City of Denton

City Hall
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AGENDA INFORMATION SHEET

DEPARTMENT: **City Manager's Office**

CM/DCM/ACM: **Christine Taylor**

DATE: **March 19, 2024**

SUBJECT

Receive a report, hold a discussion, and give staff direction regarding creating Public Facility Corporations to develop affordable housing in the City of Denton, including a comprehensive analysis of the definition, creation, and administration of Public Facility Corporations.

STRATEGIC ALIGNMENT

This action supports Key Focus Area: Foster Economic Opportunity and Affordability.

BACKGROUND

On November 14, 2023, Council Member Watts made a two-minute pitch request and received support for work session to discuss the City creating Public Facility Corporations to develop affordable housing in the City of Denton, including a comprehensive analysis of the definition, creation, and administration of Public Facility Corporations. (ID 23-227).

Staff will present information on Public Facility Corporations (PFC) authorized by Chapter 303 of the Texas Local Government Code – the Public Facility Corporation Act (Act). The presentation will focus on the definition, creation, and administration of Public Facility Corporations.

Additionally, staff is providing the requested comprehensive analysis of the Local Government Code Title 9, Subtitle C, Chapter 303 and recent changes made to Chapter 303 and Chapter 392 in H.B 2071 authorized during the 88th Legislative Session that will be effective January 1, 2024 as well as an overview of the steps required in setting up a PFC.

A **PUBLIC FACILITY CORPORATION (PFC)** is a corporation created by a local government entity to hold title to and provide funding for any real, personal, or mixed property, or an interest in property devoted to public use.

- It is authorized by Chapter 303 of the Texas Local Government Code – the Public Facility Corporation Act (Act)
- It is a **nonprofit** corporation created through Texas Secretary of State

A sponsor (municipality, county, school district or housing authority) may create one or more of the nonprofit public facility corporations to acquire, construct, rehabilitate, renovate, repair, equip, furnish, or place in service public facilities such as affordable housing developments.

A sponsor could use the PFC to:

- Issue bonds
- Finance public facilities
- Loan the proceeds of the obligations to other entities

The public benefit of a PFC

- **Incentivizes creation** of affordable housing toward City's Affordable Housing Strategic Toolkit and Affirmatively Furthers Fair Housing goals.
- Provides the opportunity to **generate revenue** with unrestricted proceeds available for a public purpose such as to
    - offset some portion tax exemption;
    - fund City's Affordable Housing Strategies;
    - grant funds to public assistance programs; and/or
    - fund future public projects.
- PFC has **negotiating power** over affordability, revenue, and Council priorities such as:
    - Requiring deeper affordability than the minimum required in PFC program.
    - Negotiating revenues from the operation and/or sale of the development.
    - Enhancing protection for renters such as requiring income qualified rent restrictions, etc.

Comprehensive Analysis of the Local Government Code Title 9, Subtitle C, Chapter 303

The Local Government Code Title 9, Subtitle C, Chapter 303, known as the Public Facility Corporation Act, pertains to public facility corporations (PFCs) in Texas. These entities are designed to assist in financing public facilities. Here's a comprehensive analysis of its key provisions:

1. **Purpose and Creation of PFCs (Sec. 303.001 - 303.003):** This section introduces the Act, stating its purpose to authorize PFCs with broad powers for financing public facilities at low borrowing costs. It defines critical terms like "corporation," "bonds," and "public facility."

2. **Constitutional Safeguards (Sec. 303.004):** In case of constitutional conflicts, an alternative procedure can be adopted.

3. **Relation with Other Laws (Sec. 303.005):** This clarifies the chapter's interaction with other laws, ensuring it doesn't limit existing state or municipal powers over property of a corporation.

4. **Limitations (Sec. 303.006):** It stipulates what the chapter does not authorize, like mortgage of public facilities.

5. **Natural Gas Provision (Sec. 303.007):** Includes natural gas under the scope of public facilities.

6. **Formation and Operation (Sec. 303.021 - 303.047):** These sections detail the process of creating a PFC, its governance, powers, and administrative aspects. It covers topics like articles of incorporation, board and officer roles, and open meeting requirements.

7. **Bond Issuance and Management (Subchapter C, Sec. 303.071 - 303.078):** Focuses on the rules regarding the issuance, sale, and management of bonds by PFCs, including refunding obligations and the use of proceeds.

8. **Dissolution of Corporation (Subchapter D, Sec. 303.101 - 303.106):** Addresses the dissolution process for PFCs, including how assets are handled and the continuation of legal rights and claims.

9. **Administration by Secretary of State (Subchapter E, Sec. 303.121 - 303.124):** Outlines the role of the Secretary of State in administering the chapter, including fee collection and document handling.

10. **Amendments (Various Sec.):** Several sections have amendments, reflecting legislative updates over time to accommodate evolving needs and circumstances.

The Act's primary goal is to facilitate the efficient and cost-effective development of public facilities by leveraging the powers and flexibility of PFCs. It outlines a detailed legal framework for the creation, operation, and dissolution of these corporations, ensuring transparency, accountability, and compliance with broader governmental objectives.

H.B 2071

House Bill No. 2071 is legislation that amends the Local Government Code, particularly Chapter 303, focusing on public facilities used to provide affordable housing. The bill introduces several key changes and additions, which are summarized in the following sections.

1. **Amendments to Section 303.021:** This section is amended to allow corporations or sponsors to finance, own, or operate multifamily residential developments only if they comply with all applicable provisions of the chapter. Additionally, the developments must be located within the area of operation of the sponsor if the sponsor is a housing authority, or within the boundaries of the sponsor if it is not a housing authority.

2. **Conflict of Interest Laws (Section 303.0415):** It establishes that members of the board of a corporation or a member of the governing body of a sponsor are subject to the same conflict of interest restrictions as local public officials under Chapter 171.

3. **Taxation and Exemption (Sections 303.042 and 303.0421):** These sections address the taxation and exemption statuses of multifamily residential developments owned by public facility corporations. Notably, the exemption under Section 303.042(c) for such developments is subject to specific conditions, such as compliance with Section 303.0421(h).

4. **Additional Requirements for Beneficial Tax Treatment (Section 303.0425):** This section outlines additional requirements related to beneficial tax treatment for certain public facilities. It

defines terms like "developer" and "public facility user" and sets specific criteria for lower and moderate-income housing units, rent charges, and tenant income calculations.

5. **Audit Requirements (Section 303.0426):** This section mandates annual audit reports for compliance from public facility users of multifamily residential developments claiming exemptions under Section 303.042(c). It details the auditing process, reporting standards, and consequences for noncompliance.

6. **Study of Tax Exemptions (Section 303.0427):** The Legislative Budget Board is required to conduct a study assessing the long-term effects on the state's funding and revenue due to ad valorem tax exemptions and sales and use tax exemptions for multifamily housing developments.

7. **Amendments to Section 392.005:** This section undergoes changes related to exemptions for multifamily residential developments owned by public facility corporations created by housing authorities.

8. **Effective Dates and Transitional Provisions:** The Act specifies the effective dates of various sections and outlines transitional provisions for developments approved or acquired before the effective date of the Act.

9. **Implementation Rules:** The Texas Department of Housing and Community Affairs is directed to adopt rules necessary to implement Section 303.0426 by January 1, 2024.

Overall, H.B. No. 2071 aims to regulate and provide a framework for the operation and taxation of multifamily residential developments, especially those aimed at providing affordable housing, while also ensuring compliance and oversight through audits and studies. Staff previously provided more targeted analysis of the changes in H.B. No. 2071 and the impact on PFCs and affordable housing specific to areas of affordability, transparency, jurisdictional issues, and tenant protections.

- **Affordability**
  - Requires 10% of units to be affordable for renters at 60% of area median income (AMI) in addition to 40% of units affordable at 80% AMI. PFC is still 100% Tax-exemption for 50% affordable units. PFC developments are still not required to reserve any units for renters earning 50% AMI or below.
  - Acquisition deals (versus new construction) must dedicate at least 15% of the cost of the property for rehab. Acquisitions may avoid the rehab requirement by increasing the share of units affordable at 60% AMI to 25%, only with approval by the elected body over the PFC.
  - Income-restricted units must make up a proportionate share of each unit size.

- **Transparency**
  - For new construction deals, the PFC user must show that the development would not be feasible without the use of the PFC structure.
  - For acquisition deals only, a “meaningful benefit test” is required that shows that 60% of tax benefit is going toward reducing rents in income-restricted units. Not required for new construction deals.

- For PFCs operating under a Public Housing Authority (PHA) that do not have a majority of the members of the governing body who are elected officials, the PFC must obtain approval the elected body of the municipality (City Council) over the PHA.
- A PFC must post information about each AHP it owns on its website.
- For all deals, a 30-day notice must be given to all impacted taxing entities.
- An annual compliance audit conducted by auditors hired by property owners is required and must be reviewed by TDHCA. Audits are only reviewed not conducted by TDHCA.
- The Legislative Budget Board will conduct a one-time study to assess the fiscal impacts of PFC's on property taxes.

- **Jurisdiction**
  - PFC deals may only occur within the jurisdictional boundaries of the PFC sponsor.
  - Tax-Exemptions Expire (unless extended with approval from same entities of initial approval):
    - Acquisition: Expires after 30 years
    - New Construction: Expires after 60 years

- **Tenant Protections**
  - Requires that PFC developments must accept Housing Choice Vouchers (HCV) and cannot require HCV holders to have monthly income in excess of 250% of the household's income.
  - The PFC user must affirmatively market to voucher holders.
  - Provides a baseline of tenant protections, including preventing retaliation regarding the right to organize and just cause eviction protection.

Creation of a PFC

The steps to creating a PFC involve:

Step 1: Preparing Bylaws and Certificate of Formation
Step 2: City Council Approval
Step 3: Submission to the Secretary of State
Step 4: File for Franchise Tax Exemption and EIN
Step 5: Organizational Meeting

Administration of a PFC

The administration of a PFC would involve:

- Complete PFC Formation
- Submission to Secretary of State and approval.
- Organizing Meeting: Initial Board of Directors Orientation, Articles, By-laws, Establish Key Priorities and Define Role in Deal Structures.
- Inform Development Community of PFC Program and Application Process
- Operation
- Receive and Review Applications to ensure that the project would only be feasible with a property tax exemption and the project is alignment with the City's affordable housing goals
- Board sets Terms and Negotiates Agreements to the maximum public benefit.

Key Points of Negotiation to Deliver Meaningful Public Benefit using a PFC

- Negotiate the partnership type that the PFC would be a member of the partnership.
- Negotiate the affordability level of the residential units and the period of affordability (including a mix of income levels).
- Negotiate revenue to the PFC which may include the following:
  - Acquisition Fee – A one time fee paid at closing.
  - Annual Revenue – A percentage of net cash flow or a lease payment.
  - Sale/Refinance Proceeds – The PFC should receive a percentage of proceeds.
- The Partnership should reimburse the PFC/City for incurred expenses:
  - Administrative
  - Legal
  - Owner Representation

Next Steps To Approve PFC

There are two actions necessary to complete the formation of the PFC.

1. Approval of the Resolution by City Council accepting the formation documents and approving submissions to the Secretary of State and necessary filings required to form the PFC.
2. Appoint the initial board members to the PFC to complete the bylaws.

OPTIONS

- Direct staff to create a development program authorizing the formation of Public Facility Corporations for future affordable housing projects
- Take no further action regarding the formation of Public Facility Corporations

PRIOR ACTION/REVIEW (Council, Boards, Commissions)

- June 28, 2022: Council Member Watts made a two-minute pitch request and received support for work session to discuss the City creating Public Facility Corporations to partner with developers to develop affordable housing in Denton (ID 22-420).
- October 25, 2022: Council provided direction to staff to create a development program authorizing the formation of Public Facility Corporations for future affordable housing projects (ID 22-1453)
- May 2, 2023: Council did not provide approval to proceed with creating a Public Facility Corporation program. (ID 23-865)

EXHIBITS

1. Agenda Information Sheet
2. Presentation

Respectfully submitted:
Dani Shaw
Director of Community Services