

- SUBJECT:** Tax exempt status for community housing development organizations
- COMMITTEE:** Local Government Ways and Means — committee substitute recommended
- VOTE:** 6 ayes — Hill, Laubenberg, McReynolds, Mowery, Puente, Quintanilla
0 nays
1 absent — Hegar
- WITNESSES:** For — Brandon Aghamalian, City of Fort Worth; Monique Allen, Maple Avenue Economic Development Corporation CHDO; Paul D. Charles, Texas Association of CDCs; Stephen Fairfield, Houston Association of Community Development Corporations and Covenant Community Capital; David Mintz, Texas Apartment Association; Walter Moreau, Foundation Communities; Rowan Smith, Texas Affordable Housing Congress; Sandra Williams, Alamo Area MHA; *(On committee substitute:)* Michael Eaton, Texas Affordable Housing Congress; Reymundo Ocanas, Texas Association of CDCs;

Against — *(On committee substitute:)* Robert Parker

On — Rodric E. Fitzgerald, American Opportunity for Housing Inc.; Jim Robinson, Texas Association of Appraisal Districts; *(On committee substitute:)* Wayne Moore, American Housing Foundation
- BACKGROUND:** Tax Code, sec. 11.182(b) allows a nonprofit organization organized as a community housing development organization (CHDO) to be exempt from taxation of property if it meets state charitable organization requirements. The CHDO also must own property on which to build or repair housing to sell or rent to a low-income individual or family meeting the organization's eligibility requirements.
- DIGEST:** CSHB 3546 would prohibit any organization from receiving a CHDO tax exemption for the 2004 tax year unless the organization had received an exemption for the 2003 tax year. CSHB 3546 instead would establish a new framework for granting tax exemptions to eligible low-income housing development projects.

Eligibility. To receive a tax exemption, an owner operating or constructing a low-income housing project would have to be a 501(c)(3) tax exempt non-profit charitable organization as defined under federal and state law. The majority of this organization's board members would have to reside in the state and would have to give notice and respond to advice from low-income households in the project's county about the planning and management of the housing project.

An owner of a housing project that was not included in this category also could be eligible for an exemption if the organization was a limited partnership of which a tax exempt non-profit charitable organization controlled all of the general partner interest. An owner also could be eligible if it was an entity of a parent organization that was a tax exempt non-profit charitable organization. If the owner fell into one of these two categories, the entity would have to be organized under Texas law and principally do business in Texas. The property could be exempt if it was under active construction or preparation for construction, but an organization could not receive an exemption if construction was completed before the bill's effective date.

Resident income requirements. For a property to receive a tax exemption it would have to rent housing to individuals and families whose median incomes were not more than 60 percent of the greater of either the area or statewide median family income, adjusted for size. A property also could receive an exemption if it sold single-family dwellings to individuals and families whose incomes were not more than 100 percent of the area or state median family income, whichever was higher.

Property use and rent requirements. Property could not be exempt unless at least 50 percent of the total square footage of dwelling units in the development was reserved for low-income individuals. The bill would allow units rented to public school employees, county or city peace officers, active duty military, honorably discharged veterans, or persons over the age of 65 to count toward the required area occupied by low-income inhabitants. The annual total of monthly rent charged for each dwelling reserved for a low-income family or individual could not exceed 30 percent of the area median family income, adjusted for family size. An organization would have to rent

the required amount of space to eligible low-income individuals within three years of the date the organization purchased the property.

Rehabilitation of property. If property was owned for the purpose of rehabilitation, it would be required that original construction of the project had been completed at least 10 years before the date that rehabilitation began. If an organization was not the original owner of a project, it would be required that the person from whom the organization bought the project had owned it for at least five years. Further, the organization would have to provide documentation from the chief appraiser or bond issuer stating that the organization had spent at least \$5,000 or the amount required by the financial lender on each dwelling unit, whichever amount was higher.

An organization rehabilitating a property also would be required to maintain an annual reserve fund for replacements for each unit in the amount required by the financial lender or \$300. Starting with the 2005 tax year, this required reserve would increase by an annual cost-of-living adjustment. Withdrawals from the reserve would have to be authorized by the financial lender or only to pay the costs of capital improvements with a depreciable value of at least five years needed to maintain habitability according to standards set by the U.S. Department of Housing and Urban Development (HUD) or the city or county.

Property appraisal. In determining the rental income for tax exempt property, the chief appraiser would have to consider restrictions placed on residents' income and the amount of rent that could be charged to these low-income residents. The appraiser would use the same capitalization rate used for other rent-restricted properties. The district would have to give public notice of the capitalization rate used to appraise exempt property.

Tax exemptions. In a school district, an eligible property's tax exemption would be 50 percent of the appraised value, multiplied by the square footage of the dwelling units reserved for low-income individuals, divided by the total square footage of dwelling units in the project.

In a taxing unit other than a school district, the tax exemption for a property with at least 75 percent of its square footage reserved for eligible low-income individuals or families would be 75 percent of the appraised value, multiplied

by the square footage of the dwelling units reserved for low-income individuals, divided by the total square footage of dwelling units in the project.

For a project in a taxing unit other than a school district with between 50 and 75 percent of units reserved for eligible low-income families, the tax exemption would be 65 percent of the appraised value, multiplied by the square footage of the dwelling units reserved for low-income individuals, divided by the total square footage of dwelling units in the project.

An exemption would not terminate due to a change in property ownership if the property was bought by an eligible organization.

Opt-out provision. The governing body of a taxing unit located in part or in whole of a county with a population over 1.4 million could require an organization to obtain approval for a tax exemption. An organization would have to submit a request for approval of the exemption to the taxing unit's governing body, and the governing body could approve or modify the organization's exemption. Further, the governing body could deny the exemption if the taxing unit could not afford the revenue loss from the exemption or if there was no need for additional low-income housing in the taxing unit's territory. The governing body could charge the organization a fee for administrative costs associated with the processing the request.

Monitoring and evaluation. CSHB 3546 would require a tax exempt housing organization to have an audit prepared each fiscal year including the auditor's opinion on whether the organization's statements fairly presented the organization's financial position and whether the organization had complied with eligibility requirements. The audit would have to be presented to the Texas Department of Housing and Community Affairs (TDHCA) and the appraisal district's chief appraiser. If the property contained 36 or fewer units, a detailed report and certification could be presented instead.

Continuing existing appraisal methods. CSHB 3546 would allow certain property renting to low or moderate income individuals or families at the time of the bill's effective date to continue to be appraised using an income-method of appraisal taking into account restrictions on residents' income and using the same capitalization rate for other rent-restricted properties. These

properties that would be required to have been financed under TDHCA's Low Income Housing Tax Credit Program, could not receive an exemption under this bill, and the owner could not have entered into an agreement with any taxing unit to make payments to the unit instead of taxes on the property.

This bill would take immediate effect if finally passed by a two-thirds record vote of the membership of each house. Otherwise, it would take effect September 1, 2003.

**SUPPORTERS
SAY:**

By redefining and clarifying the role of CHDOs in the state, CSHB 3546 would address many of the difficulties posed by these organizations in many communities while ensuring accessibility of low-income housing across the state. The bill would eliminate the old, lenient CHDO statute that led to millions of dollars in tax exemptions for housing projects that have strained local school districts, counties, and cities. CSHB 3546 would clarify precisely the organizations eligible for tax exemption and establish auditing procedures to ensure that these organizations met their obligations. The bill rationally would balance the need to encourage affordable housing for low-income Texans with a consideration of the needs of all taxing units in Texas.

While current law grants too much leniency to a CHDO regarding the use of a low income housing property, CSHB 3546 would establish needed criteria to standardize the role of CHDOs in Texas counties. The bill would require that an eligible property rented at least half of its space to families with less than 60 percent of the median family income, or sold to families with incomes less than 100 percent of the median family income.

The bill would encourage CHDOs to provide housing to valued citizens such as teachers, peace officers, military personnel, and senior citizens, by providing the organizations with credit toward the number of low-income units they must have for an exemption.

CSHB 3546 would ensure that CHDOs provided an acceptable level of habitability to residents, by requiring a CHDO to retain \$300 per unit for repair and replacement. Further, for a renovated property to be tax exempt, the CHDO would have to spend at least \$5,000 per rehabilitated unit.

CSHB 3546 would allow a governing body in Harris, Tarrant, and Dallas

county to opt-out of any CHDO tax exemption on a case-by-case basis if there was no need for additional affordable housing or if taxing entities could not afford an exemption. In those areas, the median income is so high that the market rate is already at or below 60 percent of median family income, and without the opt-out clause, virtually all of the units in these communities would be tax exempt. This is not the case in many rural and border communities, and CSHB 3546 appropriately would balance conflicts between CHDO abuse in the largest cities and the need for affordable housing across the rest of the state.

**OPPONENTS
SAY:**

By tightening eligibility requirements and reducing the tax exemption for affordable housing providers, CSHB 3546 would hurt the availability of affordable housing in Texas. The affordable housing industry relies upon public support for the important service it provides, and Texas has chosen to use tax exemptions rather than direct appropriation to address affordable housing. These nonprofit housing providers operate with limited resources, and restricting and reducing tax exemptions could lead new housing providers to charge higher rents or avoid developing projects entirely.

By increasing the number of units that would have to be affordable in a housing project, CSHB 3546 could reinforce some of the problems often associated with affordable housing projects. For reasons of social cohesion, HUD recommends tiering housing projects among low, moderate, and market-rate units, and this bill would not adequately consider this recommendation.

**OTHER
OPPONENTS
SAY:**

Tax revenues have been decreased by CHDOs in many more counties than the three eligible for the opt-out provision in CSHB 3456. The bill should allow any municipality in the state to opt out of transactions and determine if a need for affordable housing existed or if tax exemptions could be afforded.

NOTES:

The committee substitute to HB 3546 made numerous to the original, which include:

- allowing an organization to work under a limited partnership or parent organization.
- removing anti-nepotism and other regulations for an eligible organization and its board of directors;

- allowing certain groups, such as teachers and peace officers, to qualify for low-income units;
- defining requirements on income, residency, and amount of space rented to low-income inhabitants;
- requiring that rent in low-income units not exceed 30 percent of median area income;
- authorizing the opt-out provision for certain large counties;
- including the \$5,000 expense requirement on rehabilitated properties; and
- allowing organizations receiving an exemption under TDHCA's Low Income Housing Tax Credit Program to continue with this appraisal method.