019, new construction, 247 units NHP Foundation	51% at 80% AMI; 49% at market; potential 17 PBVs; no other vouchers accepted	Property tax exemption: \$1,051,693 Sales tax exemption: \$1,018,875	AMI adjusted for family size; rent restrictions at 30% of 80% AMI with no utility allowance

Beacon at Buffalo Pointe	10301 Buffalo Speedway	2019, acquisition (property built in 2016), 281 units, The Morgan Group	51% at 80% AMI; 49% at market Does not accept vouchers	Property tax exemption: \$855,777	AMI is not adjusted for family size; rent restrictions: 30% of 80% AMI; no utility allowance Income limits are \$61,000/yr for 1-and 2-person household; does not include 3 bedrooms in set aside
Red Line Station	Leona Street and Fulton Street, Houston 77026	2019, new construction, 300 units (under development) NRP Group	51% at 80% AMI; 49% at market Not required to accept vouchers	Property tax exemption: \$1,408,970 Sales tax exemption: \$1,237,500	AMI not adjusted for family size; rent restrictions at 35% of AMI level
Smart Living at Garden Oaks	450 E Rogers St, Houston, TX 77022	2019, acquisition (property built in 2018), 150 units Civicap	41% at 80% AMI; 10% at 50% AMI; 49% at market (legal docs require this, but leasing agent says property only has 80% AMI restriction, not 50%AMI) Accepts vouchers but minimum income policy may exclude	Property tax exemption: \$276,334	AMI adjusted for family size; rent restrictions at 30% of AMI level with no utility allowance
Circuit Apartments	2424 Capitol Street, Houston (2414, 2417)	2020, acquisition, 311 units AMCAL	50.2% at 80% AMI; 49.8% at market Not required to accept vouchers	Property tax exemption: \$1,435,989	30% rent restriction with no utility allowance; AMI adjusted for family size; affordable units split evenly between 1- and 2-bedroom units

Fort Worth Housing Authority

Name of apartment complex	Address	Year PFC partnership approved, type of project, # of units, developer	Income targeting; housing vouchers	Tax Exemptions	Notes
The Henderson	1000 Henderson Street 76102	2020, acquisition (property built in 1998), 194 units Greystar	51% at 80% AMI; 49% at market; 19 RAD units; Not required to accept vouchers.	Property tax exemption: \$1,099,838	No rent restrictions; AMI not adjusted for family size
Highpoint Urban Living/AKA Bottle House on Main	650 South Main Street 76104	2019, acquisition (property built in 2015), 227 units Greystar	50% at 80% AMI; 50% at market Vouchers not accepted according to leasing agent.	Property tax exemption: \$1,094,396	According to leasing agent: no affordable units and no income restrictions; advertised as "luxury apartments and condos" No rent restrictions in legal docs; AMI not adjusted for family size
The Holston	3301 Westport Pkwy 76177	2019, new construction, 520 units (under development), AMCAL	50% at market; 50% at 80% AMI; Not required to accept vouchers.	Property tax exemption: \$2,081,054 Sales tax exemption: \$2,145,000	No rent restrictions; AMI adjusted for family size
Standard River District	5200 White Settlement Rd 76114	2019, new construction; 293 units (under development) Ojala	50% at 80%AMI, 50% at market; Not required to accept vouchers.	Property tax exemption: \$622,664 Sales tax exemption: \$1,208,625	No rent restrictions; AMI not adjusted for family size
Standard Homes at Harmon	South of Harmon Road along the Bailey Boswell Extension in Fort Worth	2020, new construction; 230 units (preliminary approval) Ojala	51% at 80% AMI with 4 units at 60%; 5 at 50%; 3 at 30% AMI	Property tax exemption: \$937,227 Sales tax exemption: \$948,760	Single-family modular housing rental development; affordable units spread across bedroom sizes

Dallas Housing Authority

Note: In these conventionally-financed projects, the housing authority is using a public facility corporation, but the PFC serves as the general partner in the entity holding the leasehold interest to the property.

Name of apartment complex	Address	Year PFC partnership approved, type of project, # of units, developer	Income targeting; housing vouchers	Tax Exemptions	Notes
Inwood Station Apartments	2827 Inwood Road; Dallas 75235	2020, acquisition, 347 units Fairfield	50% at 80% AMI; 50% at market; leasing agent said on 7-17-20 that the property doesn't accept vouchers unless Veterans Administration vouchers	Property tax exemption: \$875,431	AMI adjusted for family size in legal docs; but leasing agent said on 7-17-20 that the property doesn't have any affordable units or income restricted units
Tivoli Apartments	18950 Lina Street; Dallas 75287	2019 acquisition, 190 units Fairfield	50% at 80% AMI; 50% at market. Vouchers accepted	Property tax exemption: \$407,225	Acquired from a CHDO; property already had 36 PBVs
Kensley Apartment Homes	4323 North Shore, Irving, 75038	2018; acquisition, 441 units Fairfield	Vouchers accepted	Property tax exemption: \$570,299	Leasing agent said 75% of units are market and 25% are affordable at a range of incomes (30%AMI to 80% AMI)

Other Jurisdictions with Tax-Exempt Conventionally-Financed PFC Projects

Name of apartment complex	Address	Year PFC partnership approved, type of project, # of units, developer	Income targeting; housing vouchers	Tax Exemptions	Notes
Austin Housing Authority: SoCo II	8104 South Congress Avenue, Austin 78745	2019, new construction, 270 units (in development) NRP Group	50% at 80% AMI; 50% at market Not required to accept vouchers	Property tax exemption: \$1,067,504 Sales tax exemption: \$1,113,750	AMI not adjusted for family size; no rent restrictions
Austin Housing Authority: Vega Avenue Apartments	Next to St. Andrews Episcopal School	2002, new construction, 330 units (preliminary approval) NRP Group	50% at 80% AMI; 50% at market	Property tax exemption: \$1,411,920 Sales tax exemption: \$1,361,250	
Huntsville Housing Authority: Huntsville Commons	172 Ravenwood Village Drive, Huntsville 77340	2020, new construction (preliminary approval), 250 units Lynd	50% at 80% AMI; 50% at market	Property tax exemption: \$617,783 Sales tax exemption: \$1,031,250	
Denton Housing Authority: The Enclave at Denton Apartments	1851 Brinker Rd, Denton, TX 76208	2018, new construction (in development), 270 units Integrated Real Estate Group	5% at 60% AMI; 5% at 65% AMI; 40% at 80% AMI; 50% at market	Property tax exemption: \$617,783 Sales tax exemption: \$1,031,250	Unresponsive to requests for information about the project
City of Cibolo: Trophy Oaks Apartments	FM 78 between Red River Ranch and South Main Street, Cibolo, TX 78108	2019, new construction, 324 units NRP Group	50% at 80% AMI; 50% at market; no vouchers required	Property tax exemption: \$1,254,249 Sales tax exemption: \$1,336,500	AMI not adjusted for family size; no rent restrictions
San Marcos Housing Authority: Project name unavailable	N/A	2020, new construction (in negotiation)	N/A	N/A	
City of Boerne: Project name unavailable	N/A	2020, new construction (in negotiation)	N/A	N/A	

Travis County Housing Finance Corporation

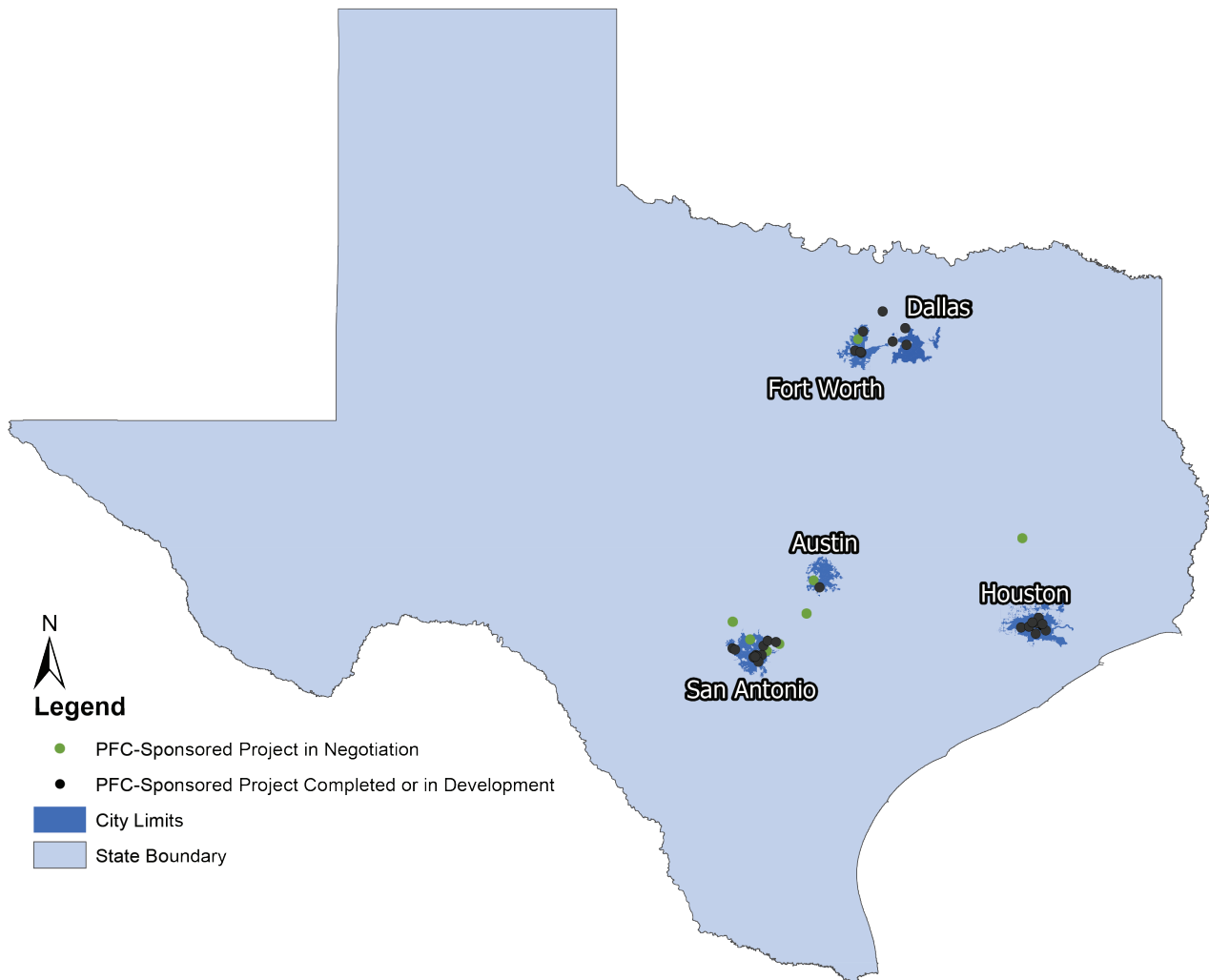
Note: In these conventionally-financed projects, which are eligible for a 100% property tax exemption, the finance corporation did not utilize a public facility corporation and the finance corporation serves as the general partner in the entity holding the leasehold interest to the property.

Name of apartment complex	Address	Year PFC partnership approved, type of project, # of units, developer	Income targeting; housing vouchers	Tax Exemptions	Notes
SOCO Dwell	4401 and 4411 South Congress Avenue, Austin	2019, new construction, 275 units/mixed-use (in development) Cypress Realty	10% at 60: AMI; 35% at 80% AMI; 15% at 90% AMI; 30% at 120% AMI Not required to accept vouchers	Property tax exemption: \$833,856 Sales tax exemption: \$1,124,375	11-year affordability period; PFC has right of refusal at FMV at 11 years; no rent restrictions
Riverside Dwell	6507 E. Riverside Dr., Austin	2019, new construction, 225 units/mixed-use (in development) Cypress Realty	12% at 60%AMI; 48% at 80%; 30% at 120%; 10% market rate Not required to accept vouchers	Property tax exemption: \$1,024,164 Sales tax exemption: \$928,125	11-year affordability period; PFC has right of refusal at FMV at 11 years; no rent restrictions
701 Trinity Street	701 Trinity Street, Austin 78701	2020, new construction, 342 units/mixed-use (preliminary approval) Cielo Property Group	45% at 80% AMI; 45% at 140% AMI; 10% at market	Property tax exemption: \$2,215,111 Sales tax exemption: \$1,410,650	Downtown high rise; 99-year income restrictions

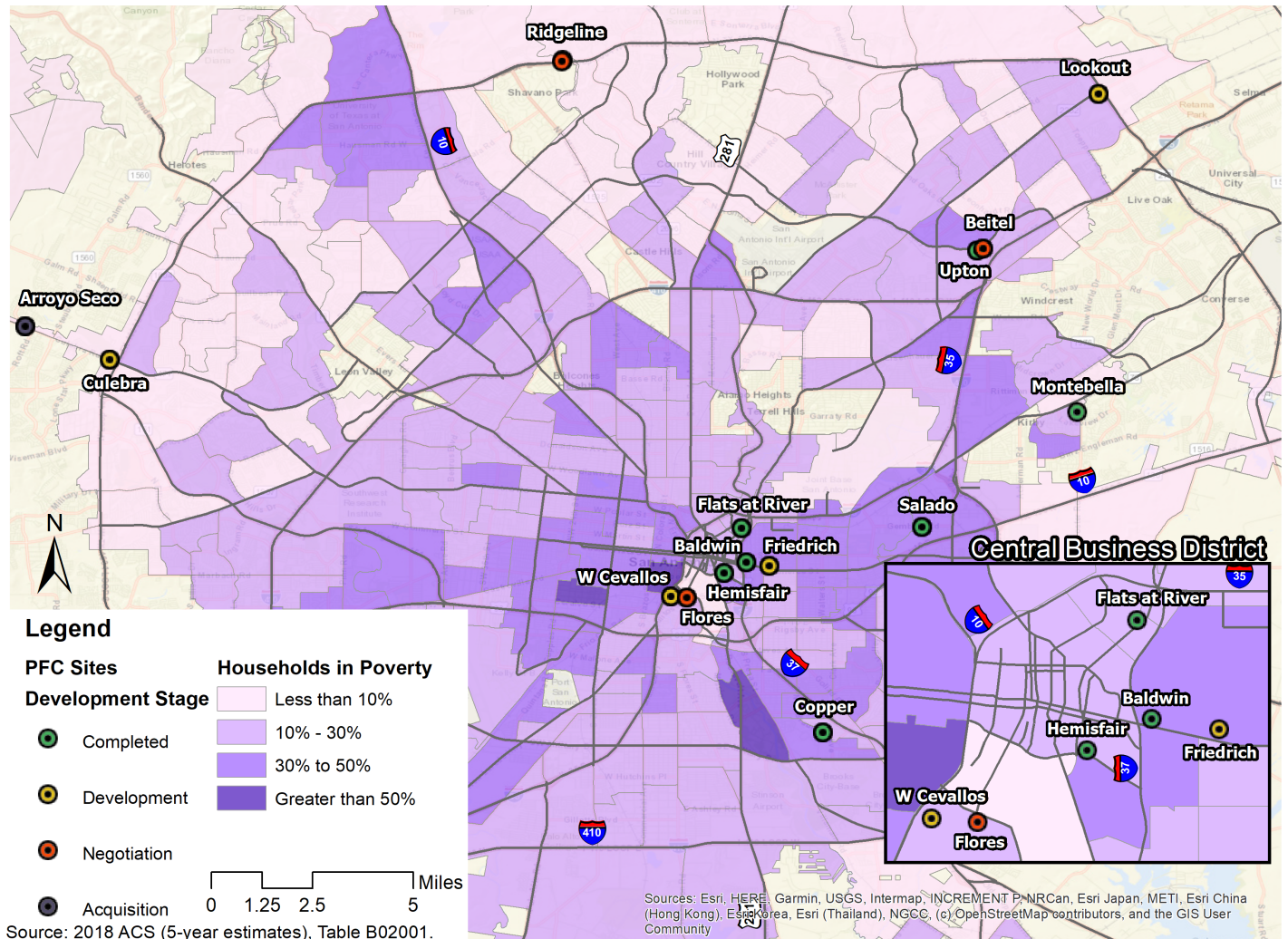
Other local government entities with public facility corporations created since 2015

Abilene Housing Authority	City of Garland	Plano Public Facility Corporation
Bonham Housing Authority	Gladewater Housing Authority	City of Port Aransas
Brazos Valley Council of Governments	Granbury Public Housing Authority	Taft Housing Authority
Ector County	Grandview Public Housing Authority	Texarkana Housing Authority
City of Fate		Uvalde Housing Authority

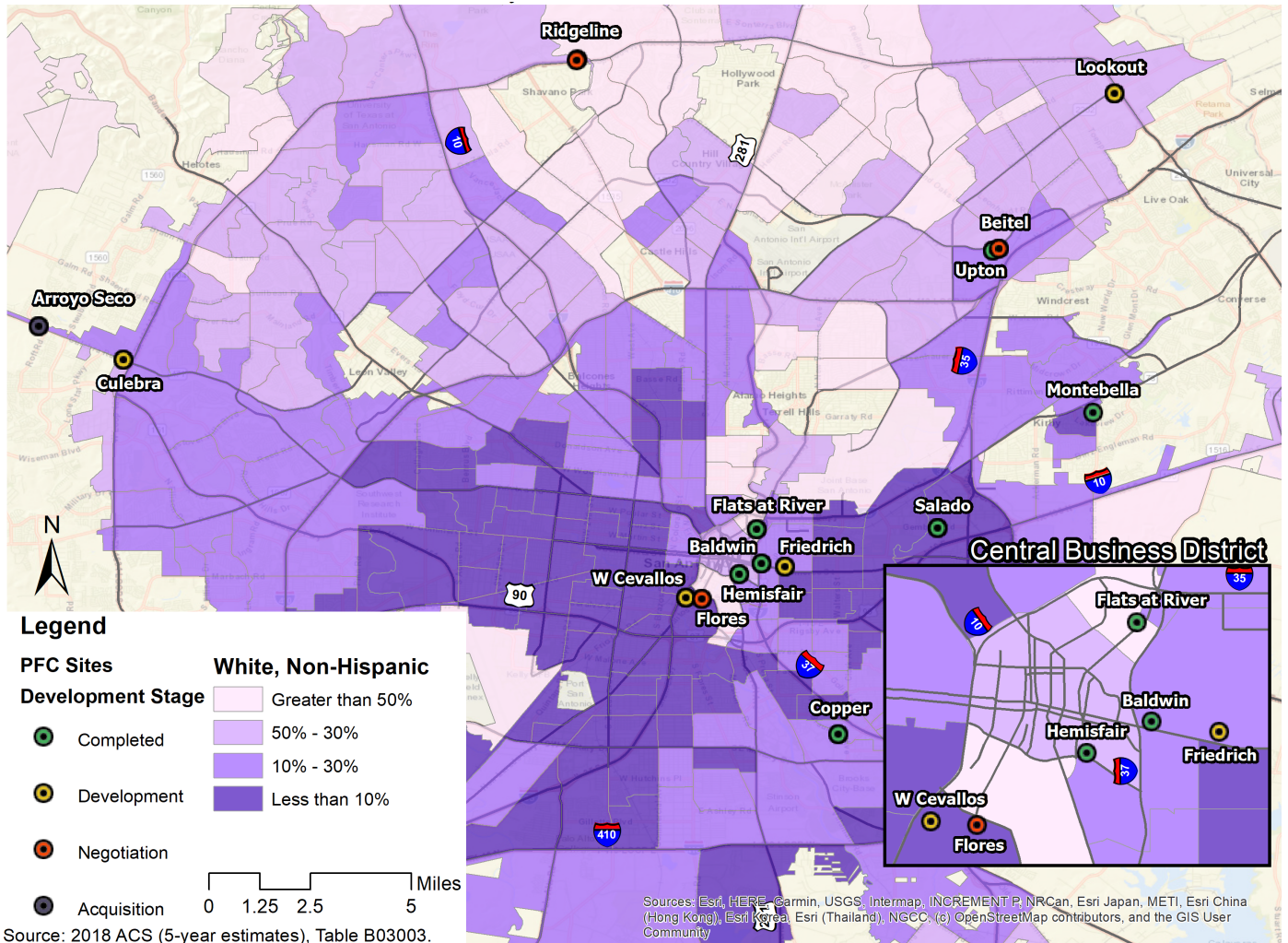
Appendix 3: Location of Tax-Exempt, Conventionally-Financed Apartments Sponsored by PFCs, June 2020



Appendix 4: PFC Site Selection and Percent of Households in Poverty by Census Tract in San Antonio, Texas

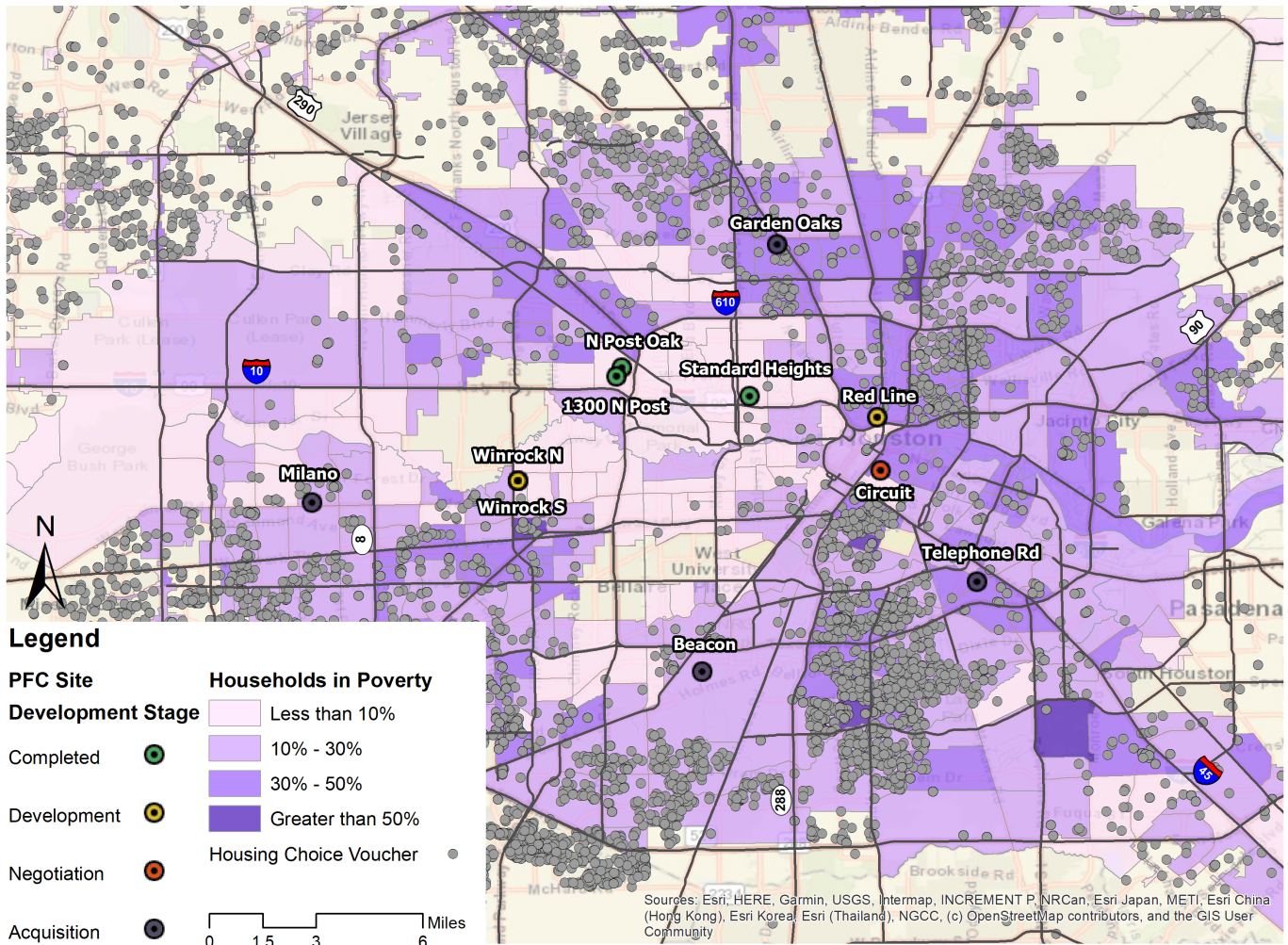


Appendix 5: PFC Site Selection and Percent of White, Non-Hispanic Residents by Census Tract in San Antonio, Texas



Source: 2018 ACS (5-year estimates), Table B03003.

Appendix 6: The Location of Housing Choice Vouchers, PFC Properties, and Percent of Households in Poverty by Census Tract in Houston, TX



Source: Housing Housing Authority (Jan. 2020). 2018 ACS (5-year estimates), Table B03002..

Endnotes

¹Property values for the 30 apartment complexes acquired or newly developed are from the local appraisal district records when available. For properties still under development or without an appraisal district valuation, the property value was estimated based on the average of the replacement and income methods of appraisal. The replacement value is calculated using the appraisal district valuation of comparable properties in the area, and the income method is ascertained from occupancy and rental rate data collected on ApartmentData.com for comparable properties. Both values are averaged and then extrapolated on a per unit basis to the subject property.

²The value of the property tax exemption is calculated using the 2019 property tax rates for the applicable local taxing jurisdictions.

³American Community Survey 2014-2018 (5-year estimate).

⁴American Community Survey 2014-2018 (5-year estimate).

⁵National Low Income Housing Coalition estimates provided to the Texas Law Entrepreneurship and Community Development Clinic, based on tabulation of the 2018 American Community Survey PUMS data.

⁶See, e.g., Christie Moffat, “Important Tool or ‘Poor Public Policy’? Property Tax-Exempt Affordable Housing Structure Under Fire,” Bisnow Houston (May 12, 2020); Peggy Heinkel Wolfe, “New Affordable Housing Project May Not be Affordable for Denton,” Denton Record-Chronicle (July 6, 2018), available at https://dentonrc.com/news/new-affordable-housing-project-mday-not-be-affordable-for-denton/article_44034e6b-43d1-5cd4-ad15-aec61b2624a1.html; Joshua Fechter and Madison Iszler, “A Rudderless Ship,” San Antonio Express-News (Feb. 14, 2020), available at <https://www.expressnews.com/news/local/article/Failings-of-San-Antonio-affordable-housing-trust-15050871.php>.

⁷Texas House of Representatives, Hearing of the Investment and Financial Services Committee (Apr.1, 2015), video recording available at <https://house.texas.gov/video-audio/committee-broadcasts/84/>. The bill comes up at 00:13:15.

⁸Texas Senate Chamber proceeding (May 21, 2015) video recording available at https://tlcsenate.granicus.com/MediaPlayer.php?view_id=30&clip_id=10254. Discussion of the bill begins at 01:18:11.

⁹See, for example, the ground leases for the Milano Apartments (Houston Housing Authority), Section 21.4, and Longhorn Quarry Apartments (San Antonio Housing Trust), Section 22.4.

¹⁰National Association for Latino Community Asset Builders, “An Organizational Assessment and Strategic Recommendations for the San Antonio Housing Trust,” July 2019.

¹¹*Id.*, at 28-29.

¹²*Id.*, at 28-29.

¹³*Id.*

¹⁴*Id.*, at 29.

¹⁵The Houston Housing Authority’s latest RFP can be found under “Development Partners” at <http://www.housingforhouston.com/doing-business-with-hha/current-solicitations.aspx>.

¹⁶Ben Olivo, “NRP Group Expects \$10m Profit from Sale of Tax-Exempt Baldwin Apartments,” San Antonio Hearon (Aug. 28, 2019), available at <https://saheron.com/nrp-group-expects-10m-profit-from-sale-of-tax-exempt-baldwin-apartments/>.

¹⁷This estimate assumes a projected 2.25% annual increase in property taxes. Through the state’s complex school financing laws, exemptions on school district taxes for maintenance and operations (M&O) do not directly impact the district but do impact the state’s overall funding available for public education. In contrast, school districts are directly impacted by exemptions that impact their interest and sinking, or I&S rate, which covers payment of debt service on bonds and pays for things like technology equipment and school buildings.

¹⁸Estimate based on the number of Section 303.042(f) apartment projects approved by PFCs across the state through the end of 2019 together with a projected 25% annual growth in projects approved beginning in 2020 through 2025, with each approved project completed and removed from the tax rolls the following year. The projected property tax exemption value for 2026 assumes a 2.25% annual increase in property taxes that would have been assessed but for the exemption.

¹⁹Estimate based on 2020 appraised values. See endnote 1 for a discussion of how appraised values are calculated.

²⁰Estimate based on 2019 tax rates and 2020 appraised property values. The 2020 tax rates had not been finalized in most local taxing jurisdictions by the time this report was written.

²¹Estimate based on the average I&S rate of Northeast, Judson, Northside, and San Antonio ISDs, which are the schools districts where PFC projects are currently located.

²²Estimate based on the 11 conventionally-financed apartment projects that were approved by PFCs in San Antonio through the end of 2019 and an estimate of four new apartment projects approved each year from 2020 through 2025 (which is the same number of projects approved in 2019). This estimate assumes each approved project is completed and removed from the tax rolls the year after approval, recognizing that some PFC-sponsored projects involve the acquisition of existing apartment complexes whereby the property comes off the tax rolls immediately upon acquisition. In contrast, new construction projects may take longer than a year to be completed. The estimate also assumes a 2.25% annual increase in appraised values with tax rates remaining the same.

²³Estimate based on 2019 tax rates.

²⁴Estimate based on the average I&S rate of Northeast, Judson, Northside, and San Antonio ISDs, which are the schools districts where PFC projects in Bexar County are all currently located.

²⁵Estimate based on 2019 tax rates and 2020 appraised property values. The 2020 tax rates had not been finalized in most local taxing jurisdictions by the time this report was written.

²⁶Estimate based on 2019 tax rates.

²⁷Estimate based on Houston ISD's 2019-2020 I&S tax rate of \$0.1667% for payment of debt service on bonds, out of the school district's total \$1.1367% tax rate.

²⁸Estimate based on the 10 conventionally-financed apartment projects that were approved by PFCs in Houston through the end of 2019 and an estimate of four new apartment projects approved each year from 2020 through 2025 (which is less than the number of projects approved in Houston in 2019). This estimate assumes each approved project is completed and removed from the tax rolls the year after approval, recognizing that some PFC-sponsored projects involve the acquisition of existing apartment complexes whereby the property comes off the tax rolls immediately upon acquisition. In contrast, new construction projects may take longer than a year to be completed. The estimate also assumes a 2.25% annual increase in appraised values with tax rates remaining the same.

²⁹Estimate based on 2019 tax rates.

³⁰Estimate based on Houston ISD's 2019-2020 I&S tax rate of \$0.1667% for payment of debt service on bonds, out of the school district's total \$1.1367% tax rate.

³¹Assumes a 2.25% annual increase in property taxes from 2020 estimates.

³²Based on Austin ISD's I&S tax rate of .123% and San Antonio ISD's I&S tax rate of .4626% for 2019-20. In Texas, for 2018-19, the average I&S rate was .2073% and the highest I&S rate was .7106%. Texas Education Association, "School District adopted I&S tax rates for 2006-19," available at <https://tea.texas.gov/finance-and-grants/state-funding/additional-finance-resources/school-district-property-values-and-tax-rates>.

³³Assumes a 2.25% annual increase in property taxes.

³⁴This is an estimate based on the average I&S rate of Northeast, Judson, Northside, and San Antonio ISDs which are the schools districts where PFC projects in Bexar County are all currently located.

³⁵This is a projection based on estimates of 2020 impacts on public education financing provided the Equity Center. Utilizing current school finance formulas, the Equity Center calculated the impacts on state public education finance in 2020 from PFC-sponsored properties with a Section 303.042(f) tax exemption in Bexar and Harris Counties. For every dollar in M&O tax revenue that is exempted off the tax rolls, the state reimburses the local districts close to \$99.98, with these funds coming out of the state's public education budget.

³⁶The utility allowances used are based on the 12/1/2019 allowances utilized by the Houston Housing Authority and are based on the tenant paying for electric and water services but not sewer. Efficiency = \$86, one-bedroom = \$97, two-bedroom = \$131

³⁷The AMI for the Houston region is based on HUD's 2020 AMI estimate for Houston-The Woodlands-Sugar Land, TX Metro FMR Area. HUD's methodology for the AMI estimate can be found at this link: <https://www.huduser.gov/portal/datasets/il/il2020/2020MedCalc.odn>

³⁸2020 Houston/The Woodlands/Sugar Land Region: HUD Maximum Annual Household Income Limits, available at <https://houstontx.gov/housing/flyers/Area-Median-Income-Chart-2020-Final-071420.pdf>.

³⁹The income and rent limits are based on HUD's 2020 limits for the San Antonio-New Braunfels, TX MSA. The utility allowances used here are based on the allowances utilized by the San Antonio Housing Authority. Efficiency = \$76, one-bedroom = \$95, two-bedroom = \$125.

⁴⁰Congressional Budget Office, "Federal Housing Assistance for Low-Income Households" (Sept. 2015), at 11, available at <http://www.cbo.gov/sites/default/files/114th-congress-2015-2016/reports/50782-lowincomehousing-onecolumn.pdf>.

⁴¹Based on HUD standards whereby the rent charged cannot exceed 30 percent of the annual income of a family whose income equals 80% percent of the area median income. The AMIs used here are based on the Austin-Round Rock, TX and San Antonio-New Braunfels, TX MSAs, with adjustments for family size in accordance with HUD standards. The rents here do not incorporate a utility allowance since none of the PFC-sponsored properties require a utility allowance.

⁴²Data from Apartmentrends.com (April 2020) for the Greater San Antonio and Austin areas.

⁴³City of San Antonio, "HUD Rent and Income Limits" July 1, 2020, available at <https://www.sanantonio.gov/Portals/0/Files/GMA/Resources/FY%202020%20HUD%20Income%20Limits%20w%2012%20updated%207.16.20.pdf?ver=2020-07-16-134709-097>.

⁴⁴City of Austin, “2020 Home and CDBG Program Income Limits by Household Size Effective Date July 1, 2020,” available at [https://www.austintexas.gov/sites/default/files/files/Housing/MFI%20Chart%20Effective%20July%201%202020%20\(002\).pdf](https://www.austintexas.gov/sites/default/files/files/Housing/MFI%20Chart%20Effective%20July%201%202020%20(002).pdf)

⁴⁵Based on HUD’s 2020 Metro Area Adjusted HOME Income Limits for a 2-person household for Austin-Round Rock, TX MSA; Houston-Woodlands-Sugarland MSA; San Antonio-New Braunfels, TX MSA, and Fort Worth-Arlington, TX MSA. The annual income limits were divided by 12 and multiplied by 30% to come up with the monthly affordable rent. For the one-bedroom units here, we used the AMI adjusted for a 2-person household since the PFC deals that adjust for family size assume a one-bedroom unit will be occupied by a 2-person household. The affordable rents here do not incorporate a utility allowance since none of the PFC-sponsored properties require a utility allowance.

⁴⁶Data from Apartmentrends.com, April 2020, for non-subsidized apartment complexes built within the prior ten years within a three-mile radius of the PFC property.

⁴⁷City of San Antonio, “HUD Rent and Income Limits” July 1, 2020, available at <https://www.sanantonio.gov/Portals/0/Files/GMA/Resources/FY%202020%20HUD%20Income%20Limits%20w%20120%20updated%207.16.20.pdf?ver=2020-07-16-134709-097>.

⁴⁸Based on data for the Greater San Antonio Area from Apartmentrends.com, April 2020.

⁴⁹Based on the 2020 appraised value in the Harris County Appraisal District records and 2019 property tax rates since the 2020 rates have not been released yet.

⁵⁰Based on the \$160,000 origination fee that HHA received and estimated annual average cash flow distribution to HHA of \$30,000.

⁵¹Estimated for 2019-2029 based on the property’s 2020 valuation in the Harris County Appraisal District appraisal records, 2019 tax rates, and a projected 2.25% annual increase in property taxes for the years 2021-2029.

⁵²Estimate based on a 2.25% annual increase in property taxes.

⁵³Ben Olivo, “NRP Group expects \$10m profit from sale of tax-exempt Baldwin apartments,” San Antonio Hearon, Aug. 28, 2019, available at <https://saheron.com/nrp-group-expects-10m-profit-from-sale-of-tax-exempt-baldwin-apartments/>; Iris Dimmick, “With Baldwin Apartments Nearly Sold, Housing Corp. Votes to Keep Its Share of Rent,” Rivard Report, Sept. 10, 2019, available at <https://therivardreport.com/with-baldwin-apartments-nearly-sold-housing-corp-votes-to-keep-its-share-of-rent/>.

⁵⁴Estimate based on a 2.25% annual increase in property taxes.

⁵⁵Revenue projections provided by the San Antonio Housing Trust, July 2, 2020.

⁵⁶Based on the property’s 2020 appraised valuation in the Bexar County Appraisal District records and an estimated 2.25% annual increase in property taxes.

⁵⁷Mitchell, Parton, “Crane Watch: Seven Apartment Projects Under Construction to Keep an Eye On,” San Antonio Business Journal, available at <https://www.bizjournals.com/sanantonio/news/2020/02/28/crane-watch-seven-apartment-projects-under.html>.

⁵⁸Texas A&M Real Estate Center, Texas Quarterly Investment Report: 1st Quarter 2020, available at <https://www.recenter.tamu.edu/articles/research-article/TexasQuarterlyApartmentReport-2242>.